

REGULATION OF TRADE ACROSS CONTESTED BORDERS

The cases of China/Taiwan, Serbia/Kosovo and Cyprus



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Kosovo–Serbia: Regulatory aspects of trade and economic relations

Shpend Kursani and Berat Thaqi

Introduction

This section examines economic exchange and models of trade regulations between Kosovo and Serbia for the period starting in June 1999, when the United Nations Interim Administration in Kosovo (UNMIK) was established, until December 2013. This period is examined because it includes various modes of cooperation between Kosovo and Serbia and disputes that followed as a result of Kosovo's declaration of independence in 2008. It also encompasses agreements and models that both parties agreed on, which regulate trade relations between the two. Despite the fact that Serbia lost its authority over Kosovo when the UN administration was established in June 1999, trade between the two has continued, with some interruptions after Kosovo declared its independence. In fact, Serbia is one of Kosovo's main trading partners. In 2013, Kosovo's imports from Serbia accounted for 11% of the country's total imports, reaching €285 million.⁸¹ On the other hand, Kosovo's exports to Serbia were only €14.5 million during the same period. This constitutes a large trade deficit for Kosovo, where on average only 5% of the imports from Serbia to Kosovo are covered by its exports.

Since the establishment of the UN administration in Kosovo in June 1999, trade regulation and models of cooperation between Kosovo and Serbia have evolved and changed a number of times. The following are the key milestones that took place in trade regulation and cooperation between Kosovo and Serbia.

- **Kosovo during effective UN administration (1999–2008):** During the first year after the establishment of the UN administration in Kosovo, trade between Kosovo and Serbia was considered as internal trade. This changed when the UN administration began enforcing the Constitutional Framework, which established the UNMIK Customs, among other institutions of self-government in Kosovo in 2001. During the period of effective UN administration over Kosovo, the latter did not have any formal bilateral trade agreement with Serbia. However, both countries allowed trade of goods and services until Kosovo changed its customs stamp as a result of its independence in 2008.
- **Kosovo after the Declaration of Independence (2008–2011):** During this period, Kosovo began acting as an independent state, sidelining the role of the UN administration. This led to trade and political disputes between Kosovo and Serbia. As soon as Kosovo decided to replace the UNMIK Customs stamp with the new 'Kosovo Customs' stamp, Serbia moved to block Kosovo's exports to Serbia, also banning it from using its territory as a transit route for trade with other third parties. Subsequently, Kosovo later decided to block imports from Serbia, leading to a further deterioration in relations between the two.
- **Kosovo after the commencement of the EU-facilitated negotiations with Serbia (2011–ongoing):** This period is marked by numerous rounds of negotiations between the two parties, where several agreements were reached, including the resolution of trade dispute between the two. Trade between the two parties was finally regulated only at the end of 2013. The negotiations were held at the level of technical experts as well as prime ministerial level, which enabled several agreements on the free movements of goods and customs to be reached.

81 Kosovo Agency of Statistics (2013). 'Foreign Trade Statistics – 2013'. Available at http://ask.rks-gov.net/tregtia-e-jashtme/publikimet/doc_view/1127-statistikat-e-tregtisaeuml-saeuml-jashtme-2013?tmpl=component&format=raw

Kosovo under UN administration

On 10 June 1999, the United Nations Security Council (UNSC) adopted Resolution 1244, which called for the establishment of an international civilian presence in Kosovo – UNMIK.⁸² According to the same Resolution, Kosovo would “enjoy substantial autonomy within the Federal Republic of Yugoslavia”⁸³ (FRY). Moreover, the FRY would “begin and complete verifiable phased withdrawal from Kosovo of all military, police and paramilitary forces according to a rapid timetable”.⁸⁴

With the establishment of UNMIK in June 1999, a decision was taken to abolish the FRY customs regime within Kosovo borders on the grounds that this customs regime was weak and outdated.⁸⁵ Instead, a provisional system of customs administration was set in place, and a uniform customs tax of 10% was imposed on all products being imported to Kosovo, with a few exceptions for some foodstuffs and medicinal products. However, this regime was not applied uniformly for all of Kosovo’s neighbouring states. For instance, during this period, customs officers were placed only at the border crossing points with Albania and Macedonia (around 40 of them), while no customs services were operational at the border crossing points with the FRY, that is, Montenegro and Serbia.⁸⁶ Therefore, UNMIK considered trade with the FRY as internal trade. On the other hand, Montenegro and Serbia had independently and unilaterally set up customs collection points at some border crossing points with Kosovo, applying customs duties ranging from 10% to 90% of the value of the product being imported from Kosovo. Therefore, Montenegro and Serbia considered the trade with Kosovo as external trade.

In light of the establishment of UNMIK and the withdrawal of the FRY security forces, the UN Special Representative of the Secretary General (SRSG) in Kosovo, on 15 May 2001, signed the UNMIK Regulation 2001/9. This regulation put in place the Constitutional Framework on Interim Self-Government in Kosovo, which foresaw the establishment of all the necessary self-governing institutions in Kosovo.⁸⁷ In addition, the Constitutional Framework provided for the establishment of the Customs Service in Kosovo, which was referred to as the ‘UNMIK Customs Service’. Under the Kosovo Constitutional Framework, the Provisional Institutions of Self-Government (PISG) were responsible for only administrative and operational parts of the Customs Services.⁸⁸ The SRSG, on the other hand, enjoyed ‘supreme’ powers over the PISG, including powers over the Customs Services such as: exercising control and authority over the UNMIK Customs Service; and powers to appoint the chief executive of the Customs Service and Tax Inspectorate.⁸⁹

