Order Code RL30371

Serbia and Montenegro: Current Situation and U.S. Policy

Updated January 11, 2006

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Summary

Serbian strongman Slobodan Milosevic's long reign came to an end in October 2000, when he was deposed from power by a popular revolt after he refused to concede defeat in an election for the post of President of the Federal Republic of Yugoslavia (FRY) won by his opponent, Vojislav Kostunica. Although it achieved some successes, the new democratic government was beset with internal conflicts almost from its beginning, including over cooperation with the Yugoslav war crimes tribunal. It received its greatest blow in March 2003, when Serbian Prime Minister Zoran Djindjic was murdered by organized crime figures linked to the Serbian security apparatus. Organized crime, extremists within the Serbian military and security apparatus, and the links between them continue to pose a threat to Serbia's democratic development.

On December 28, 2003, the extreme nationalist Serbian Radical Party won a stunning victory in early Serbian parliamentary elections, but fell short of a majority. In March 2004, a minority government of democratic parties formed a government without the Radicals. However, the government depends on the parliamentary support of Milosevic's Socialists, who are not in the government but are in a position to extract concessions from it. Democratic forces in Serbia received a boost from Serbian presidential elections in June 2004, which resulted in a victory for Boris Tadic, a pro-Western, pro-reform figure over a Radical Party candidate.

In a years-long confrontation with Milosevic, Montenegrin leader Milo Djukanovic seized control of virtually all levers of federal power on the republic's territory. He sought to rapidly achieve an independent Montenegro, but opposition from the United States, European Union and Russia stymied these efforts. In 2003, under heavy EU pressure, Serbia and Montenegro formed a loose union of two republics. Montenegro agreed to put off plans for independence for at least three years. Montenegrin officials say that they plan to call an independence referendum in April 2006.

The United States and other Western countries have sought to encourage Serbia and Montenegro's integration into Euro-Atlantic institutions. However, these efforts have been hampered by controversy over the future status of Serbia's Kosovo province, Serbia's failure to fully cooperate with the Yugoslavia war crimes tribunal, and Serbia's fitful progress in reforms, particularly in such areas as rule of law and military and security sector reform.

Since Milosevic's downfall, Congress has appropriated significant amounts of aid to Serbia and Montenegro to promote reforms. In each fiscal year from FY2001 to FY2006, Congress conditioned U.S. aid to Serbia on a certification by the President that a series of conditions had been met by Serbia, above all cooperation with the Yugoslav war crimes tribunal. The second session of the 109th Congress may consider similar certification provisions in the FY2007 foreign aid bill. This report will be updated as events warrant.

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Political Background

Despite defeats in wars in Croatia, Bosnia and Kosovo, international isolation and the impoverishment of his people, Serbian strongman Slobodan Milosevic remained in power for more than a decade. He did this by maintaining tight control over key institutions (such as the police, army, judiciary and most of the media) as well as much of the economy. He retained a reservoir of support among some sectors of the population, such as the elderly and those living in rural areas, in part by appealing to Serbian nationalism. He also played skillfully on weaknesses and divisions in Serbia's opposition. His reign came to an end on October 5, 2000, when he was deposed from power by a popular revolt after he refused to concede defeat in an election for the post of President of the Federal Republic of Yugoslavia (FRY) won by his opponent, Vojislav Kostunica on September 24, 2000.[1] Milosevic's party, the Socialist Party of Serbia (SPS) was also trounced in simultaneous elections to the federal parliament and local governments.

Serbia and Montenegro at a Glance

In February 2003, the Federal Republic of Yugoslavia (FRY) was replaced by a loose union of the FRY's two republics, now simply called "Serbia and Montenegro." Each republic has its own president, parliament and government, which are responsible for most government functions on its territory. (Before Milosevic's rise to power, Serbia had two autonomous provinces on its territory, Vojvodina and Kosovo, but Milosevic eliminated many of their powers. Currently Vojvodina retains some elements of autonomy and Kosovo is under U.N. administration.) The functions of new joint governing bodies are limited largely to foreign policy and defense.

Area: 102,173 sq. km. (slightly smaller than Kentucky), of which Serbia (including Kosovo) 88, 361 sq. km., and Montenegro 13,812 sq. km.

Population: 10.39 million (1991 census), of which Serbia 7.82 million (excluding Kosovo), Montenegro 0.62 million, and Kosovo 1.96 million (est.).

Source: The Statesman's Yearbook 2001.

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[1] For detailed accounts of the events leading up to Milosevic's fall, see Steven Erlanger and Roger Cohen, "How Yugoslavia Won its Fight For Freedom," *New York Times*, October 15, 2000, 1; and R. Jeffrey Smith, "How Milosevic Lost His Grip," *Washington Post*, October 14, 2000, 1.

The victor in the election was a coalition of often-feuding opposition parties called the Democratic Opposition of Serbia (DOS). The DOS agreed on a joint slate of candidates for the federal parliament and local elections. They named Vojislav Kostunica as their joint candidate to run against Milosevic for the federal Presidency. Kostunica's main advantages, according to many observers, were a reputation for honesty and his long-standing, unwavering opposition to Milosevic. Kostunica, a former law professor, sharply criticized the Milosevic regime's cynical manipulation of the law and legal system, as well as the often lawless behavior of those close to the regime. He emphasized the need for the rule of law in Serbia, similar to that practiced in other European countries and the United States. Kostunica holds strongly nationalist views. He has been a fierce critic of United States and NATO policy in Kosovo and Bosnia. This may also have made him popular with many Serbs. After their victory in federal and local levels, the DOS swept to further victories in elections for the Serbian parliament on December 23, 2000. On January 25, 2001, the parliament approved a DOS government led by Prime Minister Zoran Djindjic.

