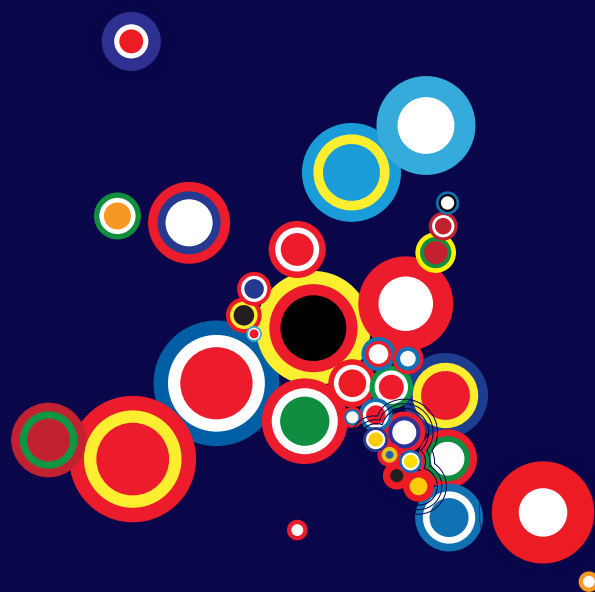




INSTRUMENT FOR PRE-ACCESSION ASSISTANCE (IPA II) 2014-2020

MONTENEGRO

Support for Public Finance Management (PFM) Policies



Action summary

The overall objective of the Action is to ensure fiscal sustainability and sound management of public finances in line with EU legislation and numerical fiscal rules. The Action will improve the efficiency, effectiveness and transparency of the Public Finance Management (PFM). It is expected to result in significant advancements in the functioning of the budgetary system, managerial accountability, state aid policy, public private partnership (PPP), concessions and public procurement (PP), and external audit.

The action translates at national level the efforts of the EU member states to safeguard the macroeconomic and fiscal stability in the EU, thus ensuring that Montenegro will be able to join the EU as a state with strong public finance and good economic governance.

The public finance reform of the country has a two-fold objective. One is to make Montenegro capable of implementing the EU requirements on identification, prevention and management of fiscal risks, excessive fiscal deficits and harmful macroeconomic imbalances. On the other hand, it must ensure that public spending is structured in the way that maximizes the development impact on the national economy and ensures better quality of life for the citizens.

Action Identification	
Action Programme Title	Annual Action Programme for Montenegro (2014)
Action Title	Support for Public Finance Management (PFM) Policies
Action Reference	IPA/2014/ 032-022.2/ME/PFM
Sector Information	
IPA II Sector(s)	Democracy and Governance
DAC Sector	15111 Public finance management
Budget	
Total cost	EUR 4.0 million
EU contribution	EUR 3.6 million
Management and Implementation	
Method of implementation	Indirect management
<i>Indirect management:</i> National authority or other implementing body	Directorate for Finance and Contracting of the EU Assistance Funds (CFCU)
Implementation responsibilities	/
Location	
Zone benefiting from the action	Montenegro
Specific implementation area(s)	/
Timeline	
Deadline for conclusion of the Financing Agreement	At the latest by 31 December 2015
Contracting deadline	3 years following the date of conclusion of the Financing Agreement, with the exception of the cases listed under Article 189(2) Financial Regulation
End of operational implementation period	6 years following the date of conclusion of the Financing Agreement.

1. RATIONALE

PROBLEM AND STAKEHOLDER ANALYSIS

To achieve a fiscal sustainability, Montenegro's policy focuses primarily on the consolidation of public finances, in order to reduce fiscal vulnerabilities. Guided by this principle, the Government of Montenegro has been implementing a number of consolidation measures. The main goal of economic policy of the country is to achieve real convergence with the EU. The EU *acquis* requires that future Member States should identify potential risks, prevent or correct any excessive fiscal deficits and harmful macroeconomic imbalances and correct the imbalances that are already in place. With a view to improving the overall system of public finances in Montenegro, as well as harmonising the regulations with EU *acquis*, the Parliament of Montenegro adopted the *Law on Budget and Fiscal Responsibility* introducing numerical fiscal rules and medium-term budget framework.

In order to establish basic principles of good fiscal management, reflecting in clear linkages between budgeting and government policies, Montenegro will continue implementing programme budgeting, that will represent one of the most effective and efficient methodology in achieving this goal. The activities conducted so far in the field of **programme budgeting** have been extensive and very important from the point of view of changing the methodology of budgeting and moving towards the alignment with international practices, and creating a solid foundation for continuance of the process. Although the overall structure is in place, the system has not been fully developed, performance indicators were not introduced, and linkages between performance based budgeting and government policies were not thoroughly established. Within the Ministry of Finance, an internal system of budget management has been developed in order to improve technical capabilities of budget planning and control of budget execution, which provided high-quality technical support to budget analysts, and significantly improve the efficiency of operations. However, the main disadvantage of this system is that it isn't connected to the SAP system (system used by the Treasury to record the payments), technology is outdated and based on internal network. Furthermore, accounting and reporting reform is needed, having in mind ESA standards.

An important segment of the reforms in public finance area is the further implementation of the **Public Internal Financial Control (PIFC)**, according to the EU requirements. In the upcoming period, the system of internal financial control will be implemented to ensure budget funds spending to be in line with the *Budget Law*. Future activities in the area of PIFC will focus on strengthening the managerial responsibility, improving the financial management and further strengthening of internal audit units, in terms of the number of auditors and their professional competence. Risk management is an integral element of an internal control system and should be further developed so that it is implemented systematically across all the public sector.