Trade with the FRY (Montenegro and Serbia) was treated as fully internal trade by UNMIK authorities only until 1 July 2001, when value added tax (VAT) came into force in Kosovo under Regulation 2001/11 on VAT passed by Kosovo Parliament on 31 May 2001.⁹⁰ Regulation 2001/11 provided that a VAT rate of 15% was to be collected for all imports, including those from the FRY (Montenegro and Serbia).⁹¹ This meant that customs services were, for the first time, established at border crossing points with the FRY (Montenegro and Serbia), where only VAT

82 United Nations (1999). ‘Resolution 1244 (1999)’. Available at <http://www.securitycouncilreport.org/atf/cf/%7B65BFCF9B-6D27-4E9C-8CD3-CF6E4FF96FF9%7D/kos%20SRES%201244.pdf>

83 United Nations (1999). Op. cit. Annex 2, Paragraph 5.

84 United Nations (1999). Op. cit.

85 World Bank (1999). *Kosovo: Building Peace Through Sustained Growth: The Economic and Social Agenda*. Available at http://ec.europa.eu/enlargement/archives/seerecon/kosovo/documents/kosovo_building_peace_1999.pdf

86 Ibid.

87 Assembly of Kosovo (2001). ‘Constitutional Framework for Provisional Self-Government in Kosovo’. Available at http://www.assembly-kosova.org/common/docs/FrameworkPocket_ENG_Dec2002.pdf

88 Assembly of Kosovo (2001). Op. cit. Chapter 5 (c).

89 Assembly of Kosovo (2001). Op. cit. Chapter 8 (x).

90 UNMIK (2001). ‘UNMIK Regulation No. 2001/11 on Value Added Tax in Kosovo’, 31 May 2001. Available at http://www.atk-ks.org/wp-content/uploads/2010/07/Regulation_2001_11.pdf

91 UNMIK (2001). Op. cit. Chapter 2, Section 2, Paragraph 2.1.

and no customs duties were being collected – this marked a *de jure* establishment of Kosovo as a separate customs zone. The decision urged the FRY to add an annex to its previous Resolution to the Security Council of 4 May 2001 on the position of Serbian people and members of other non-Albanian communities in Kosovo, in which it stated a deep concern about UNMIK's decision. In the annex, the FRY authorities to the UN stated that “[t]he establishment of customs points at the administrative boundary of Kosovo and Metohija with central Serbia is giving cause for added concern among [Serb] citizens [living in Kosovo]”.⁹² Furthermore, Serbia considered UNMIK's decision to be in violation of UNSC Resolution 1244, adding that such policies, including fiscal policies, in Kosovo should be pursued in consultation with the Yugoslav authorities.⁹³ Notwithstanding the reactions by Serbia, the UNMIK Customs Services at the border crossing points with Serbia continued to function normally to a large extent, until Kosovo declared its independence in February 2008.

The context within CEFTA

On 27 July 2007, Kosovo together with five other countries of the Western Balkans became a full member of the Central European Free Trade Agreement (CEFTA).⁹⁴ CEFTA is based on principles of the free market economy along the lines of the Marrakesh Agreement Establishing the World Trade Organization (WTO).⁹⁵ In addition, the agreement aims to promote cooperation in areas of common interest based on equality, mutual benefit, non-discrimination and international law.⁹⁶ Given that Kosovo was not an independent state, UNMIK signed the ratification agreement on behalf of Kosovo on 19 December 2006. It is worth mentioning that UNMIK, on behalf of Kosovo, had already signed bilateral trade agreements with Albania (2003), Macedonia (2005), Croatia (2006), and BiH (2006) on behalf of the PISG of Kosovo, which all later became members of CEFTA. Kosovo and Serbia had never signed a bilateral trade agreement before. However, as soon as the parties became members of CEFTA, all the previous bilateral agreements were automatically cancelled in accordance with Annex 2 of CEFTA.⁹⁷ Serbia did not refuse Kosovo's membership of CEFTA for two reasons: first, the agreement was signed by UNMIK and not the Kosovo authorities; and second, Kosovo was represented by an UNMIK representative and not by someone delegated by the Kosovo authorities. This was done in accordance with UNSC Resolution 1244.⁹⁸

Kosovo's membership of CEFTA was seen as a good opportunity for the weak and small economy of the Kosovo. It was assumed that the weak private sector would gain experience in facing competition, thereby increasing its efficiency and improving product quality. In addition, Kosovo and the other members of CEFTA would be exposed to approximately 30 million customers without trade barriers. Furthermore, the agreement would prepare Kosovo for membership of the EU and the WTO. However, as Figure 4 below shows, Kosovo did not gain much market within CEFTA; on the contrary, its exports to the CEFTA members continued to decrease even after it became a member of CEFTA. In addition, the political disputes that unfolded between Kosovo and Serbia after the former declared its independence in February 2008 did not help Kosovo in gaining much from CEFTA and its potential access to this free trade zone.

92 UNMIK (2001). 'UNMIK Regulations – Annex to the letter dated 5 May 2001 from the Permanent Representative of Yugoslavia to the United Nations addressed to the President of the Security Council'. Available at <http://www.icj-cij.org/docket/files/141/15034.pdf>

93 'Kosovo and Metohija' is the Serbian government denomination for Kosovo.