However, soon after the DOS took power, tensions arose between supporters of FRY President Kostunica and Serbian Prime Minister Djindjic. These conflicts slowed reforms and disillusioned many Serbs, who once had high hopes that Milosevic's overthrow would lead to a dramatic improvement in their living standards. One key subject of dispute was cooperation with the International Criminal Tribunal for the former Yugoslavia (ICTY). On June 28, 2001, the Serbian government transferred Milosevic to the ICTY to face war crimes charges. Serbian Prime Minister Zoran Djindjic defended the transfer of Slobodan Milosevic and other indictees, saying they were needed so that the FRY could receive vitally-needed international aid. Kostunica condemned the transfer of Milosevic as illegal and claimed that he had not been informed of the move beforehand. The DSS left the Serbian government in August 2001.

The DOS government received another blow on March 12, 2003, when Djindjic was assassinated by two gunmen as he got out of his car in front of the Serbian cabinet office. Serbian police soon learned that organized crime figures linked to the Serbian security apparatus were responsible for Djindjic's murder. One of Djindjic's accused assassins, now in custody, was a senior officer of the Special Operations Unit (JSO). The JSO conducted highly sensitive operations for the Milosevic regime, reportedly including war crimes in Bosnia and Kosovo. Djindjic allowed it to continue operating after Milosevic's fall because its leader, Col. Milorad Lukovic (known as "Legija"), had provided support to the democrats during the anti-Milosevic uprising. The gunman told interrogators that he killed Djindjic after Legija (who had since retired and become the head of the powerful Zemun organized crime gang) told him Djindjic was planning to dissolve the JSO and send its members to the International Criminal Tribunal for the Former Yugoslavia (ICTY) for war crimes trials. Other sources say that the assassination was motivated primarily by fears of a crackdown on organized crime. Organized crime, extremists within the Serbian military and security apparatus, and the links between them continue to post a threat to Serbia's democratic development and Euro-Atlantic integration.

Current Political Situation in Serbia

The increasingly instability of the ruling DOS coalition led the Serbian government to call early parliamentary elections on December 28, 2003. The results reflected public disillusionment with the performance of the previous government and resurgent nationalism in Serbia. By far the largest party in the 250-seat parliament is the Serbian Radical Party, which won 82 seats. Milosevic's Socialist Party of Serbia won 22 seats. Democratically-oriented parties won the remaining seats. Kostunica's Democratic Party of Serbia (DSS) won 53 seats, the Democratic Party won 37 seats, and the G-17 Plus party won 34 seats. The monarchist and moderate nationalist Serbian Renewal Movement, in coalition with the New Serbia party, won 22 seats.

Kostunica assembled a minority government of democratic parties, consisting of the DSS, G17 Plus, and the SPO/NS. The DSS received the interior and justice ministry posts, which are key in the fight against organized crime and corruption. G17 Plus plays an important role in economic affairs. The parliament approved the new Serbian government on March 3, 2004. There were also changes in the joint Serbia and Montenegro government. The Foreign Minister is Vuk Draskovic, leader of the SPO.

The most controversial aspect of the Serbian government is its dependence on support from the SPS, which does not have ministers in the government but provides it with a majority in parliament. In justifying his overtures to the Socialists, Kostunica asserted that they have reformed themselves since they were in power under Milosevic, a claim that many analysts would dispute. Critics have charged that the government has had to make concessions to the Socialists on several issues in order to remain in power.

On June 13, 2004, Serbia held a presidential election. Although the Serbian presidency is not a powerful post, analysts viewed the election as a key indication of Serbia's democratic development and orientation toward Euro-Atlantic institutions. A victory for the candidate of the extreme nationalist Radical Party, Tomislav Nikolic, would have been viewed as a serious setback for Serbia's path toward integration with Western institutions. Nikolic was opposed by Democratic Party leader Boris Tadic and Dragan Marsicanin of the DSS. In the first round of the vote, Nikolic won 30.6% of the vote. Tadic took second place with 27.37%. In a surprise result, wealthy businessman Dragoljub Karic won 18.23%. Karic, a prominent business figure in the Milosevic era, ran on a populist program. In a blow to the DSS and the government, their candidate, Dragan Marsicanin, received a mere 13.3% of the vote. In the June 27 runoff between the two top first-round finishers, Tadic beat Nikolic 53.53% to 45.1%. Tadic's victory was greeted with relief by Western governments. These results confirmed the growing strength of Tadic's pro-Western Democratic Party but also continued strong support for the Radicals.

In October 2005, the DS began a boycott of the Serbian parliament, after a scandal involving the defection of two DS deputies to the DSS. Tadic is seeking the dissolution of the current government and the holding of new parliamentary elections as soon as possible. (The parliament's full term would otherwise expire in late 2007.)

The current government is weak but continues to hang on, partly because several parties are likely to lose all of their seats in parliament when new elections are held. The weakness of the current government also appears to suit the Radicals and Socialists, who have not yet sought to overturn it. However, events in the next year may destabilize the government. These could include a Kosovo settlement perceived to be unfavorable to Serbia; Montenegro's independence; the transfer of indicted war criminal Ratko Mladic to the International Criminal Tribunal for the Former Yugoslavia; an economic downturn; or scandals over privatization or other issues.

Experts disagree on their predictions for the outcome of possible early elections. According to public opinion polls, the Radicals remain the most popular single party in Serbia. However, they may not be able to form a majority on their own or with the Socialists, who may lose all of their seats in the parliament. On the other hand, a nationalist backlash over Kosovo or other issues could put the Radicals over the top. Another option could be for them to strike a deal with the DSS or a new populist party lead by tycoon Bogoljub Karic. The international community would likely strongly disapprove of the participation of the Radicals in a Serbian government. An alternative could be for the DS, DSS, and other democratic parties to form a government, but continuing animosities among their leaders could make this difficult.