In the **state aid** area, Montenegro needs to further amend and complement its legislation, to strengthen its administrative capacity and to build up an effective enforcement record. Support to the Government, local self-governments and business associations are needed, having in mind that relaxation of the competition rules in the short term usually only accommodate problems for business while in the long run could undermine development of an open market economy and sustainability of public finances. Montenegrin *Law on Public Procurement* provides an adequate level of alignment with the *acquis*. However, as the EU legislation is undergoing substantial changes, further legislative modifications will be needed. As preparation of the new legislation on Public Private Partnership (PPP) and concessions is ongoing, the support to its implementation will be needed.

In the **external audit** area, Montenegro needs to further improve organizational structure of the State Audit Institution (SAI) focusing on development of professional skills of its audit staff. It is also necessary to enhance audit capacities for performing broad range of audit types, including financial and performance audit work. Montenegro needs to further ensure an efficient mechanism for reporting and monitoring implementation of recommendations of the SAI. Montenegro has put into place institutional arrangements to manage pre-accession funds in indirect mode. However, these new structure have a lack of practical experience, especially in the case of Audit Authority (AA). Thus, to address these challenges the AA require day-to-day access to technical assistance, as well as formalised capacity building tailored to the specific needs of external audit of the use of IPA funds.

RELEVANCE WITH THE IPA II INDICATIVE STRATEGY PAPER (OR MULTI-COUNTRY STRATEGY PAPER) AND OTHER KEY REFERENCES

In the *Indicative Strategy Paper for Montenegro (2014-2020)* (the Strategy Paper) economic governance and public financial management are recognised amongst the main challenges in the sector of democracy and governance. As regards public financial management, the Strategy Paper explains that there is not yet a comprehensive public financial management reform strategy and an action plan (a public financial management reform programme) in place that would cover all relevant sub-systems and sequence reforms accordingly. The overall legal framework for budget management is in place, with plans under preparation to establish a formal Medium-Term Budgetary Framework and to strengthen fiscal rules. While the central capacity for macroeconomic projections is satisfactory, a key concern relates to the weak capacity for budget planning and fiscal analysis in line ministries. Long-term efforts are needed to introduce accrual accounting and budget reporting based on economic, programming and administrative classification. Montenegro also needs to invest in upgrading the IT systems it uses in financial management.

Referring to PIFC, the Strategy Paper indicates that implementation of PIFC is at early stage. Attention needs to be given to improving managerial accountability, improving the quality of financial management and control and prevention of fraud and irregularities. PIFC will also need to be implemented at local level and in the state-owned enterprises. As concerns external audit, the State Audit Institution recently adopted a strategic development plan for its institutional development, but its audit capacity remains limited for implementation of both financial and performance audits. In addition, since some of the public financial management sub-systems are covered under specific accession negotiating chapters (economic and monetary policy, public procurement, public internal financial control, external audit...), there is a need to also address these accession specific aspects.

Montenegro 2013 Progress Report states that, regarding *Economic criteria*, fiscal risks remain high. The fiscal position of the government remains challenged by substantial contingent liabilities and growing debt. Some progress has been made in the area of public procurement (chapter 5). Montenegro is still at an early stage with regard to harmonization with the *acquis* on utilities, concessions, and defence procurement, and needs to strengthen implementation and enforcement capacity at all levels. As for chapter 8 (Competition policy), some progress was made as regards the alignment of the legislative framework with the *acquis*. The independence of the competition authorities, particularly in the state aid field, needs to be demonstrated through the enforcement record, which still needs to be significantly improved. Capacity relating to the formulation economic policy formulation and coordination needs to be strengthened (chapter 17). Further efforts are needed to improve fiscal reporting and to align with ESA standards. Also, in the area of chapter 18 (Statistics), Montenegro has to ensure further investment in a number of statistical areas and full harmonization with the EU's statistical standards and methodologies.

Further progress has been made in the area of financial control (chapter 32). Montenegro needs to further improve the application of the managerial accountability principle. Further strengthening the financial independence and capacity of SAI is also required. Finally, for the chapter 33 (Financial and budgetary provisions), administrative framework for applying the own resources rules needs to be established and the capacity to correctly apply the rules needs to be built up.”

In 2011, the Government of Montenegro adopted the *Public Administration Reform Strategy 2011-2016*, along with the *Framework Plan for its Implementation*, which identifies activities to be undertaken in reforming areas of state administration, local governance and organisations exercising public powers. Related to the state administration, further reform of public finances is envisaged in Chapter 1.2 focusing on stabilisation, control of expenditure and wages, as well as on rationalisation activities. Related to the external audit, further improvement is envisaged in Chapter 1.2.3 focusing on improvement of the legislative framework, strengthening of the professional capacity and implementing measures in the form of promotion of this institution with the aim of recognizing the importance of its role in the wider public.

Additionally, in 2013 the Government of Montenegro adopted the *Plan for the Internal Restructuring of Public Sector*, with the main goal of creating efficient, cost cutting and effective public sector that rests on the best international standards and practice, with specific goal especially focusing on PIFC and midterm budgeting. Also, *Montenegro Development Directions 2013-2016* in the chapter VII – Public Sector Reforms, identified improvement in public finance management as a key priority, while *Montenegro Pre-accession Economic Programme 2013-2016*, in its Chapter III, focuses on fiscal consolidation as well as on improvement of the public finance quality and institutional framework.