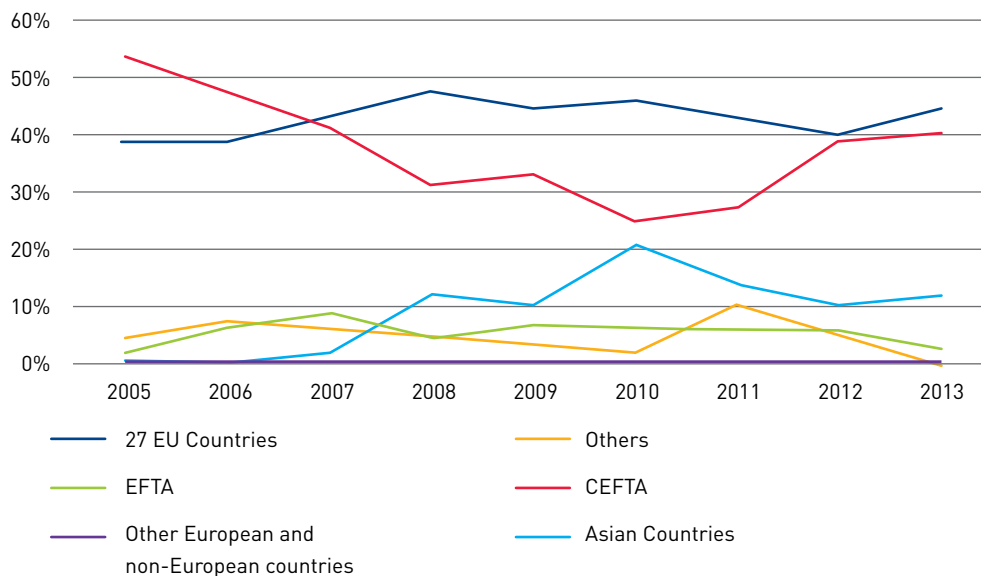
94 CEFTA was founded in 1992 by four Central European countries: Czech Republic, Hungary, Poland and Slovakia. Later on, other countries joined too such as: Slovenia (1996), Romania (1997), Bulgaria (1998), Croatia (2003) and Macedonia (2006). The last countries to join the agreement in 2007 were six south-east European countries: Albania, Bosnia and Herzegovina (BiH), Moldova, Montenegro, Serbia, and Kosovo under the representation of UNMIK.

95 CEFTA (2006). 'Consolidated Version of the CEFTA 2006 – Preamble'. p. 2. Available at <http://192.232.255.119/~cefta/sites/default/files/trade/ANN1CEFTA%202006%20Final%20Text.pdf>

96 Ibid.

97 See reference to bilateral agreements being terminated on the date of entry into force of CEFTA in CEFTA (2006). 'Agreement on Amendment of and Accession to the Central Free Trade Agreement', Article 4, Paragraph 5. Available at <http://192.232.255.119/~cefta/sites/default/files/CEFTAMAINTEXT2006.pdf>

98 CEFTA (2006). Op. cit.

Figure 4: Kosovo's exports by region (2005–2013)⁹⁹

Note: EFTA refers to the European Free Trade Association.

After the declaration of independence

Two days after Kosovo's declaration of independence, on 19 February 2008, the border crossing points with Serbia 1 and 31 in the northern part of Kosovo were set on fire by Serb extremists supported by Belgrade.¹⁰⁰ The setting on fire of the border crossings is attributed to two main reasons: one concerns the symbolic gesture of refusing to live in an independent Kosovo; the second relates to the fact that they did not want to pay any VAT to the budget of an independent Kosovo. According to local Serbs and businesses, the collected sums of VAT at the border crossing points with Serbia would no longer go to Kosovo's Consolidated Budget under UNMIK, but to the budget of an independent Kosovo instead. As such, they considered that this would imply recognition of independence, which the Serbs wanted to avoid at all costs.¹⁰¹ This created a situation whereby the northern part of Kosovo became de facto a free economic zone under Serbia's rule, with very limited, if no authority at all of Kosovo over this part of its territory. After Kosovo's declaration of independence, and following the demolition of the border crossing points in the northern part of Kosovo, the Serbian government took the decision to exempt Serbia's economic operators (businesses) trading with the northern part of Kosovo from paying Serbian VAT too. In other words, not only were the Serbian businesses exporting goods to the northern part of Kosovo not paying Kosovo's VAT, but they were also refunded the Serbian VAT for all the products that entered the north, which set the stage for all sorts of smuggling activities.¹⁰²

In addition, ever since Kosovo's declaration of independence, the Serbs living in the northern part began defying even the limited authority wielded by the international community in the north, including that of UNMIK – and especially the EU Rule of Law Mission in Kosovo (EULEX), which the Serbs and Serbia itself constantly viewed to be in the service of a now independent 'Albanian state'.¹⁰³ Shortly after its declaration of independence, Kosovo established its own

⁹⁹ Kosovo Agency of Statistics (2013). Op. cit.

¹⁰⁰ Kosovo and Serbia maintain six official border crossing points. The two border crossing points 1 and 31 are in the Serb majority populated area of the northern part of Kosovo, while the other four border crossing points are in the north-east and eastern parts of Kosovo.

¹⁰¹ Authors' interview with a local Serb from the north, 20 December 2013, Mitrovica North.

¹⁰² Serbia's economic operators began using this opportunity by claiming that they had exported to the northern part of Kosovo on paper, but without doing so in practice, thus claiming VAT refunds for the value of the products they were claiming to export to the north.