Major Political Parties and Groups in Serbia

Democratic Party (DS): The DS was the largest party in the 2001-2003 democratic coalition government. It established a reputation for pro-Western pragmatism under its former leader, Prime Minister Zoran Djindjic. This reputation has also hurt the party among some Serbs, who have seen it as opportunistic, riddled with corruption, and too eager to appease the West. Djindjic was assassinated in March 2003 by organized crime figures associated with the former Milosevic regime. It suffered a substantial decline in support in the December 2003 elections but began to recover its strength when it went into opposition in 2004. Its popularity has also been boosted by its new leader, former Defense Minister Boris Tadic, who won Serbian presidential elections in June 2004.

Democratic Party of Serbia (DSS): The DSS is led by Vojislav Kostunica, formerly Yugoslav President and now Prime Minister of Serbia. Like other democratic parties, the DSS favors democracy, the rule of law (a particular interest of Kostunica's), and free market reform, but has a markedly nationalist orientation. It was highly critical of the decision to transfer Milosevic to war crimes tribunal in June 2001 and has continued to strongly criticize the tribunal. The DSS plays the leading role in the current Serbian government, established in March 2004. Its popularity has fallen since it has taken a leading role in the government.

G-17 Plus: Formerly a non-partisan economic reform group, G-17 Plus registered as a political party in early 2003. It won 34 seats in the December 28, 2003 parliamentary elections. It is perhaps the most pro-Western and pro-economic reform force in the government, where it holds key posts in the government dealing with the economy. However, its strength has declined as the government's popularity has decreased.

Serbian Radical Party (SRS): An extreme nationalist party, led by Vojislav Seselj, who is now facing war crimes charges at Yugoslav war crimes tribunal in The Hague. Although ostensibly anti-Communist, the SRS held posts in the Milosevic regime, which cost the SRS dearly in the 2000 elections. However, the SRS surged in popularity as the pro-Western and pro-reform government's fortunes waned. The SRS condemned

cooperation with the war crimes tribunal, government corruption scandals, and poor living standards, and slightly moderated its warlike, anti-Western rhetoric. The SRS won a spectacular victory in the December 2003 elections, becoming by far the largest party in the Serbian parliament. However, it did not win a majority on its own and is viewed as a pariah by democratic parties, and is therefore in opposition. Nevertheless, it remains the most popular party in Serbia.

Serbian Renewal Movement (SPO)/New Serbia: The SPO is a democratically-oriented, nationalist, pro-monarchist party, led by Serbia and Montenegro Foreign Minister Vuk Draskovic, who has had a reputation for political unpredictability. It formed an electoral coalition with a smaller group called New Serbia.

Socialist Party of Serbia (SPS): The SPS is the successor to the Serbian branch of the Yugoslav Communist party. Under the leadership of Slobodan Milosevic, the party used nationalism to dominate Serbian politics from the late 1980s until its defeat in the 2000 elections. The SPS was further weakened by Milosevic's transfer to the Yugoslav war crimes tribunal in June 2001. Its influence continues to decline, but it remains a significant force in Serbian politics. The SPS won 22 seats in the December 2003 elections, even fewer than in 2000. It is not in the government, but its support is crucial for the government to have a majority in parliament.

Strength of Serbia Movement (PSS): This party, led by Milosevic-era business tycoon Bogoljub Karic, currently has no formal representation in the Serbian parliament. However, given Karic's strong showing in the 2004 presidential vote and continuing support for the PSS in opinion polls, Karic could be a kingmaker if parliamentary elections are held in 2006. The PSS's vague, populist platform has led critics to charge that it is mainly a vehicle for protecting Karic's extensive business interests. Karic is under investigation for allegedly attempting to bribe a member of parliament.

Political Situation in Montenegro

Since 1997, Montenegro has been controlled by an anti-Milosevic faction of the local Socialist Party led by Milo Djukanovic. In October 1997, Djukanovic was elected President of Montenegro. As Djukanovic consolidated his grip on power in Montenegro, a cold war developed between Montenegrin leaders and the Milosevic regime. Milosevic did not allow Montenegro to participate in setting federal policies. For his part, Djukanovic moved to seize control of virtually all of the levers of power in Montenegro. Djukanovic successfully sought relief from Western sanctions against the FRY and received Western aid to boost Montenegro's economy.

After Milosevic's fall, efforts by Montenegrin leaders to push forward with independence from Yugoslavia were stalled by intense international pressure, particularly from the European Union. In addition to their concerns about the impact Montenegrin independence might have on the situation in Serbia and Montenegro, EU officials were also concerned that the collapse of Yugoslavia could hurt the chances of keeping Kosovo as part of the Serbia and Montenegro union.

On March 14, 2002, EU foreign policy chief Javier Solana brokered an agreement between Serbia and Montenegro on restructuring the relationship between the two republics. The FRY would be formally abolished and the country would be

renamed "Serbia and Montenegro." A "union of states" would have a popularly elected parliament, a president chosen by the parliament, and a government. It would deal with foreign affairs, defense, international economic relations, economic relations between the republics, and the protection of human and minority rights. The two republics would attempt to reform and harmonize their economies in line with EU standards. The agreement would allow either state to declare independence after three years. The agreement asserts that Serbia would inherit the FRY's sovereignty over Kosovo as laid out in U.N. Security Council 1244. In February 2003, the Federal Republic of Yugoslavia was formally dissolved and "Serbia and Montenegro" came into being as the new joint state.[2]

On October 20, 2002, Montenegro held parliamentary elections. A DPS-led coalition won an absolute majority of 39 of the 75 seats in the parliament. An SNP-led bloc won 30 seats, and the Liberals won 4. Presidential elections were scheduled for December 22, 2002. Fearing an opposition boycott which could depress turnout and therefore invalidate the vote, Djukanovic resigned as President on November 26, 2002 and was elected to the post of Prime Minister by the parliament. Djukanovic's concerns about the presidential vote proved correct when the results of the December 22 vote were invalidated due to low turnout. After a repeat presidential election failed for the same reason in February 2003, former Prime Minister and Djukanovic supporter Filip Vujanovic was elected as President when a third election was held in May 2003.