Montenegro Development Directions 2013-2016 state that large fiscal deficit and increasing public debt are pointing to the urgency of fiscal adjustment in order for the mid-term forecasts to take place. The main issue in getting public finances on sustainable path is distinctive structural deficit. Without considerable structural changes in public expenditure and revenues, the long term sustainability cannot be assured.

The *Montenegro Pre-accession Economic Programme 2013-2016* states that the priority objective of economic policy in the period 2014-2016 is stabilization and consolidation of public finances, with foreign and domestic investments growth, which will have multiplicative effects on the entire economy, primarily on the sectors of construction, trade, transport and continuation of the process of stabilization of the financial sector.

On 28th June 2012, the Government of Montenegro adopted the *Strategy for Further Development of Public Internal Financial Control System in Montenegro for the Period 2013-2017* with the aim of further development of the established system. The integral part of the strategy is the *Action Plan for Implementation of the Strategy for Further Development of Public Internal Financial Control System 2013-2017 in Montenegro for the period 2013-2014*.

The State Audit Institution adopted the *Strategic Development Plan for 2012-2017* and *Action Plan* for achievement of strategic goals. The main strategic goals and priorities for future development of the SAI are particularly defined in three strategic goals: introduction of new types of audits, audit quality improvement and ensuring quality control of audits; capacity building of the Institution as well as improvement of communication policies.

SECTOR APPROACH ASSESSMENT

Government of Montenegro adopted *Public Administration Reform Strategy for Period 2011-2016* along with the *Action Plan for its Implementation* on the session held on 31st March 2011. The main aim of the

Strategy is the structural adjustment of public administration according to the best EU standards, public administration rationalization, increased efficiency and savings, improved coordination within public administration, openness, availability; strengthening legality of the work of local government bodies, achieving greater level of cooperation between local self-government units as well as between local self-government units and public services established by the state which provide services at the local level; systematic strengthening of public services and organizations exercising public functions.

Having in mind that implemented measures are not sufficient for the sustainability of public finances in short-term and mid-term, as well as that improved public administration efficiency requires analysis of realistic public sector the Government adopted the *Plan for Internal Restructuring of Public Sector* in 2013. This Plan represents the key instrument for further support of the programming, while priorities identified in this sector shall be also linked with those defined in the enlargement agenda.

Along with planned reorganization of public administration special attention will be given to the:

- strengthening of the system of public finances;
- enhancing information society (e-Government);
- strengthening of the EU integration process.

This sector policy is led by the Ministry of Interior, being responsible for the enhancement of the institutional capacity and efficient public administration. The other ministries involved in this public administration reform process are the Ministry of Finance and the Ministry for Information Society and Telecommunications. In Montenegro the functionality of the coordination within the government institutions and with other donors is satisfactory, even though there is room for further improvements within the sector and government level.

It's important to stress out that currently there is no sector budget and the allocations are placed in the budget within the line ministries/institutions. Expenses for IPA co-financing of the Actions will be planned in each consumer unit separately, within the total expenditure.

The *Law on the Budget and Fiscal Responsibility* is adopted by the Parliament and it will provide a base for a medium-term planning, which is the determination of medium-term budgetary framework, as well as with numerical fiscal rules.

LESSONS LEARNED AND LINK TO PREVIOUS FINANCIAL ASSISTANCE

Up to now, the area of the public finance management has not been supported with the comprehensive IPA project that would tackle the different sub-sectors with strategic and coordinated approach. Nevertheless, different sub-sectors have been supported by IPA I funds, as well as by other donors. In the PIFC area, IPA 2009 Project *Strengthening the Management and Control System for EU Financial Assistance in Montenegro* focused on the development of the PIFC in public sector and on strengthening the capacity of the Central Harmonization Unit (CHU) to coordinate the establishment and development of Financial Management Control Manual (FMC) and an internal audit function throughout the public sector. Current IPA 2012 Project *Strengthening the Management of EU Funds and General Administrative Procedures* focuses on internal audit at local level. Regarding other donor activities, the Ministry of Finance, in cooperation with the Centre of Excellence in Finance (CEF) from Ljubljana, with the support of Central European Initiative (CEI), the Government of the Federal Republic of Germany and the Government of the Republic of Slovenia, has been organizing trainings and certification for internal auditors, based on international standards and best practices. In the external audit area, the most relevant for capacity building is the IPA 2009 Project *Strengthening of External Audit in Montenegro* which focused on drafting the *Strategic Development Plan of the SAI from 2012-2017* and *Manual on*

Planning and Performing Financial Audit and Regularity Audit as well on introduction of performance auditing within the organizational structure of the SAI. Implementation of the twinning light contracts *Audit Quality Control in the State Audit Institution of Montenegro* and *Strengthening the Audit Authority of Montenegro* started in 2014.

The state aid part of the Action will build upon the results and achievements of the past actions that were funded by EU. The IPA 2011 project *Strengthening State Aid Management in Montenegro* is ongoing and has the objective to ensure full harmonisation of the system for state aid in Montenegro with the EU *acquis*. Regarding public procurement, IPA 2007 Project *Further Development and Strengthening of the Public Procurement System in Montenegro* had the overall objective to implement the EU internal market requirements in the field of public procurement and to foster efficiency and transparency in the use of public funds. Within the IPA 2009 Project *Enhancing the Public Procurement System in Montenegro*, development of a small software application to complete the current system functionalities was ensured as well as detailed technical specification and a financial plan for an integrated e-procurement system. Moreover, during 2013, SIGMA provided technical assistance to preparation of the Amendments to the Law on Public Procurement.