¹⁰³ S. Kursani (2014). *Altering the Status Quo in the Northern Part of Kosovo after the First Brussels Agreement*. Available at [http://www.iksweb.org/repository/docs/Altering_the_status_quo_in_the_northern_part_of_Kosovo_Final_Shpend_Kursani_\(2\)_578268.pdf](http://www.iksweb.org/repository/docs/Altering_the_status_quo_in_the_northern_part_of_Kosovo_Final_Shpend_Kursani_(2)_578268.pdf)

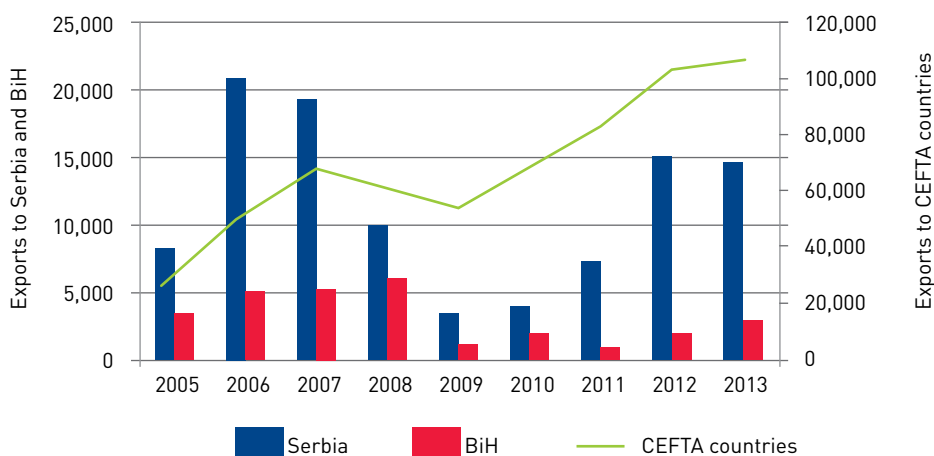
Customs Services, which meant that it took over all of UNMIK's executive authorities under the UNMIK Customs Services. In addition, as Kosovo adopted its state symbols, it began replacing all the UNMIK symbols with the new Kosovo symbols starting from June 2008, around four months after its declaration of independence. The Kosovo authorities changed the previously used UNMIK Customs stamp with the new Kosovo Customs stamp in December 2008 (see Picture 2), around 10 months after it declared its independence and around six months after it began replacing the old symbols with the new ones. As soon as Kosovo changed its customs stamp in December 2008, Serbia and Bosnia and Herzegovina (BiH) decided to block all imports from Kosovo on the grounds that such customs stamps were illegal and against the CEFTA.

Picture 2: Example of UNMIK stamps and the new Kosovo stamps used at the border crossing points



Even though Kosovo continued to be represented by UNMIK in the CEFTA, the change of customs stamps, according to Serbia and BiH, were considered a breach of the CEFTA. As a result, Serbia and BiH blocked their imports from Kosovo as well as the use of their territory as a transit route for Kosovo products. Kosovo's exports to Serbia fell by 65% in 2009, compared with exports in 2008 (see Figure 5). Throughout the period during which Serbia and BiH blocked Kosovo's exports, the latter lost €30 million in exports, representing around 4% of Kosovo's total exports for the period 2009–2011.

Figure 5: Kosovo exports (2005–2013)¹⁰⁴ (€ thousands)



104 Kosovo Agency of Statistics (2013). Op. cit.

As Figure 5 above shows, although the blockade remained in effect until 2011, Kosovo's exports to Serbia did not completely stop in reality. This is because the Serbian Tax Authority operating in the northern part of Kosovo was issuing documents to Serbian businesses in Kosovo, and they were then able to export from Kosovo to Serbia. These goods were not registered as exports to Serbia transiting through the northern part of Kosovo since, as noted above, it was a de facto part of Serbia's economic zone; they were registered at the other border crossing points between Kosovo and Serbia being used by the Serb-owned businesses in Kosovo.¹⁰⁵ Serbia's decision to issue such documents to Serb-owned businesses in Kosovo was in direct conflict with the concept of Kosovo having a sole customs region, where only Kosovo authorities could issue such documents.¹⁰⁶

Kosovo, on the other hand, did not use the dispute resolution mechanisms provided by the CEFTA. According to Article 42 of the agreement (CEFTA), parties should first try to resolve disputes between themselves through consultations and cooperation in the Joint Committee. If the parties failed to resolve the dispute, after taking the steps foreseen in the agreement, then the Joint Committee would recommend the appropriate measures, although the parties would have the right to agree or disagree with those measures. If the parties considered that a solution had not been reached, after 90 days of the request for consultations, they could take provisional rebalancing measures. In addition, parties could request arbitration procedures. However, an arbitral tribunal could be established only if more than one member of the CEFTA filed a complaint for the same issue and for the same party towards which the complaint was addressed. If the arbitral tribunal was established, its decisions would be all binding. Kosovo did not follow these procedures; instead, the authorities in Kosovo sent letters of complaint to Serbian authorities, the European Commission and the Secretariat in Brussels.¹⁰⁷ The UN SRSG in Kosovo assured Serbia and BiH through an official letter that the change of customs stamp was in compliance with UNSC Resolution 1244 since it included only the word 'Kosovo' and not the 'Republic of Kosovo'.¹⁰⁸ However, the issue was never sent for consultation at the CEFTA Joint Committee. Kosovo used the rebalancing (reciprocity) measures only in 2011, as will be discussed below.