Observers have noted that Montenegro is a small republic with few industries and resources, it is highly dependent on trade and, allegedly, smuggling. Since coming to power, Djukanovic and other Montenegrin leaders been accused of complicity with smuggling operations and organized crime activities, sometimes in cooperation with the Italian Mafia figures. Italian police investigated Djukanovic's possible role in a long-standing cigarette-smuggling operation. Montenegrin leaders claim these charges of criminal conduct by top-ranking officials have been fabricated by domestic opponents and some European countries to undermine Montenegrin efforts to secure independence.

In November 2002, a Moldovan woman charged that she was kept in a Montenegrin brothel and abused by top Montenegrin officials. A Montenegrin deputy prosecutor was arrested on sex trafficking charges. A Montenegrin court later threw out the charges, claiming the woman's testimony was insufficient to warrant a trial. U.S. officials expressed disappointment with the decision. Montenegro's chief prosecutor stepped down in July 2003, amid the scandals. In September 2003, a group of independent experts, appointed by Organization for Security and Cooperation in Europe and the Council of Europe, issued a confidential report on the sex trafficking claims. The Montenegrin government has said it will implement the suggestions made in the report to strengthen Montenegro's efforts in the fight against trafficking, as well as to "completely clarify" the case of the Moldovan woman. In June 2004, the government established a national coordinator to fight human trafficking.

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[2] For more on the Serbia and Montenegro union, see CRS Report RS21568, *Serbia and Montenegro Union: Prospects and Policy Implications*, by Julie Kim.

Major Political Parties in Montenegro

Democratic Party of Socialists (DPS): The largest party in Montenegro, the DPS is the successor to the Montenegrin sister party of the Socialist Party of Serbia. In 1997, Milo Djukanovic, its leader, broke with Milosevic, taking most of the party with him. Although comprised of former Communists, the DPS espouses support democracy, free market reform and closer ties with the West.

Liberal Alliance of Montenegro: A small opposition political group that strongly supports Montenegrin independence, political and economic reform, and a pro-Western foreign policy. It criticizes the DPS for its Communist past, its lack of commitment to a truly democratic Montenegro, and charges that it has manipulated the economy for the personal gain of Djukanovic and his cronies. However, an alliance with the Socialist People's Party in 2002 laid it open to charges of opportunism.

People's Party of Montenegro (PP): Like the DPS, the PP favors political and economic reform and closer ties with the West. However, it is more strongly in favor with closer ties with Serbia than the DPS. The PP was a member of the governing coalition with the DPS until December 2001, when it quit the government in protest against a DPS plan for Montenegro's independence.

Social Democratic Party (SDP): A center-left party that shares similar domestic and foreign policy goals with the DPS. It strongly favors independence.

Socialist People's Party (SNP): The SNP was formed from the minority faction of the former Yugoslav communist party in Montenegro that remained loyal to Milosevic. It strongly favors close ties with Serbia and opposes independence.

Montenegrin government leaders have announced their intention to hold a referendum on independence in April 2006, more than three years from the time when the Serbia and Montenegro union constitution was approved. Some observers say that such a referendum could be risky for the government, given the at-best wafer-thin majority for independence in Montenegro.

The EU, once openly hostile to Montenegrin independence, has shifted its position somewhat. After calling for a postponement of the referendum in late 2005 (which the Montenegrin government rejected), the EU insisted that the referendum be held in strict accordance with democratic standards and the recommendations by the Venice Commission of the Council of Europe. The commission suggested that Montenegro retain the minimum 50% turnout requirement contained in current law for the referendum to be valid. The commission also suggested that an unspecified level of support exceeding a simple majority be required for independence to be adopted. Either threshold could be difficult for pro-independence forces to meet, depending on how they are interpreted and applied. EU-mediated talks between the government and the opposition on the terms of the independence vote may prove difficult, as pro-union forces have little incentive to cooperate with the government, particularly given open EU skepticism about independence.

Kosovo and Southern Serbia

Kosovo was an autonomous province within Serbia until 1990, when its autonomy was eliminated by Milosevic. The move provoked the province's ethnic Albanian majority to non-violent resistance then, by 1998, armed revolt by the Kosovo Liberation Army. In order to put a halt to the conflict (including atrocities by Serbian forces) and restore the province's autonomy, the United States and other NATO countries launched an campaign of air strikes against Serbia between March and June 1999. In June 1999, Milosevic agreed to withdraw his forces from Kosovo, permitting a NATO-led peacekeeping force to be deployed. Under the terms of U.N. Security Council Resolution 1244, Kosovo is governed by a U.N. Mission in Kosovo (UNMIK), until an autonomous Kosovo government can run the province itself. UNSC 1244 does not say what Kosovo's final status should be, but supports the territorial integrity of the FRY (which was replaced by the Serbia and Montenegro union in 2003).[3] Direct dialogue between Belgrade and the Kosovo government began in October 2003 but has achieved few results so far.

Serbian leaders strongly oppose independence for Kosovo, an outcome favored by virtually all ethnic Albanians, who make up over 90% of the population of the province. Serbian leaders have expressed frustration at the inability of the U.N. Mission in Kosovo (UNMIK) and KFOR, the NATO-led peacekeeping force in the province, to provide conditions for the return of Serb refugees to their homes and for Serbs remaining in the province to have a normal life. These frustrations were underlined by sweeping anti-Serb riots in Kosovo in March 2004, when 19 Serbs were killed, over 900 injured, 4,500 Serbs were driven from their homes, and many Serb homes and other property were destroyed. KFOR, UNMIK, and local police largely proved unwilling or incapable of stopping the rioters.

The Serbian government position is that Kosovo must never become independent. This view is backed by an all-party consensus in the Serbian parliament. Serbian leaders have encapsulated their current position on status with the phrase "more than autonomy, but less than independence." Serbia has also put forward a decentralization plan for Kosovo. The plan would set up autonomous Serb regions in northern Kosovo and other Serbian-majority enclaves. Serbian-majority areas in Kosovo would be controlled by local Serb authorities, with their own police, and would be linked with each other and with Serbia. Ethnic Albanian authorities would control the rest of the province. Such a plan would have the benefit, from Belgrade's point of view, of consolidating its control over northern Kosovo, where most Serbs in the province now live, and where important economic assets, such as the Trepca mining complex, are found. Ethnic Albanian leaders strongly oppose the idea for these very reasons.

