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ANNEX B

Annual Action Programme for Montenegro for the year 2019

1 IDENTIFICATION

Beneficiary	Montenegro
Basic act: CRIS/ABAC Commitment references and budget line(s):	Instrument for Pre-accession Assistance (IPA-II) 2019/041-168 EUR 1 715 000 from 22.02 01 01 2019/041-169 EUR 28 300 000 from 22.02 01 02
Total cost:	EUR 30 015 000
EU Contribution:	EUR 30 015 000
Method of implementation	<p><u>Direct management by the European Commission for:</u></p> <ul style="list-style-type: none"> • <i>Action 1 – EU Integration Facility</i> • <i>Action 2 - Support to COVID-19 crisis response in Montenegro (Budget Support)</i> <p>Direct management by the European Commission for all activities, with the exception of one complementary support activity.</p> <p>Indirect management with the International Labour Organization (ILO) for a complementary activity under action 2 - <i>Support to COVID-19 crisis response in Montenegro</i></p> <ul style="list-style-type: none"> •
<u>Final date for concluding Financing Agreement(s) with the IPA II beneficiary</u>	At the latest by 15 November 2020
Final date for contracting, including the conclusion of contribution/delegation agreements	Three years following the date of conclusion of the Financing Agreement
Indicative operational implementation period	Six years following the date of conclusion of the Financing Agreement.
Final date for implementing the Financing Agreement (date by which this programme should be de-committed and closed)	12 years following the conclusion of the Financing Agreement.

2 DESCRIPTION OF THE ACTION PROGRAMME

2.1 SECTORS SELECTED UNDER THIS ACTION PROGRAMME

- Rationale for the selection of the specific sectors under this programme:

The *Annual Action Programme (AAP) for Montenegro for the year 2014* contributed to the achievement of the objectives identified in the Indicative Strategy Paper 2014-2020 (ISP) of Montenegro and its subsequent revision through actions covering six of the eight priorities defined in the ISP. The first sectors initially covered by IPA II funds included *democracy and governance, the rule of law and fundamental rights, environment and climate action, transport, competitiveness and innovation, and the Agriculture and rural development* sector.

The *Annual Action Programme for Montenegro for the year 2015* covered *Democracy and governance* and the *Rule of law and fundamental rights* sectors. It also included the first sector budget support programme aimed at supporting the implementation of the integrated border management strategy.

In 2015, Montenegro developed a *Regional Development Operational Programme 2016-2020 (RDOP)* to provide a multiannual framework for IPA programming in *environment, competitiveness and transport* sectors. Two actions, focusing on economic development and growth by providing assistance to the Environment and climate action and Competitiveness and innovation sectors, were included in the *Action Programme for the year 2016*. A third action aiming at the improvement and development of the transport sector was included in part 1 of the *Annual Action Programme for Montenegro for the year 2017*.

The *Annual Action Programme for Montenegro for the year 2017* part 2 strengthened and complemented the existing EU support to the democracy and governance sector targeting the area of public administration reform (PAR), which is one of the key priorities of the Enlargement Strategy.

In 2018, the *Annual Action Programme for Montenegro* addressed issues concerning the Democracy and Governance, Rule of Law and Fundamental Rights and Competitiveness and Innovation, Agriculture and Rural Development. In addition, the AAP 2018 included an action funded under the performance reward granted to Montenegro in the area of Education, Employment and Social Policies focusing in the area of Health.

The current Annual Action Programme for Montenegro for the year 2019 (AAP 2019) focuses on two sectors: Democracy and Governance, and Education, employment and social policies.

Under the **Democracy and Governance sector**, the AAP 2019 will set up a new EU Integration Facility (EUIF) with EUR 1 715 000 EU contribution. The EU Integration Facility focuses mainly on technical support and capacity building related to the EU accession process. By ensuring the effectiveness and impact of actions financed through IPA II, the EUIF will also help the preparation for future cohesion and structural funds. In addition, special attention will be granted to ensuring good communication and visibility of EU actions in specific sectors as well as performing programme evaluations that will inform and steer preparation of future IPA III programmes.

Within Education, employment and social policies sector, EUR 28 300 000 is allocated for Support to COVID-19 crisis response in Montenegro, following the outbreak of worldwide COVID 19 pandemic.