Finding a model: EU-facilitated negotiations between Kosovo and Serbia

Kosovo was unable to export to Serbia for more than two-and-a-half years until the agreement on the customs stamp was reached on 2 September 2011 in the EU-facilitated negotiations between Kosovo and Serbia that commenced on 8 March 2011. The EU-facilitated negotiations brought both parties around the negotiation table for the first time since Kosovo declared its independence. These negotiations were a political process, which in the beginning dealt with 'technical' matters. After five rounds of negotiations took place in Brussels, Edita Tahiri (negotiator for Kosovo) and Borislav Stefanović (negotiator for Serbia), on 2 July 2011, finalised three agreements on:¹⁰⁹ freedom of movement; civil registry books; and acceptance of university diplomas. The three issues on which the parties managed to agree did not touch on the issue of the northern part of Kosovo, and did not require any particular compromise from either party.¹¹⁰

The next round of negotiations, the sixth one in a row, had been scheduled for 20 July 2011; however, Serbia informed the EU facilitator, Robert Cooper, that they were not ready to join this round of the negotiations.¹¹¹ As noted in Cooper's letter, sent to both parties a day before the sixth

¹⁰⁵ Ibid.

¹⁰⁶ European Commission (2010). *Kosovo 2010 Progress Report*, COM(2010) 660. Available at http://ec.europa.eu/enlargement/pdf/key_documents/2010/package/ks_rapport_2010_en.pdf

¹⁰⁷ GAP Institute (2011). *Kosovo in CEFTA: In or Out*, Policy brief. Available at http://www.institutigap.org/documents/72590_CEFTAEng.pdf

¹⁰⁸ European Commission (2010). Op. cit.

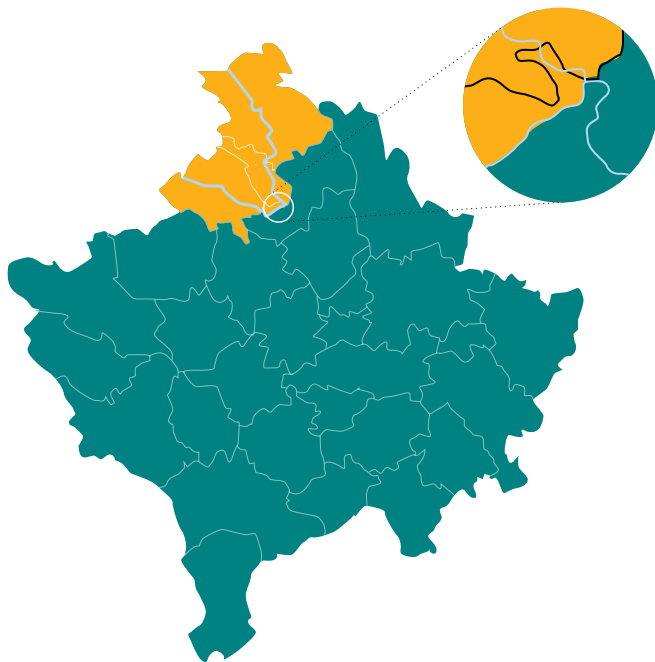
¹⁰⁹ 1st meeting held on 8–9 March 2011; 2nd meeting held on 28 March 2011; 3rd meeting held on 15 April 2011; 4th meeting held on 17–18 May 2011; and 5th meeting held on 2 July 2011.

¹¹⁰ S. Kursani (2014). Op. cit.

¹¹¹ B92 (2011). 'Better prospects for agreement in September', 20 July 2011. Available at http://www.b92.net/eng/news/politics.php?yyyy=2011&mm=07&dd=20&nav_id=75533

round of negotiations, he had to cancel the meeting “as it became clear that no agreement would be reached”.¹¹² Serbia’s reluctance to continue with the next round of negotiations was due to the fact that the talks would touch on issues concerning the status quo in the northern part of Kosovo, which Serbia was keen to keep as it enjoyed overwhelming influence in that area.¹¹³ These issues included, among others: regional trade and free movement of goods; telecoms and energy issues; car licences, which were also discussed during the previous rounds of negotiations, but on which no agreement was reached. Any agreement on such issues would, in one way or another, alter the status quo that persisted in the northern part of Kosovo for two-and-a-half years.

Picture 3: Map of Kosovo, with northern part (in orange)



Given that Kosovo wanted to reach an agreement on the free movement of goods, in order to remove Serbia’s blocking of Kosovo products, and since Serbia wanted to postpone such an agreement, one day after the meeting was cancelled, the Kosovo government decided, on 20 July 2011, to apply reciprocity trade measures against Serbia.¹¹⁴ Executing such a decision was not a problem for the four border crossing points with Serbia in the north-east and eastern parts of Kosovo. However, it was a problem at the two border crossing points (gates 1 and 31) in the northern part of Kosovo, where Kosovo had very limited, if no, authority and presence. EULEX was the sole authority present at the two border crossing points in the northern part of Kosovo. The Kosovo government asked EULEX to implement the government decision and block the incoming products from Serbia entering Kosovo; however, EULEX refused to do so. This left the Kosovo government with no alternative but to move ahead and implement the measure on its own. Accordingly, the government sent its Regional Operations Special Units (ROSU) to take over the two border crossing points in the north. This led to clashes between the ROSU and the local population supported by parallel security structures installed by Serbia in the northern part of Kosovo, which resulted in the killing of one ROSU member.