To a certain extent, the Serbian plan seeks to strengthen and ratify the existing situation, particularly in northern Kosovo. Since 1999, international officials and ethnic Albanians have criticized Serbia for supporting "parallel structures" that cement its control over Serb-majority areas at the expense of UNMIK's authority.

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[3] For more on Kosovo, see CRS Report RL31053, *Kosovo and U.S. Policy*, by Steven Woehrel and Julie Kim.

International officials have also criticized the Serbian government for (successfully) calling on Kosovo Serbs to boycott Kosovo government institutions. They have noted that such a move isolates Kosovo Serbs at a time when UNMIK is devolving more powers to the Kosovo government and Kosovo's future status is being determined.

Some observers have speculated that Serbia's hard-line stance may be a negotiating tactic, with a possible fall-back position that would try to secure a partition of Kosovo, with northern Kosovo formally becoming part of Serbia and the rest becoming independent. However, the United States and other members of the Contact Group have ruled out a partition of Kosovo. Serbian leaders may also seek or be offered other forms of compensation, such as easier terms for NATO and EU membership, or at least increased aid from these institutions and their member countries. Serbian experts realize that such concessions, even if offered by the international community, may lack credibility due to "enlargement fatigue" in many European countries, among other factors.[4] Moreover, Serbian experts warn that the current political situation in Serbia may make any public concessions on its part difficult, given the weakness of the Serbian government and continued strength of the Radicals.

With the help of the international community, Serbia has had success in defusing an insurgency in ethnic-Albanian inhabited areas of southern Serbia comprising the of municipalities of Presevo, Medvedja and Bujanovac. In March-May 2001, NATO troops in Kosovo permitted the phased reintroduction of Yugoslav forces into a demilitarized zone bordering Kosovo that ethnic Albanian guerrillas had used as a springboard for attacks on Serbian territory. Under pressure from the international community, the guerrillas disbanded in May 2001. Western countries pressed Serbia to seek a peaceful settlement to the conflict by dealing with some of its underlying causes, including the ethnic balance of local police and the economic situation in the area.

In February 2001, Serbian put forward a peace plan for the region. The plan called for boosting the participation of ethnic Albanians in local government and police, with help from the Organization for Security and Cooperation in Europe. Local elections were held in July 2002 in the region. Ethnic Albanian parties now control the local governments of Presevo and Bujanovac, while Serb groups control Medvedja. However, the problems in the area are not completely solved. Some ethnic Albanians complain of discrimination, and occasional violence continues. In response to a boycott call by local ethnic Albanian leaders, almost no ethnic Albanians voted in the Serbian parliamentary elections in December 2003. Local leaders said that the Serbian election law made no provision for setting aside seats for ethnic minorities who cannot meet the requirement of winning 5% of the vote to enter the parliament. Final status talks in Kosovo could have an impact on the stability of southern Serbia. Some local ethnic Albanian leaders have called for their region to be joined to Kosovo, if Kosovo becomes an independent state.

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[4] Discussions with experts on Serbia, October 2005.

Economic Situation

The democratic leadership in Belgrade faced daunting economic challenges when it took over from the Milosevic regime in 2000. The FRY's economy suffered from years of economic mismanagement, economic isolation and the lingering effects of NATO air strikes in 1999. Many key enterprises and banks were controlled by regime cronies who managed them poorly and stole large sums from them. According to FRY officials, Serbia's Gross Domestic Product (GDP) in 1999 was only 45% of its 1990 level. Unemployment was about 35% in 2000. Conflicts in the former Yugoslavia left the FRY with over 800,000 refugees and displaced persons to care for, or about 10% of the country's population. In the final year of his rule, Milosevic increased the money supply in order to fund reconstruction projects after the Kosovo war, fueling inflation and the depreciation of the dinar, Serbia's currency. The inflation rate for 2000 was 70%. The country suffered from high levels of internal and external indebtedness. Budget deficits at all levels of government, including pension and other social welfare arrears, amounted to 8-10% of GDP. There was a tangle of bad bank debts and interenterprise arrears, amounting to 80% of GDP. There was also an external debt of $11.6 billion, or about 140% of GDP.[5]

Since 2001, the Serbian government embarked on a comprehensive economic reform program. They conducted prudent fiscal and monetary policies that have reduced inflation. They made some cuts in public spending, particularly in funding for police and military forces. The fiscal and budgetary systems are being overhauled to make them fairer and more transparent. The government ran a consolidated budget surplus of 1.5% of GDP in 2005. The country's foreign trade regime has been liberalized. Reform of the banking sector has begun. Serbia has moved to privatize "socially-owned" firms, but many still need to be restructured and sold off. Foreign direct investment (FDI) has increased rapidly in recent years. Serbia and Montenegro took in $1.17 billion in net FDI from January-September 2005.

These reform policies have had mixed results. Serbia and Montenegro has experienced rapid economic growth in recent years. Gross Domestic Product rose 8.9% in 2004 and an estimated 6.5% in 2005. Much of the increase in GDP has been due to growth in the service sector, including retail trade. Industrial production has picked up as well. Real monthly wages increased 5.7% year-on-year for the period from January-October 2005.

On the other hand, consumer price inflation, after decreasing for several years since 2001, accelerated to 16% year-on-year at the end of 2005. Unemployment remains very high, 33% of the workforce in mid-2005. As large companies are restructured, more people are losing their jobs, although the government has made great progress in decreasing regulatory red tape and simplifying labor laws in order to stimulate job growth among small and medium-sized businesses. Poverty remains a problem. In 2003, the World Bank estimated that 10% of the population of Serbia

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[5] Paper presented by FRY Deputy Prime Minister Miroljub Labus at December 12, 2000, donor coordination conference, available from the EU/World Bank website at [http://www.seerecon.org].

and Montenegro was under the poverty line, defined as 60 Euros (about $73) a month.