The Programme *Strengthening Public Finance Capacities in the Western Balkans and Commonwealth of Independent States* funded by Government of Slovakia focused on improving capacities for macro-economic and fiscal analysis and forecasting, preparation of a road map for the ESA 2010 methodology, improving accounting and reporting systems and strengthening capacities for public debt management.

There are a number of generic lessons learnt through previous assistance to institution building in Montenegro. Often, project implementation is hampered by both insufficient staff and/or high turnover of staff, and resources allocated to (newly established) institutions, and sometimes inadequate to them to properly exercise their mandate. Further improvements in the regulatory systems are dependent on the stronger government leadership and the inter-institutional coordination, as well as on finding working operational mechanisms for coordination and harmonisation of policy. The most effective style of work requires a pragmatic and participatory approach. The public administration is relatively small and under considerable workload pressure. Coaching and provision of practical examples as well as exchange of experience is more successful when based on small group discussions on particular issues of current concern. In the previous projects, the key issue appeared to be lack of practical support i.e. orientation to theoretical knowledge without regard to local circumstances.

2. INTERVENTION LOGIC

LOGICAL FRAMEWORK MATRIX

OVERALL OBJECTIVE	OBJECTIVELY VERIFIABLE INDICATORS (OVI)	SOURCES OF VERIFICATION	
To ensure fiscal sustainability and sound management of public finances in line with EU requirements	Government effectiveness	World Bank	
SPECIFIC OBJECTIVE	OBJECTIVELY VERIFIABLE INDICATORS (OVI)	SOURCES OF VERIFICATION	ASSUMPTIONS
To improve efficiency, effectiveness and transparency of the public finance management (PFM)	<p>Significant improvement in the PEFA or similar external assessment rating</p> <p>Steady progress at accession negotiation on related chapters number 5, 8, 17, 18, 32 and 33</p>	<p>PEFA or other similar assessment report</p> <p>Government reports on negotiations</p>	Stable external environment and economic recovery (positive trend)
RESULTS	OBJECTIVELY VERIFIABLE INDICATORS (OVI)	SOURCES OF VERIFICATION	ASSUMPTIONS
<p>R1: Improved budget system based on transparent programme structure, clear policy objectives and performance indicators to provide solid basis for further fiscal reforms</p> <p>R2: Improved transparency and accountability of decision making as regards PFM</p> <p>R3: Key PFM policies – state aid, concessions and public procurement, improved as regards legislation, institutional set-up and capacities</p> <p>R4: Strengthened external audit performed by State Audit Institution and the Audit Authority</p>	<p>Programme-based budget introduced</p> <p>PIFC Strategy and its AP implemented in line with applicable timetables</p> <p>Improvement of the structure of granted state aid</p> <p>Increased competition in public procurement procedures and concessions award procedures</p> <p>Improved coverage of the external audit function</p> <p>Application of international audit standards in the external audit both at the SAI and AA</p>	<p>EC Progress Report</p> <p>Reports to the Government and to the EC</p> <p>Official Gazette of Montenegro</p> <p>Report on implementation of programme budgeting</p> <p>Consolidated Report on PIFC in Montenegro</p> <p>Annual report on granted state aid</p> <p>State aid enforcement record (inventory)</p> <p>De-minimis database within SACU.</p> <p>Annual report on public procurement</p> <p>SAI's Annual Report</p> <p>Audit Reports submitted to the Parliament of Montenegro</p> <p>Audit Reports published at the official web site of the SAI</p> <p>AA Reports</p>	<p>Commitment and good and continuous interaction of stakeholders</p> <p>Strong inter-ministerial co-operation and understanding of the importance to prioritize the fields of future action in such horizontal and multidisciplinary domains</p> <p>Continued commitment and good interaction of SAI and Parliament</p> <p>Improvement in the accounting system and IT applications used in the PFM</p> <p>Training of the accountants and financial managers across the administration</p>

ACTIVITIES	MEANS	OVERALL COST	ASSUMPTIONS
<p>R1 - A1: Amending the national legislation to allow programme-based budgeting and medium term budgetary framework based on analysis of the best EU practice;</p> <p>R1 - A2: Introduce programme-based budgeting;</p> <p>R1 - A3: Strengthen institutional capacities for macro-economic and fiscal programming, as well as for economic analysis;</p> <p>R1 - A4: Asses functionalities of the current information system for budget planning and centralized calculation of earnings, define and implement the necessary upgrades to allow sound financial data on the whole budget cycle;</p> <p>R1 - A5: Streamline requirements for sector level and medium term planning;</p> <p>R1 - A6: Implement gradual transition to modified cash to accrual accounting in the public sector;</p> <p>R1 - A7: Prepare Business Continuity Plan of the MoF;</p> <p>R1 - A8: Assessment of the training needs and delivery of trainings for all spending units and the local governments.</p> <p>R2 - A1: Review of managerial accountability, formulate and implement recommendations for improving the delegation of responsibility across public sector;</p> <p>R2 - A2: Redefinition of processes and delegation lines in the ministries to enhance the concept of managerial accountability;</p> <p>R2 - A3: Establishing risk management system at central and local level;</p> <p>R2 - A4: Developing appropriate quality assurance and indicators for financial management and control.</p> <p>R3 - A1: Comprehensive analysis of national legal framework and enforcement practices, development of recommendations for changes and preparation of required amendments for key sectors with high impact on public finances – state aid, concessions, PPP and public procurement (and others if deemed necessary);</p> <p>R3 - A2: Support for improving the state aid policy through 1) development of the Action Plan for opening/closing of negotiations on state aid; 2) Building the capacity of the SACU and SACC for control over state aid via training on SA case law, economics and procedures, daily support on enforcement of state aid legislation, identification of non-notified aid and implementation of regular <i>ex-post</i> control, as well as support for the establishment of transparent and reliable</p>	Service	EUR 4 000 000	<p>Development of a PFM Reform Strategy</p> <p>Ensured surveillance mechanism over PFM reform</p> <p>Government and Parliament readiness to revise and adopt new legislation harmonised with the EU</p> <p>Enough absorption capacity for the planned TA activities.</p> <p>Fluctuation of trained staff is limited.</p>