The EU wanted to prevent such a situation by facilitating talks between the parties to resolve any disagreement in a peaceful manner, that is, at the negotiation table. Therefore, on 26 July

112 European Union (2011). ‘Press statement: EU facilitated dialogue – next round of talks postponed’, Brussels, 19 July 2011. Available at http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/EN/foraff/123964.pdf

113 S. Kursani (2014). Op. cit.

114 Tema Online (2011). ‘Kosova nis reciprocitetin, bllokun mallrat e Serbisë’, 20 July 2011. Available at <http://www.gazetatema.net/web/2011/07/20/kosova-nis-reciprocitetin-bllokun-mallrat-e-serbise/>

2011, the Head of the CFSP, Catherine Ashton, issued a statement “that the efforts must focus on resolving the underlying issues through the EU facilitated dialogue. The dialogue is the only way forward to solve the issue of customs stamps and to re-establish free trade in both directions”, without much additional instruments at her disposal to resolve the conflict.¹¹⁵ The next day, on 27 July 2011, a number of Serb organised criminal groups damaged one of the border crossing points in the northern part of Kosovo; as a result, the KFOR German troops present in the area reacted by taking control of the situation, thus preventing further deterioration of the security situation.¹¹⁶ The fact that Serbia wanted to maintain the then existing status quo in the north was confirmed when the Serbian negotiator, Borislav Stefanović, himself came to the northern part of Kosovo and encouraged the local Serb population to prevent Priština’s attempts to establish its authority there.¹¹⁷ Stefanović used his visit to also meet with the KFOR German troops and agreed with them that these troops would remain at the border crossings in the north until 15 September 2011.¹¹⁸

Steps towards removal of mutual trade blockade

Germany, as one of the key EU member states and one that is increasing its political influence over the Western Balkans, played a key role in restoring the situation and preventing further escalation. At a meeting with Serbia’s then President, Boris Tadić, held in Belgrade on 23 August 2011, Germany’s Chancellor, Angela Merkel, pressed the former to renounce Serbia’s intentions to maintain its influence in the northern part of Kosovo and to resume the negotiations with Kosovo on issues that were left to be discussed. Given that Serbia was keen to accelerate its way through the EU accession process, Germany was able to change Serbia’s course with reference to the EU conditionality instruments of the accession process. On 2 September 2011, only 10 days after Chancellor Merkel met President Tadić in Belgrade, the negotiations between Kosovo and Serbia resumed and the agreement on free movement of goods and the customs stamp was reached. Finally, Serbia agreed to allow the Kosovo Customs stamp to be used for imports from Kosovo, which led to the Kosovo government lifting the trade reciprocity measure it had imposed on 20 July 2011.¹¹⁹ The parties finally lifted their mutual trade blockade on 16 September 2011, ending the 58-day reciprocity measures applied by Kosovo. It should be noted that this agreement did not please the local Serbs in the northern part of Kosovo. They rightly suspected that such an agreement would alter the status quo, which would be to their disadvantage as Kosovo authorities would increase their presence in the area. Their contempt resulted in the establishment of dozens of roadblocks to prevent Kosovo government personnel (police and customs officers) from entering the north. As a result, Kosovo was only able to dispatch its customs officers to gates 1 and 31 in the north by air transport, assisted by EULEX helicopters – a situation that lasted for around a year.

Impact of reciprocity measures with Serbia

During the 58 days of reciprocity measures applied by Kosovo, Serbian imports were mainly replaced by imports from the other regional countries. Figure 6 below shows Kosovo’s import portfolio for the third quarter of each year between 2008 and 2012. As the figure shows, imports from Serbia during the third quarter of 2011, during which the reciprocity measures applied, represented only 5% of Kosovo’s total imports, compared with 11%–12% of imports in the third quarter of the previous three years. Besides some of Kosovo’s other trade partners, such as the EU, which are not shown in this graph, but which could have substituted Serbia’s imports to Kosovo as well, it is clear that Macedonia played a significant role in substituting these imports to

115 European Union (2011). ‘Statement by the spokesperson of EU High Representative Catherine Ashton on the situation in northern Kosovo’, Brussels, 26 July 2011. Available at http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/EN/foraff/124060.pdf

116 S. Kursani (2014). Op. cit.

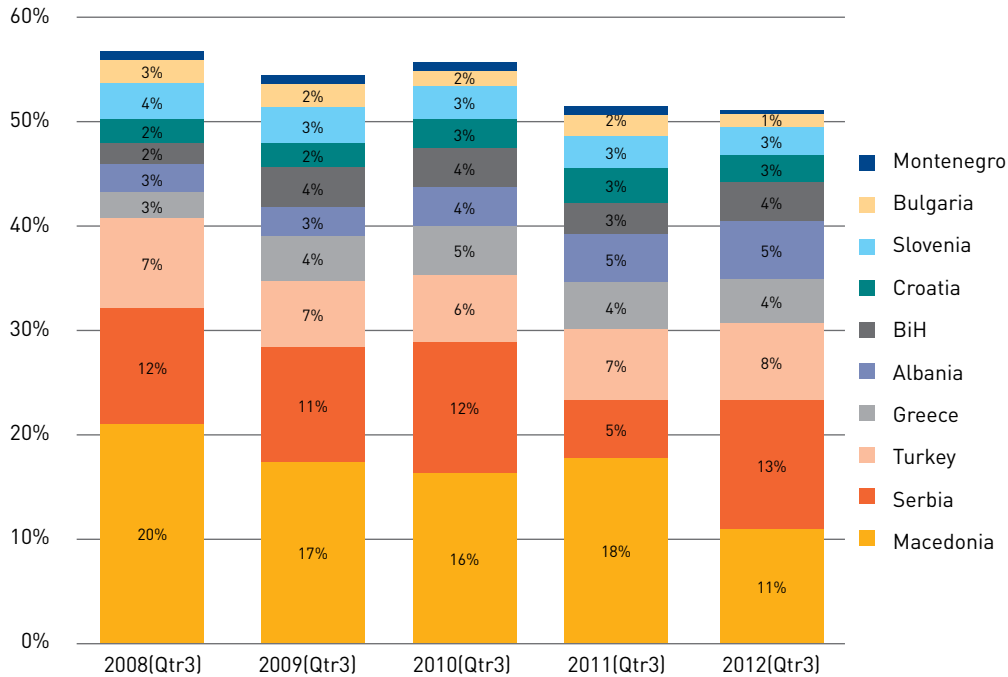
117 Ibid.