Serbia and Montenegro's economic policies have been supported by the International Monetary Fund and other international financial institutions. In May 2002, the IMF extended a three-year, $889 million loan to Serbia and Montenegro, after disbursing the final part of a $249 million standby loan offered in 2001. The IMF has urged Serbia and Montenegro to push forward with the restructuring and privatization of "socially-owned" firms, cut public spending, and reverse the recent spike in inflation.

Serbia and Montenegro has made substantial progress in reducing its foreign debt, due to a rapid inflow of foreign direct assistance, strong foreign exchange reserves, and debt forgiveness deals with the Paris Club in 2002 and the London Club in 2004. At the end of 2004, Serbia and Montenegro's external debt was $13.5 billion, or 63% of GDP, down from 102% in 2001. The country's current account and trade deficits shrank in 2005, due to increased foreign direct investments, increased exports, and reduced imports, which had surged from 2001 to 2004.

Under Djukanovic, Montenegro pursued a separate economic policy from Serbia. Its switch to the Deutschmark (and later the Euro) limited the damage of Milosevic's lax monetary policies. It has pursued sound fiscal and monetary policies. However, the republic's few industries need extensive restructuring, and its economy is heavily dependent on trade with Serbia and foreign countries. Privatization has accelerated in the past year, spurring very strong inflows of foreign direct investment. Moreover, some have complained about corruption in the privatization process.[6]

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[6] Global Insight report on Serbia and Montenegro [http://www.globalinsight.com], January 2006; Economist Intelligence Unit Country Report on Serbia and Montenegro, January 2006; documents from the Donor Coordination Meeting for Serbia and Montenegro, November 18, 2003, which can be found at [http://www.seerecon.org].

International Response

European Union

Eventual membership in the European Union is a key objective of the foreign policy of Serbia and Montenegro. The EU has committed itself to admitting Serbia and Montenegro when it is ready. However, the path to membership may be a long and difficult one. In October 2005, the EU announced that it would begin negotiations with Serbia and Montenegro on a Stabilization and Association Agreement (SAA). The agreement would provide a framework for enhanced cooperation between the EU and Serbia and Montenegro in a variety of fields, including the harmonization of local laws with EU standards, with the perspective of EU membership. While the European Union has not conditioned its aid to Serbia on war crimes cooperation, EU officials have made clear to Serbian leaders that a closer relationship with the EU, including concluding an SAA, requires Serbian cooperation with the ICTY. Other conditions include progress in political and economic reforms, especially rule of law and reform of the military and security sector. Although it is not a formal condition for an SAA, the talks could be stalled if Serbia strongly opposes a possible EU-supported solution to the Kosovo status issue.

On December 1, 2001, the FRY was granted preferential trading status with the EU. For 2005 and 2006 combined, the EU has budgeted 89 million Euro in aid for Serbia in 2004, 100 million for Montenegro, and 90 million for the Serbia and Montenegro union government.[7]

The European Union opposes Montenegro's independence. EU leaders fear that it would work against greater integration in the region as a whole, possibly strengthening separatist forces in Bosnia, Kosovo, and Macedonia. EU foreign policy chief Javier Solana brokered the March 2002 agreement to set up the current union of Serbia and Montenegro. Although the agreement permits either republic to leave the union within three years, EU officials at first pressed the two republics to stay together and to more closely align their economic policies, warning that such integration would be necessary if Serbia and Montenegro wished to secure an SAA in the near future or join the European Union in the longer term.

However, EU officials softened their stand in October 2004, when the EU adopted a "twin track" approach to SAA negotiations with Serbia and Montenegro. Although Serbia and Montenegro would sign a single SAA with the EU, technical aspects such as customs tariffs would be negotiated separately with each republic. Although EU leaders stressed that the "twin track" plan did not signal that they were abandoning their support for the joint state, many observers (and Montenegrin leaders) viewed it as a tacit recognition that the joint state was not working. The EU has warned Montenegro that if it opts for independence, it may have to hold separate SAA talks with the EU, delaying the process by months.

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[7] EU Commission Enlargement website, [http://europa.eu.int/comm/enlargement/cards/financial_en.htm].

NATO

In June 2003, Serbia and Montenegro made a formal request to join NATO's Partnership for Peace (PFP) program. The United States and NATO have set the arrest of Ratko Mladic as the remaining obstacle to PFP membership for Serbia and Montenegro. Leaders in Serbia and Montenegro say they want to join PFP in order to secure Western aid and advice in reforming their armed forces, including the establishment of full civilian control.

Since 2003, Serbia and Montenegro has taken steps to reform its armed forces, including by putting the General Staff and intelligence and security agencies under the control of the civilian Minister of Defense. Hundreds of high-ranking officers from the Milosevic era were retired or dismissed. Other planned changes include redrafting defense and national security strategies, and restructuring and reducing the size of the armed forces along lines suggested for NATO candidate states. Efforts must also be made to reform the country's intelligence agencies. Serbia and Montenegro does not have troops deployed to Iraq as part of the U.S.-led coalition there or in Afghanistan.

U.S. Policy

In its policy toward Serbia and Montenegro, the Administration has tried to support the country's democratic transition and integration into Euro-Atlantic institutions. However, the United States has continued to insist that Belgrade meet its international obligations, including to the International Criminal Tribunal for the Former Yugoslavia (ICTY). The Administration has advocated Serbia and Montenegro's membership in NATO's Partnership for Peace, if it delivers ICTY indictee Ratko Mladic to the Tribunal. On May 7, 2003, President Bush signed a presidential determination that permits Serbia and Montenegro to receive U.S. defense articles, services, and assistance.