<p>operational de-minimis database; 3) Methodological support to the SA grantors to introduce measures to support development of economic activities in line with state aid rules; 4) Trainings for grantors, private sector representatives and judges;</p> <p>R3 - A3: Support for the implementation of the new EU rules on PPP/concessions: 1) training of concession grantors, 2) development of adequate procedures for the attribution of concessions, 3) establishment of monitoring system for implementation of the concession contracts;</p> <p>R3 - A4: 1) Support for the implementation of the new public procurement law for classical sector, utilities and defence procurement, 2) support for monitoring of the public procurement through training to procurement officers and businesses and development of manuals and procedures;</p> <p>R3 - A5: Raising awareness on key policies linked to public finance.</p> <p>R4 - A1: Standardization of the audit process for financial and performance audit aligned with ISSAI standards;</p> <p>R4 - A2: Improving the audit capacity of SAI through: 1) Assessment of training needs, preparation and implementation of HRD and Training Programme, focusing on conducting performance audit; 2) support in horizontal development functions within sectors; 3) Drafting and testing guidelines on conducting performance audit and final budget accounts, as well as updating and testing the Manual on planning and performing financial audit and regularity audit; 4) Drafting Communication Strategy that focusing on enhancement of relations with the Parliament; 5) Drafting internal guidelines for monitoring realization of the recommendations from the audit reports;</p> <p>R4 - A3: Assistance to the AA in implementation of IPA: 1) Assess training needs, develop and implement training programme for the auditors; 2) Improve the audit manual for different types of audits according to the international audit standards; 3) Improve the capacity to apply specific audit techniques; 4) Development of AA strategic plan and Action Plan for its implementation; 5) Introduction of quality assurance.</p>			
---	--	--	--

ADDITIONAL DESCRIPTION

The overall objective of the Action is to ensure fiscal sustainability respecting numerical fiscal rules introduced in accordance with the legislation. The specific objective is to improve public finance management policies in order to ensure efficiency, effectiveness and transparency in public finance. The Action is organised around 4 axes corresponding to key processes in the management of public finance:

1. Budgetary system. The activities are planned in order to ensure a complete implementation of **the programme budgeting** that will contribute to improve strategic management practices and enable more efficient allocation and consumption of public resources. The Action will analyse the best practices and experiences in programme budgeting within the member states, as well as the current regulation and procedures in Montenegro. Based on this analysis, the proposals for necessary amendments to the national legislation will be made in order to support full development and implementation of the programme budgeting. The Action will support preparation of the National Action Plan for implementation of the programme budgeting system, programme budgeting manual and improvement of the current budget circular resulting in comprehensiveness of the budget programming and the use of the latest Information Technology (IT). Based on the analysis of the current programme structure, the relevant changes will be proposed along with the identification of performance indicators for programmes and sub-programmes that would be used for monitoring the implementation and meeting the targets, objectives and task of the programmes/sub-programmes. The Action will support analysis of the best practices of the EU in implementing medium term budgetary framework and amendments of current legislation and procedures to meet the requirements set by the *acquis*.

Additionally, functionalities of the current IT system for budget planning (Budget Management System) will be assessed and the necessary upgrades implemented. Upgrade of the IT system for budget planning would be based on improving functionalities of the system, as well as connecting the system to other IT systems in place (SAP system for budget execution) that would allow the use of the databases and better control of the spending. Furthermore, completion of the IT system for the Centralized Calculation of Earnings is required. Preparation of the Business Continuity Plan of the MoF (planning and preparation of the procedures in case of any risk and changed business conditions as well as the procedures for returning to normal situation) is also envisaged.

The Action will support the implementation of the strategy for the transition from the public sector to accrual accounting and trainings for the staff of Ministry of Finance as well as trainings for accountants in the consumer units and the local governments.

2. Public Internal Financial Control (PIFC) with a specific focus on improving the transparency and accountability of decision making as regards PFM

The Government of Montenegro updated the *Action Plan (AP) for Implementation of the Strategy for Further Development of Public Internal Financial Control System 2013-2017*, in order to put emphasis on activities that will contribute to the strengthening of **managerial accountability** and the framework for the delegation of responsibilities, as key activities of the process for improving the management of public funds in Montenegro. In order to implement the AP, the assistance is needed in reviewing existing practices. The aim of the Action is to develop the system for delegation of authority and power across public sector bodies and strengthen capacities, especially of the finance departments in order to support managerial accountability. Regarding **the risk management**, the Action will result in establishing the risk assessment in budget proposals and key planning documents and analysing the risk management practices after the first cycle of implementation. The Action will also focus on developing of appropriate quality assurance and indicators for financial management and control.