118 B92 (2011). ‘Belgrade: KFOR stepped outside UNSCR 1244’, 28 July 2011. Available at http://www.b92.net/eng/news/politics.php?yyyy=2011&mm=07&dd=28&nav_id=75662

119 European Union (2011). ‘Press statement: EU facilitated dialogue – Agreement on Customs Stamps and Cadastre’, Brussels, 2 September 2011. Available at http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/EN/foraff/124501.pdf

Kosovo. Imports from Macedonia during the third quarter of 2011 represented 18% of Kosovo's total imports compared with 16%–17% in the third quarter of the previous two years.

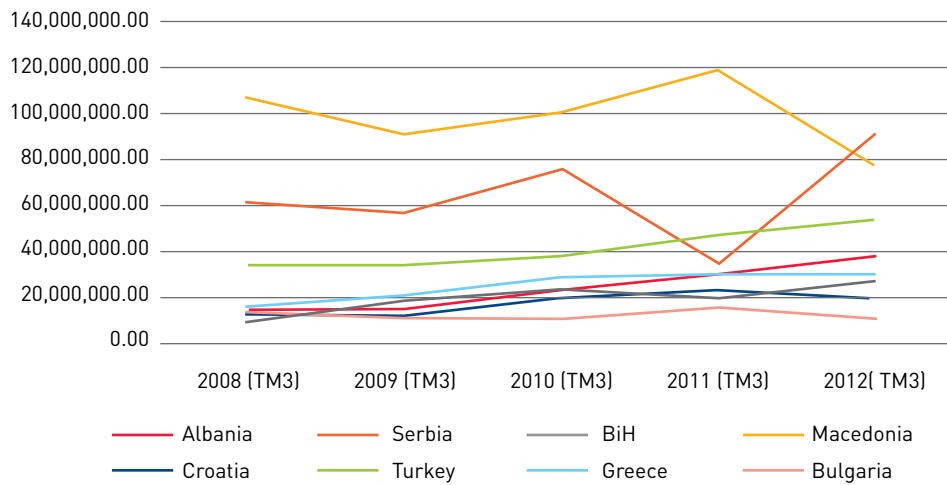
Figure 6: Impact of trade reciprocity with Serbia on Kosovo's total imports for third quarter of year (2008–2012)¹²⁰



Moreover, regarding the volume of imports, Figure 7 below shows a sharp decline in imports from Serbia during the third quarter of 2011 – that is, from around €80 million in the third quarter of 2010 to below €40 million in the third quarter of 2011. It is clear that there are two countries in the region with which Kosovo registered a sharper increase in import volume during the third quarter of 2011 – namely, Macedonia and Bulgaria. Imports from Macedonia during the third quarter of 2011 rose to €120 million from around €100 million in the third quarter of 2010, while imports from Bulgaria exceeded €15 million during the third quarter of 2011 compared with around €10 million in the third quarter of 2010. Therefore, it could be said that imports from Macedonia and Bulgaria substituted the imports from Serbia during the application of the reciprocity measures not only relative to all imports, but also in absolute terms, because as soon as the reciprocity was lifted, the import figures for these two countries dropped to their previous lower levels in the third quarter of 2012, while imports rose from Serbia.

¹²⁰ Authors' own calculation based on Kosovo Agency of Statistics data.

Figure 7: Impact of trade reciprocity with Serbia on Kosovo's total import volume for third quarter of year (2008–2012)¹²¹ (€)



An agreement that would work

It is worth mentioning that, although Kosovo and Serbia agreed on the free movement of goods and on customs stamps, and even though the Kosovo authorities were installed at border crossing points in the north, the local Serb population and businesses smuggled products from Serbia into Kosovo via “alternative roads”.¹²² They did so because they did not want to go through customs checkpoints of the independent Kosovo authorities and wanted to avoid paying customs. Moreover, during this period, the Kosovo authorities at the border crossing points in the northern part of Kosovo were merely playing the role of monitoring officials; the real executive power for customs services at the two border crossing points in the north rested with members of EULEX, who often did not implement orders from Pristina. This meant that many products were imported into Kosovo without the collection of VAT or other customs duties in accordance with the CEFTA. In other words, the agreement on free movement of goods that was reached with Serbia on 2 September 2011 did not translate into meaningful revenue for the Kosovo budget because the Kosovo authorities were not collecting these duties at the two border crossing points in the north.

During the subsequent rounds of negotiations, at the end of 2011, the concept of Integrated Border Management (IBM) was discussed as “a way forward to find a European solution for crossing points”.¹²³ The agreement on the IBM was essential for Kosovo because it needed to establish an official border crossing that Serbia would have to respect – one that would allow Kosovo to set proper border control for its northern part and to collect VAT and other customs duties, as with the other border crossing points. A preliminary agreement on “the EU developed concept of integrated management for crossing points (IBM)”¹²⁴ was reached at the eighth round of the technical dialogue between Edita Tahiri and Borislav Stefanović. This meant “that the parties [would] gradually set up joint, integrated, single and secure posts at all their common crossing points”.¹²⁵ The agreement also stipulated that EULEX “[would] be present in line with its mandate”.¹²⁶

¹²¹ Authors' own calculation based on Kosovo Agency of Statistics data.