- Overview of past and on-going EU, other donors' and/or IPA II beneficiary's actions in the relevant sector: **Education, employment and social policies**
- Within the Response to the COVID-19 crisis, in order to mitigate the impact of the COVID-19 pandemic and crisis in Montenegro, a large-scale and all-encompassing budget support programme, worth EUR 40.5 million EU contribution has been identified as the most effective and efficient intervention to help Montenegro reduce the macro-economic effects of the crisis on the economy, preserve vulnerable social groups from the disruptive effects of the crisis and guarantee their continued access to basic social services and increase access of vulnerable business to economic relief.
- In the EU response to the crisis, synergies are sought between this programme and the following operations, either already provided or planned, also in conjunction with other donors:
- Montenegro has requested an emergency financial support from the **European Macro Financial Assistance (MFA)**, up to EUR 60 million. MFA is an EU crisis response instrument linked to the emergency Rapid Financing Instrument of the International Monetary Fund (IMF). The objective of this assistance is to ease the country's external financing constraints, alleviate its balance of payments and budgetary needs, strengthen its foreign exchange reserve position and help the country address the current external and financial vulnerabilities. The MFA is available for 12 months period and disbursed in two instalments of up to EUR 30 million each. The policy conditions attached to this assistance will be based on the economic stabilisation and reform programme endorsed by the Montenegrin authorities and consistent with agreements reached by Montenegro with the IMF. The process of agreeing upon a Memorandum of Understanding and setting the MFA conditionality is ongoing.
- **SOPEES programme** (National IPA 2020, EUR 3.5 million): the programme aims at enhancing inclusion and employability of the long-term unemployed, with the focus on social welfare beneficiaries, women, youth, by supporting life in the community and through local partnerships initiatives for employment.
- **Improvement of Budgeting System, Multi-annual Budget Framework and Public Internal Financial Control System (National IPA 2014, EUR 1.3 million)**: the project aims to increase fiscal sustainability and sound management of public finances in line with EU requirements. The specific objectives of the contract are: a) the full implementation of a medium-term budget framework, b) the full development and implementation of a program budgeting based system and c) the improvement of Public Internal Financial Control system. The contract will include complementary activities to support the transition to accrual accounting, to improve the quality of budget documents and for the establishment of a system of prevention and recovery from potential threats to business continuity.

- **Development and strengthening of the capacities of State Audit Institution and Audit Authority (National IPA 2014, EUR 0.6 million):** the project aims to further strengthening public sector external audit in Montenegro by providing support to Audit Authority (AA) and State Audit Institution (SAI). This includes strategic advice, improvements of operational manuals and procedures for different type of audit including usage of ad hoc IT tools, trainings, on the job assistance and strengthening relationships with the parliament.
- **Support to strengthening health systems and vulnerable groups (EUR 20 million IPA multicountry):** 1. New interventions to support needs of vulnerable groups, especially elderly and children; 2. Interventions to improve the resilience of health systems, by intensifying existing work through the European Centre for Disease Prevention and Control, as well as a new engagement with the WHO.
- **Economic Reactivation Package (EUR 455 million, IPA multicountry):** The interventions will support the economy recover and inject much needed liquidity to financial intermediaries and small and medium enterprises (SMEs) in the region through work with the IFIs (EUR 202 million reorientation of existing programmes, plus “new funding” including: EUR 95 million reprogrammed IPA funds, EUR 38 million of the IPA 2020 programme adapted to COVID-19, and EUR 120 million of the Western Balkans Guarantee reoriented to mitigate the socio-economic consequences of the pandemic).
- In addition, a package of **emergency support measures dedicated to Western Balkan Countries** has being discussed, to be implemented by the European Investment Bank (EIB), in the amount of EUR 700 million. Funds will be granted, if requested, primarily to help the health sector, small and medium-sized enterprises and entrepreneurs to overcome the liquidity problems caused by the pandemic crisis. The assistance will also include the expertise of the EIB together with partner banks in the countries. The definition of needs and priorities is ongoing.
- In the response of the international community, close coordination will be ensured between the EU and the following entities and projects:
- **The Rapid Financing Instrument (RFI) (IMF, EUR 30 million)** provides rapid and low-access financial assistance to its member countries facing an urgent balance of payments need, without the need to have a full-fledged program in place. It can provide support to meet a broad range of urgent needs, including those arising from commodity price shocks, natural disasters, conflict and post-conflict situations, and emergencies resulting from fragility. Financial assistance under the RFI is provided in the form of outright purchases without the need for a full-fledged program or reviews. Montenegro requested RFI assistance in April, and the procedures for its approval is ongoing.
- **Second Fiscal and Financial Sector Resilience Policy-Based Guarantee** (World Bank, EUR 80 million) was used for the execution of EUR 250 million syndicated loan in May from commercial banks. The 12-year loan has been withdrawn in mid-May, with a 3.63% interest rate. Its release was conditioned to the implementation of governmental reforms to safeguard fiscal sustainability and make the financial sector more resilient to potential shocks. The WB is considering to increase the guarantee of additional EUR 25 million with the aim to further ease the COVID-19-related pressure on the public finances.