3. Key polices with significant impact on public finance and in particular state aid, public procurement and Public Private Partnership (PPP) /concessions, which are important for the health of the public finances, fight against corruption and application of the EU rules as regards single market.

The Action will focus on introducing improvements as regards legislation, institutional set-up and administrative capacities. The planned activities combine improvement of the institutional set-up and legal framework for **state aid** control that will ensure strong institutional mandate for enforcement of rules in accordance with EU practices. The comprehensive analysis of national legal framework will be performed regarding rights and powers of State Aid Control Commission - SACC and State Aid Control Unit - SACU. It will also include the assessment of the enforcement practices of the existing legislation. Subsequently, recommendations will be developed aiming at changes in legislation and administrative practices, leading to preparation of required amendments of state aid legislation. If needed, support will be provided for the process of the negotiations in Chapter 8 - Competition policy, which might include the development of relevant Action Plans for opening/closing of negotiations. Daily advisory and training for the SACU and SACC will be provided for enforcing the state aid legislation, as well as case law and procedures. Additionally, support will be given for identifying non-notified aid (unlawful state aid) and implementing regular *ex-post* control of aid measures approved/rejected by the SACC, including opening state aid investigation procedures. Furthermore, the Action is going to support the establishment of a transparent, reliable and operational de-minimis database. The Action will provide methodological support to the State Aid (SA) grantors (central and local level) for introducing measures for developing economic activities in line with state aid rules (focus on horizontal vs. ad-hoc SA). Likewise, the training and raising awareness events on state aid issues for grantors (central and local level), private sector representatives and judges will be organised. A special focus will be given on provision of methodological support to draft changes in proposed SA schemes in order to align non-compliant state aid measures with applicable SA rules.

The Action will support implementation of the EU rules on concessions/PPP and public procurement. This will inter alia include: training to concession grantors, development of adequate procedures for the attribution of concessions, establishment of a system for monitoring over the implementation of the concession contracts, support to monitoring of the public procurement through training to procurement officers and business, development of manuals and procedures, etc.

4. External audit. The Action will strengthen the external audit, performed by State Audit Institution (SAI) and the Audit Authority (AA).

The development and strengthening of the **SAI** is based on strategic development plan. Future activities will be focused on strengthening of the human resources management in the SAI and improving the professional skills of audit staff. Activities will include the strengthening of audit capacities to perform different types of audits, especially financial and performance audit, aligned with International Standards of Supreme Audit Institutions (ISSAI) standards. The support will be additionally provided for development of the horizontal functions within the sectors (legal department, methodological department for legislature and standardization). The Action will draft guidelines on conducting performance and final budget accounts audit. Throughout duration of the Action, testing of guidelines will be completed. At least one pilot audit (on-the-job training) will be completed yearly, both for performance audit and final budget accounts audit. The Action will assist the SAI in updating the Manual on planning and performing financial and regularity audit. The updated Manual will be tested on at least one financial audit (on the job training) yearly, throughout duration of the Action. Application of audit methodology and manuals for different types of audits will provide a sound foundation for co-ordinated programme of institution-building and capacity-strengthening. The Action will be also focused on enhancing the communication policies with the Parliament when monitoring the realization of recommendations given in the audit reports. Hence, the Action will provide support in drafting internal guidelines for monitoring.

Additionally, the activities will contribute to strengthening the capacities of the **AA** to implement IPA requirements. Also, the Action will provide a training programme, including on-the-job trainings for auditors, as well as internship opportunity. Other activities will be focused on drafting and testing the necessary procedures for different types of audits, followed by their monitoring and reporting. During the Action, the implementation of specific audit techniques will be completed (analytical procedures, sampling, control evaluation etc.). Furthermore, the supervision of pilot audits will be performed in order to assess the compliance of pilot audits in each phase with the respective audit procedures, best practices, as well as the preparation of the corresponding reports.

3. IMPLEMENTATION ARRANGEMENTS

ROLES AND RESPONSIBILITIES

The main beneficiaries of the Action will be the Ministry of Finance, the Audit Authority (AA) and the State Audit Institution (SAI).

The Directorate for Finance and Contracting of the EU Assistance Funds (CFCU) being the Implementing Agency under IPA bears the sole responsibility for the proper implementation of all contracts in line with the relevant contractual provisions and the requirements governing the indirect management of EU assistance. The Project Implementation Unit (PIU) of the Ministry of Finance will provide support to the CFCU whereby ensuring the proper technical implementation of the contract activities. In this regard, the CFCU and the PIU will closely cooperate throughout the contracts implementation process.

Implementation monitoring will be performed in order to obtain information on progress achieved and collect data required to prepare relevant reports for the National IPA Coordinator (NIPAC) Office and the CFCU, provide advices and contribute to tackling any problems and possible mistakes which could endanger the successful completion of the implementation. The major tools of the PIU for performing monitoring are: monitoring visits, participation in the regular progress meetings, participation in the Steering committees meetings, review of regular progress reports and participation at on-the-spot checks, carried out by the CFCU.