The United States backed EU efforts that produced the Serbia and Montenegro union in 2003 that replaced the Federal Republic of Yugoslavia. In testimony before the Senate Foreign Relations Committee on November 8, 2005, Undersecretary of State Nicholas Burns said that the United States does not oppose the Montenegrin government's efforts to hold an independence referendum but has warned that the referendum must be held peacefully and as the result of a process that "all sides" accept as legitimate. He added that the main U.S. goal in the region is "reform and progress toward Europe for both Serbia and Montenegro, in or outside the state union."[8]

Cooperation with the War Crimes Tribunal

The fate of Milosevic and other persons indicted by ICTY has been a controversial issue in Serbia's relations with the United States. In each of the past

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[8] Statement of Nicholas Burns before the Senate Foreign Relations Committee, November 8, 2005.

six fiscal years (FY2001-FY2006), Congress has conditioned U.S. aid to Serbia after a certain date in the Spring of that year on a presidential certification that Serbia has met certain conditions, especially cooperation with the ICTY. The provisions also recommended that U.S. support for loans to the FRY be conditioned on the certification. U.S. conditions on aid to Serbia may have had a significant impact on Serbian cooperation with the Tribunal. Since the coming to power of Serbian democrats in late 2000, Serbian cooperation with the ICTY has followed a similar pattern each year: Serbia delivers several indictees to the Tribunal just before or, at most, a few weeks after the certification deadline. The Administration makes the certification as required by the legislation, and urges Serbia to do more. However, Serbian cooperation then slows, with Serbian leaders claiming that political and legal obstacles preclude greater efforts. Nevertheless, more indictees are delivered as the next deadline for certification approaches, and so on.

In a December 2005 report to the U.N. Security Council, ICTY Chief Prosecutor Carla Del Ponte said Serbia's cooperation with the Tribunal had "deteriorated" since her last report in June 2005, which provided an upbeat assessment of Serbian compliance. She said that, while some government agencies are cooperating well with the ICTY, the army of Serbia and Montenegro has been particularly unhelpful, including on such issues as access to documents. Moreover, Del Ponte said the Serbia continues to lack a "serious" action plan to transfer the remaining fugitives to the Tribunal. Of the six remaining fugitives sought by the ICTY, Del Ponte said that Mladic, Karadzic, and three other indictees are "within reach" of Serbian authorities (the sixth indictee is in Russia).[9] In January 2006, the Serbian government admitted that Mladic had been drawing a Serbian Army pension as late as mid-November 2005.

U.S. Aid

Due to U.S. and international sanctions on the FRY, the United States provided little aid to Serbia and Montenegro before FY1999. From FY1999 through FY2001, the United States obligated $136.8 million in aid to Serbia and $137.9 million in aid to Montenegro. An addition $133.5 million was allocated to the FRY as a whole for the same period.[10] The Administration provided $106.7 million in SEED funding for Serbia in FY2002 and $60 million for Montenegro. The Administration allocated $110 million for Serbia for FY2003 and $25 million for Montenegro. It budgeted $95 million in aid for Serbia in FY2004 and $18 million for Montenegro. In FY2005, the Administration requested $87 million in SEED aid for Serbia and $15 million for Montenegro. The FY2005 foreign aid measure (P.L. 108-447) provided $73.6 million for Serbia and $20 million for Montenegro. The FY2006 foreign aid bill contains $70 million in aid for Serbia and $15 million for Montenegro. SEED aid is being used to help Serbia and Montenegro establish a free market economy. U.S. aid provides advice on restructuring the banking sector, privatization, tax reform, WTO accession, fighting financial crime, and providing credit facilities to help small business and develop a mortgage market. Other SEED aid is aimed at strengthening

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[9] For a transcript of Del Ponte's remarks to the Security Council, see the ICTY website, [http://www.un.org/icty].

[10] USAID, U.S. Overseas Loans and Grants, July 1, 1945-September 30, 2001.

democratic institutions and civil society in the two republics, including by supporting the development of effective local governments.[11] Other U.S. aid is targeted at strengthening Serbia and Montenegro's exports and border controls.

Congressional Response

During Milosevic's reign, congressional action on the FRY focused on codifying and tightening sanctions against Serbia and denying it most aid, while providing significant assistance to Montenegro and some democratization assistance for Serbia. As in previous years, the House and Senate-passed versions of the FY2001 foreign operations appropriations bills included provisions that would have implemented these objectives. However, Milosevic's removal from power intervened during conference deliberations on the bill (H.R. 4811). The measure, signed by the President on November 6, 2000 (P.L. 106-429), provided $600 million for central and eastern Europe in Support for East European Democracy Act (SEED) funds. An additional $75.825 million in emergency supplemental funding was earmarked for Serbia, Montenegro and Croatia combined.

From the funds in the bill, the Administration was permitted to provide up to $100 million for Serbia. The bill did not include an earmark for Montenegro, but the conference report says that Montenegro "should" receive $89 million. Section 594 of the measure added the condition that no funds from the bill can be made available for Serbia after March 31, 2001 unless the President certifies that Serbia is "(1) cooperating with the International Criminal Tribunal for Yugoslavia including access for investigators, the provision of documents, and the surrender and transfer of indictees or assistance in their apprehension; (2) taking steps that are consistent with the Dayton Accords to end Serbian financial, political, security and other support which has served to maintain separate Republika Srpska institutions; and (3) taking steps to implement policies which reflect a respect for minority rights and the rule of law."

The law said that the United States should support the membership of the FRY to regional and international organizations subject to a certification by the President that the FRY has applied for membership on the same basis of other former Yugoslav republics, and has taken steps to settle issues related to state liabilities, assets and property. It also said that after March 31, 2001, the United States should instruct its representatives to international financial institutions to support loans to the FRY subject to the conditions in the Presidential certification on aid to outlined above (Section 594). The section did not apply to Kosovo, Montenegro, humanitarian aid or assistance to promote democracy in municipalities.

Another section of the law also prohibited any aid to countries that harbor war criminals, although this provision could be waived by the Secretary of State if he provides a determination to Congress that such aid supports the implementation of the Bosnian peace accords (Section 563).