¹²² Kosovar Institute for Research and Development (2012). *Autonomy for the Northern Part of Kosovo: Unfolding Scenarios and Regional Consequences*, Policy Paper Series 2012/05. Available at http://www.kipred.org/advCms/documents/46046_Autonomy%20for%20the%20northern%20part%20of%20Kosovo%20-%20Unfolding%20scenarios%20and%20regional%20consequences.pdf

¹²³ European Union (2011). 'Press statement: EU facilitated dialogue – Positive resumption', Brussels, 21–22 November 2011. Available at http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/EN/foraff/126265.pdf

¹²⁴ European Union (2011). 'Press statement: EU facilitated dialogue – Agreement on IBM', Brussels, 2 December 2011. Available at http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/er/126544.pdf

¹²⁵ Ibid.

¹²⁶ Ibid.

An additional technical protocol for IBM needed to be signed by both parties in order to initiate the implementation of this agreement; however, Serbia kept delaying its implementation for more than a year. Even Kosovo's then Foreign Minister, Enver Hoxhaj, voiced these concerns at the UNSC meeting on 14 May 2012, reiterating that Serbia was not signing the technical protocol on IBM implementation.¹²⁷ Minister Hoxhaj believed that Serbia was doing this because it was still trying to retain its influence in the north and even partition Kosovo at its north.¹²⁸ The issue of the lack of implementation of the 2 December 2011 agreement on the IBM was also discussed at the fourth round of the negotiations held at the level of prime ministers. On 17 January 2013, the then Prime Minister of Kosovo, Hashim Thaçi, and the then Prime Minister of Serbia, Ivica Dačić, met for the fourth time, discussing the issue of IBM implementation.^{129, 130} Serbia's prime minister was persuaded to move on with the implementation of the agreement only after Kosovo's prime minister agreed in principle that the collection of VAT and customs duties at the two border crossing points in the northern part of Kosovo (gates 1 and 31) would be allocated for the four Serb majority municipalities of the northern part of Kosovo.¹³¹ Around a month later, both parties reached an agreement on the technical protocol for the implementation of the IBM on 24 February 2013.¹³² Kosovo signed the technical protocol on 28 February 2013, while it took Serbia an additional six months to sign the protocol. Kosovo eventually began collecting taxes at the two border crossing points in the northern part of Kosovo from mid-December 2013, and ever since this has continued to work normally and in accordance with the agreements reached between Kosovo and Serbia since 2011.

Summary

- With the establishment of UNMIK in Kosovo in June 1999, a decision was taken to abolish the FRY customs regime on the grounds that the regime was weak and outdated. In the beginning, UNMIK considered trade between Kosovo and Serbia as internal trade, and no customs services were set at the border crossing between Kosovo and Serbia until 2011.
- The UNMIK Customs Services became fully operational in mid-2001 when it passed a regulation on the Constitutional Framework. This was the period when UNMIK and the self-governing institutions in Kosovo passed a regulation on VAT, which had to be collected at the border crossing points. This made Kosovo a separate customs zone from Serbia, thus treating trade between the two as external trade. However, no customs duties were collected for imports from Serbia.
- Kosovo never had a bilateral free trade agreement with Serbia. However, on 27 July 2007, Kosovo together with five other countries of the Western Balkans, including Serbia, became full members of the CEFTA. Kosovo was represented by UNMIK.
- When Kosovo declared its independence in February 2008, the border crossing points with Serbia (gates 1 and 31) in the northern part of Kosovo were set on fire by Serb extremists supported by Belgrade. Serbs in the northern part of Kosovo refused to live in an independent Kosovo and did not want to pay any VAT towards the budget of an independent Kosovo.

127 Kosovo Ministry of Foreign Affairs (2012). 'Minister Hoxhaj: The duplicity of Serbia', 14 May 2012. Available at <http://www.mfa-ks.net/?page=2,4,1238>

128 Ibid.

129 As mentioned previously, Serbia was dragging the implementation of IBM, as it would substantially change the status quo in the North by undermining Serbia's influence that it had maintained through its "open and free" economic zone.

130 European Union (2013). 'Statement by the EU High Representative Catherine Ashton after the fourth meeting in the framework of the EU-facilitated dialogue', Brussels, 17 January 2013. Available at http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/EN/foraff/134784.pdf

131 S. Kursani (2014). Op. cit.

132 European Union (2012). 'Press statement: EU facilitated dialogue – Agreement on Regional Cooperation and IBM technical protocol', Brussels, 24 February 2012. Available at http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/EN/foraff/128138.pdf

- After independence, Kosovo began adopting its state symbols, replacing all the previously used symbols under the UNMIK heading with new symbols. In December 2008, Kosovo replaced the UNMIK Customs stamp with the new Kosovo Customs stamp. This led Serbia and BiH to block their imports from Kosovo and to prohibit Kosovo businesses from using their respective territories as a transit route for Kosovo's exports to third parties.
- In response, Kosovo applied 58 days of trade reciprocity measures with Serbia and BiH, running from 20 July 2011 until 16 September 2011. This ended when the parties reached a provisional agreement on free movement of goods and customs stamps. Serbia was pressed to accept Kosovo Customs by Germany, a key EU member state.
- Nonetheless, although the trade blockade was lifted by both parties, Kosovo still did not collect VAT at the border crossing points in the north. This finally changed when an additional agreement on the IBM and a subsequent agreement on the technical protocol for IBM implementation was reached and signed in 2013.
- Trade relations between Kosovo and Serbia were finally regulated and trade principles began to be implemented as agreed starting from December 2013.