A Steering Committee (SC) will be established to review the Action progress. It will comprise of representatives of PIU of the Ministry of Finance, beneficiary institutions, NIPAC Office and the EUD. The SC may invite other organisations to attend meetings in cases where this will bring added value to discussion, direction and outcomes of the Action. Representatives of the other key stakeholders may also be invited to attend SC meetings.

IMPLEMENTATION METHOD(S) AND TYPE(S) OF FINANCING

The activities will be achieved through procurement of a service contract. The national co-financing will be provided jointly with the EU funds by the beneficiary of the Action i.e. Ministry of Finance, AA and SAI.

4. PERFORMANCE MEASUREMENT

METHODOLOGY FOR MONITORING (AND EVALUATION)

Monitoring and evaluation of the implementation of this Action will be conducted in accordance with the rules of indirect management and respecting the requirements and provisions of IPA II regulations and those that will be laid down in Framework Agreement and in respective Financing Agreement. Achieving of the Action results will be regularly monitored by the responsible national implementing body and National IPA Coordinator.

Implementation of this Action will be subject of special attention of Sectoral Monitoring Committee and IPA Monitoring Committee which shall measure progress in relation to achieving the objectives of the actions and their expected outputs, results and impact by means of indicators related to a baseline situation, as well as progress with regard to financial execution. The sectoral monitoring committee will report to the IPA Monitoring Committee and will make proposals on any corrective action to ensure the achievement of the objectives of the Action and enhance its efficiency, effectiveness, impact and sustainability.

Moreover, in accordance with Article 8 of Commission Implementing Regulation (EU) no 447/2014 NIPAC shall take measures to ensure that the objectives set out in the Action are appropriately addressed during the implementation of EU assistance. Procedures for implementing monitoring activities will be set out in the revised Manuals of Procedures aligned with new IPA regulations. Best practices from the monitoring of implementation of previous actions and recommendations given by external monitoring in this sector will be also taken into consideration.

This Action shall be subject to evaluations, in accordance with Article 30(4) of Regulation (EU, EURATOM) No 966/2012 and with Article 22 of Commission Implementing Regulation (EU) no 447/2014. The results of evaluations shall be taken into account by the IPA Monitoring Committee and the Sectoral Monitoring Committee.

INDICATOR MEASUREMENT

INDICATOR	DESCRIPTION	BASELINE (2010)	LAST (2013)	MILESTONE 2017	TARGET 2020	SOURCE OF INFORMATION
OVERALL OBJECTIVE INDICATOR Government effectiveness	This indicator measures the quality of public services, the quality of the civil service and its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to its stated policies	57.4	55.45	60.33-60.61	60.72 - 61.21	World Bank
ACTION OUTCOME INDICATOR 1 Significant improvement in the PEFA or similar external assessment rating	The purpose of the assessments is to provide the Montenegrin authorities with an internationally-recognized evaluation of the current performance of the Montenegrin PFM systems. In the absence of a PEFA report in 2018-2020 or in case of incompatibility of data due to modifications in PEFA methodology, other similar assessment reports will be used.	Overall rating PEFA 2008	Overall Rating PEFA 2013	Improvement in the 2013 ratings in at least 10% of the PEFA indicators	Improvement in the 2013 ratings in at least 20% of the PEFA indicators	PEFA or other similar assessment report
ACTION OUTCOME INDICATOR 2 Steady progress at accession negotiation on related chapters number 5, 8, 17, 18, 32 and 33	Number of the closing benchmarks considered met in the relevant negotiations chapters	0	0	25% of the closing benchmarks implemented	100% of the closing benchmarks implemented	Government reports on negotiations
ACTION OUTPUT INDICATOR 1 Programme-based budget introduced	Degree of implementation of programme-based budgeting	Overall structure is in place since 2008, the system has not been fully developed	Programme based budget not developed	Programme based budget developed	Programme-based budget in place	EC Progress Report Reports to the Government and to the EC Official Gazette of Montenegro Report on implementation of programme budgeting
ACTION OUTPUT INDICATOR 2 PIFC Strategy and its AP implemented in line with applicable timetables	On 28 June 2012, the Government of Montenegro adopted the Strategy for Further Development of Public Internal Financial Control System in Montenegro for the period 2013 - 2017 with the aim of further development of the established system.	16 institutions covered with internal audit	65 institutions covered with internal audit	87% institutions covered with internal audit	97% institutions covered with internal audit	EC Progress Report Reports to the Government and to the EC SAI Reports Official Gazette of Montenegro Consolidated report on PIFC in Montenegro