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[11] USAID Budget Justification to the Congress, Fiscal Year 2006, Annex III Europe and Eurasia.

Members of Congress hailed the transfer of Milosevic to the ICTY on June 28, 2001. On June 29, Senators McConnell and Leahy introduced S.Res. 122. The resolution praised Prime Minister Djindjic and other Serbian leaders for their "courage" in transferring Milosevic and called on them to continue to transfer indictees to the ICTY and to release all political prisoners from Serbian jails. It expressed the sense of the Senate that the United States should continue to provide aid to the FRY to support economic, political and legal reforms there. The resolution was adopted by unanimous consent on July 18, 2001.

FY2002 foreign appropriations legislation (P.L. 107-115) contained the same conditions on aid to Serbia as in FY2001. The Administration made the certification on May 21, 2002. Secretary of State Colin Powell pointed to the passage of the war crimes cooperation law and the surrender of several indictees over the previous few weeks, as well as the release of ethnic Albanian prisoners from Serbia in March 2002 as justification for the move. Secretary Powell also said that, in the wake of the certification, the Administration favored working with Congress to restore Normal Trade Relations (NTR) status for the FRY.

The FY2003 foreign aid appropriations measure was included as part of the Consolidated Appropriations Resolution for FY2003 (P.L. 108-7). The bill contained certification provisions on aid to Serbia similar to the FY2001 and FY2002 bills, and required the President to make the certification by June 15, 2003. Secretary of State Powell made the certification on June 15, but noted that Serbia and Montenegro still need to give their full cooperation to the ICTY, including the transfer of Mladic and Karadzic.

On March 5, 2003, the House passed H.R. 1047, which, among other provisions, would permit the President to restore Normal Trade Relations (NTR) status to Serbia and Montenegro, notwithstanding the provisions of P.L. 102-420. P.L. 102-420 imposed conditions on restoring NTR to the FRY, including a Presidential certification that the FRY had ceased armed conflict with other peoples of the former Yugoslavia, agreed to respect the borders of the former Yugoslav states, and ended support to Bosnian Serb forces. In 2002, the House passed a similar measure in H.R. 5385, but the Senate did not consider a companion version before the adjournment of the 107th Congress.

The House passed H.Res. 149 on April 9, 2003. The resolution offered condolences to the people of Serbia and the family of Zoran Djindjic; noted that implementing reforms and cooperating with the International Criminal Tribunal for the former Yugoslavia must continue despite the "significant risks" they pose for the leadership of Serbia and Montenegro; and that the United States should continue to support the reforms started by Djindjic, including the fight against organized crime and corruption.

On November 4, 2003, the Administration restored Serbia and Montenegro's Normal Trade Relations (NTR) with the United States. The FRY's NTR status was suspended in 1992, in response to its role in the war in Bosnia, according to the terms of P.L. 102-420 (106 Stat. 2149). The legislation permits the Administration to restore NTR to Serbia and Montenegro if the President certifies that the FRY had ceased armed conflict with other peoples of the former Yugoslavia, agreed to respect

the borders of the former Yugoslav states, and ended support to Bosnian Serb forces. Administration officials say the move was made in response to the improved situation in Serbia, especially in defense reform and cutting links between the Serbian and Bosnian Serb armed forces. In June 2005, the Administration granted duty-free treatment to some products from Serbia and Montenegro under the Generalized System of Preferences (GSP).

The FY2004 foreign aid appropriations bill was added to an omnibus appropriations bill (H.R. 2673). The bill contains the certification process as in FY2001-FY2003, but tightens the provisions by specifically naming the transfer of Ratko Mladic as one of the steps Serbia must take to cooperate with the ICTY. The deadline for the certification was March 31, 2004. The Administration declined to make the certification, resulting in the suspension of about $16 million in U.S. aid to Serbia. The FY2005 foreign aid appropriations were incorporated into an omnibus spending bill (P.L. 107-447). It contains the same certification process as the FY2004 bill, but with a certification deadline of May 31, 2005. The conference report deleted a Senate provision to deduct from U.S. aid to Serbia an amount equal to Serbian government aid to indicted war criminals.

The FY2006 foreign operations appropriations bill (H.R. 3057) was approved by the House on November 4 and the Senate on November 10. It was signed by the President on November 14, 2006 (P.L. 109-102). The bill contains $70 million in aid for Serbia and $15 million for Montenegro. Section 563 contains the Serbian aid conditions. The provision conditioned U.S. aid to Serbia after May 31, 2006, on "(1) cooperating with the International Criminal Tribunal for Yugoslavia, including access for investigators, the provision of documents, and the surrender and transfer of indictees or assistance in their apprehension, including making all practicable efforts to apprehend and transfer Ratko Mladic and Radovan Karadzic, unless the Secretary of State determines and reports to the Committees on Appropriations that these individuals are no longer residing in Serbia; (2) taking steps that are consistent with the Dayton Accords to end Serbian financial, political, security and other support which has served to maintain separate Republika Srpska institutions; and (3) taking steps to implement policies which reflect a respect for minority rights and the rule of law." It says the Administration "should" vote for loans and aid for Serbia and Montenegro from international financial institutions after May 31, 2006, if the certification is made. The aid conditions do not apply to Montenegro, Kosovo, humanitarian aid, or assistance to promote democracy.

The provision specifically names Karadzic as well as Mladic as persons Serbia should detain. Second, it allows the Administration to issue a certification even if the two men are not transferred, if it determines that the two are not living in Serbia. (The exact whereabouts of the two men are uncertain. Mladic is widely assumed to be living in Serbia under the protection of former and serving military and security officials. Most speculation on Karadzic's location places him in Bosnia.)

The second session of the 109th Congress may consider similar conditions on FY2007 aid to Serbia, if Mladic and/or Karadzic are not turned over to the ICTY.

Figure 1. Map of Region

Adapted by CRS from Magellan Geographix.