INDICATOR	DESCRIPTION	BASELINE (2010)	LAST (2013)	MILESTONE 2017	TARGET 2020	SOURCE OF INFORMATION
ACTION OUTPUT INDICATOR 3 Improvement of the structure of granted state aid	Increase in the share of state aid granted under schemes for horizontal state aid objectives by SA grantors (central and local level) that support development of economic activities in Montenegro and decrease of aid for restructuring	3%	4.8%	Increase by at least 20% of the horizontal state aid at the cost of other state aid	Increase by at least 20% of the horizontal state aid at the cost of other state aid	Annual report on granted state aid State aid enforcement record (inventory) De-minimis data base within SACU
ACTION OUTPUT INDICATOR 4 Increased competition in public procurement procedures and concessions award procedures	Increase in the competition rate on the public procurement market – % change in the number of bids per tender	0	3,1 bids per tender	5% increase in the No of bids per tender	10% increase in the No of bids per tender	EC Progress reports Annual report on public procurement
ACTION OUTPUT INDICATOR 5 Improved coverage of the external audit function	Number of audits performed by SAI and AA and increased share of state funds covered by the external audit function	SAI – 14 AA – N/A	SAI - 16 AA - N/A	Increase by at least 5% of the number of conducted audits	Increase by at least 10% of the No of conducted audits At least 60% of the state funds covered by external audit (SAI) At least 75% of the EU funds subject to external audit (AA)	SAI's Annual Report Audit Reports submitted to the Parliament of Montenegro Audit Reports published at the official web site of the SAI AA Reports
ACTION OUTPUT INDICATOR 6 Application of international audit standards in the external audit both at the SAI and AA	Developing audit manuals and performing audits in compliance with international audit standards and strengthening audit staff to perform different types of audits (SAI and AA)	0%	0%	5% increase of the share of performance audits (SAI) Quality assurance plans established and a mechanism in place for detecting non-compliance with international standards	10% increase of the share of performance audits (SAI) At least 30 trained audit staff (SAI) Decreasing trend of in compliance reports	SAI's Annual Report AA Reports EC Progress Report

5. CROSS-CUTTING ISSUES

ENVIRONMENT AND CLIMATE CHANGE (AND IF RELEVANT DISASTER RESILIENCE)

Environment protection legislation in Montenegro is comprehensive and it is going through an intensive process of harmonisation with the EU *acquis*. The proposed Action will give attention to environmental issues. Action aims to support State Aid (SA) grantors (central and local level), to focus the new SA measures on horizontal objectives vs. ad-hoc SA, which interprets the use of EU environmental SA rules, in order to facilitate a setting-up of a cleaner business environment in Montenegro. Also, the Action will include increased use of electronic means, reduction in paper consumption (recto/verso prints) etc.

ENGAGEMENT WITH CIVIL SOCIETY (AND IF RELEVANT OTHER NON-STATE STAKEHOLDERS)

The various coordination mechanisms for external assistance, particularly the sector-based coordination group, have ensured that all the central-level stakeholders have been consulted on this Action. Likewise, all the primary stakeholders have been consulted in the formulation of the intervention and will participate in the implementation of the both, as direct beneficiaries and as members of the Steering Committee (SC). The views of civil society will be sought during the implementation of the Action. Beside civil society, the Action supports the accessibility of other stakeholders such as media, local authorities and institutions and research centres. In this manner, the Action would contribute to the creation of contacts at different levels and sectors of activities, while building long term partnerships and networking among the above mentioned stakeholders.

EQUAL OPPORTUNITIES AND GENDER MAINSTREAMING

There is extensive equal opportunity legislation in Montenegro. The proposed Action will ensure that the internal policies, structures or operating procedures of the beneficiary institutions conform with the rules and promote equal opportunity. In supporting legislative harmonisation and further institutional and administrative capacity building, gender needs will be taken into consideration and provisions that enhance equal opportunities will be introduced. All of the planned activities will respect the principles of equal treatment and opportunities for women, especially trainings and raising awareness events.

MINORITIES AND VULNERABLE GROUPS

Special attention to minorities and vulnerable groups will be integral part of any activity of the Action. Being the multiethnic society, Montenegro is committed to preserve the culture, history, language and religion of their national minorities and of the majority. Thus, the beneficiary institutions will implement mechanisms to ensure that in the legislative process, the internal policies, structures or operating procedures, the principle of equitable representation of ethnic minorities and the protection of their rights is taken into consideration.

6. SUSTAINABILITY

The Action will have a positive impact on the capacity of both public administration and external stakeholders, which will secure long-term sustainability of the Action. The sustainability of the Action will further be addressed through the adoption of legislation aligned with the EU *acquis*, which create the framework needed for further success in accession process. Tools for achieving sustainability are training of the officials and other stakeholders, strong awareness-raising measures at both central and local level (public and private partners and general public) and enriched links between Montenegrin and EU institutions.

7. COMMUNICATION AND VISIBILITY

Communication and visibility will be given high importance during the implementation of the Action.

The implementation of the communication activities shall be the responsibility of the beneficiary, and shall be funded from the amounts allocated to the Action.

All necessary measures will be taken to publicise the fact that the Action has received funding from the EU in line with the Communication and Visibility Manual for EU External Actions.

The use of *Communication and Visibility Manual for EU External Actions* is compulsory. The contractor shall use the appropriate stationery in letterheads or fax headers sheets and report presentation format, but should add the phrase “*This Action/programme is funded by the European Union*” as well as the EU flag when relevant. Elements of the communication strategy may include: press release, press conferences, leaflets and/or brochures, newsletters, web pages, vehicle panels, promotional items, reports, audio-visual productions. Any supplies or equipment delivered under an EU-funded Action must be clearly identified and must visibly carry the EU logo and the mention “*Provided by the support of the EU*” in the operational language of the EU programme and in the local language.

Visibility and communication actions shall demonstrate how the intervention contributes to the agreed programme objectives and the accession process. Actions shall be aimed at strengthening general public awareness and support of interventions financed and the objectives pursued. The actions shall aim at highlighting to the relevant target audiences the added value and impact of the EU's interventions. Visibility actions should also promote transparency and accountability on the use of funds.

It is the responsibility of the beneficiary to keep the EU Delegation fully informed of the planning and implementation of the specific visibility and communication activities.

The beneficiary shall report on its visibility and communication actions in the report submitted to the IPA Monitoring Committee and the Sectoral Monitoring Committees.