- **Support to the reform of the system for determination of disabilities (the UN Development Programme (UNDP), EUR 1 million EU support):** the purpose of this action is to rationalise the way the National Disability Determination System is conducted in Montenegro, as to facilitate access to the adequate services to the right users. The foreseen result will be the establishment of a functional national disability determination system. This area has been identified by the EU as a gap in the overall governmental programme dealing with the social card system.
- **Gender Programme (UNDP, EUR 0.735 million EU support):** the project focuses on 3 areas of gender equality: economic empowerment of women, fight against gender based violence and political participation of women. The activities include training of around 150 women in entrepreneurship in Podgorica and Nicksic, with the development of business plans. In addition, 16 municipalities allocated budget lines for women entrepreneurship (EUR 120 000).
- **Protection of children from violence (the UN's Children's Fund UNICEF, EUR 0.3 million EU support):** the project aims at providing quality prevention and protection services so that children are effectively protected from all forms of violence and exploitation. Its specific objective is to strengthen the capacities of social and child protection, health, education, police, and justice professionals to prevent and protect children from violence and to enhance inter-sectoral collaboration so that children are provided with high quality, multi-sectoral support. Activities include the *improvement of the case management system* and *training for case managers* who work with children who were exposed to violence;
- The project **Early Childhood Development (ECD) in Montenegro (UNICEF, EUR 1 million EU support)** aims to support the improvement of health and development of children up to 6 years of age, including children with disabilities, in order to reach their full potential. Its specific aim is to ensure that young children, especially the most vulnerable, and their parents/caregivers benefit from quality, equitable, mutually reinforcing systems of health, education, social and child protection. In addition, the action will support the development of the first national ECD policy, with a costed Action Plan and a clear monitoring and evaluation framework. Start date: 1 August 2020.
- **Supporting Entrepreneurship through Advanced Advisory and Information Services for SMEs (the European Bank for Reconstruction and Development (EBRD), EUR 1.4 million (EU support):** the project aims to enhance the business environment and competitiveness of the private sector of Montenegro, by providing direct advisory assistance for SME and by supporting the development of the Single Access Point for business information.

List of Actions foreseen under the selected Sectors/Priorities:

Sector/Priority/Action	Direct management [EUR]	Indirect management	
		With entrusted entity [EUR]	With IPA II beneficiary [EUR]
Democracy and Governance			

EU Integration Facility	1 715 000	0	0
Education, employment and social policies			
Support to COVID-19 crisis response in Montenegro	28 100 000	200 000	0
TOTAL	29 815 000	200 000	0

2.2 DESCRIPTION AND IMPLEMENTATION OF THE ACTIONS

The envisaged assistance is deemed to follow the conditions and procedures set out by the restrictive measures adopted pursuant to Article 215 TFEU¹.

SECTOR	Democracy and Governance	EUR 1 715 000
Action 1	EU Integration Facility	EUR 1 715 000

(1) Description of the Action, objectives, expected results and key performance indicators

- Description of the action and objectives

This action will provide effective and efficient response to emerging priorities linked to the EU accession process as well as to improve the quality and maturity of planning and programming documents and to support effective implementation and visibility of EU assistance.

This action focuses mainly on technical support and capacity building related to the EU accession process and it should ensure adequate visibility, effectiveness and impact of actions financed through IPA II. The EU Integration Facility provides flexible support to the national authorities aimed at addressing specific needs identified in the course of the implementation of IPA II, but it may also be used in ad-hoc circumstances where EU assistance is required and/or suggested.

The *objective* of the action is to support Montenegro in the successful conducting of the EU accession process, including compliance with cohesion and structural funds related rules and standards.

- Expected results and key performance indicators

The *expected results* of this action are:

- R1: Legislative and institutional capacities of Montenegrin administration for transposition and implementation of the EU *acquis* and capacities for leading and carrying out the accession negotiations strengthened.
- R2: Capacities and relevant documentation for identification, programming, implementation, visibility and evaluation of EU assistance developed.

The achievement of the results envisaged by the action will be measured by the following *indicators*:

- Number of projects focusing on capacity building activities under the EUIF.
- Percentage of successful EUIF applications.
- Number of Actions Programmes adopted by the European Commission.

(2) Assumptions and conditions

Assumptions for this action are:

¹ https://eeas.europa.eu/headquarters/headquarters-homepage/8442/consolidated-list-sanctions_en

- Continued commitment of government structures to the accession process;
- Ensured adequate staff for state administration;
- All relevant coordination mechanisms established and functioning;
- Availability and commitment of staff for capacity building interventions.

Failure to comply with the requirements set out above may lead to a recovery of funds under this programme and/or the re-allocation of future funding.

(3) Implementation modalities:

(3)(a) Indirect management with international organisation.

(i) A part of this action may be implemented in indirect management with an entity which will be selected by the Commission services using the following criteria: nature of the action, operational and technical capacity, value added, transparency and absence of conflict of interest. The implementation by this entity entails the activities deemed necessary to be implemented under Indirect Management with International Organisations. This modality will contribute to achieve both results mentioned in section (1). Its use will depend on the beneficiary's needs and requests.

(3)(b) Direct management (project approach)

Procurement:

The envisaged procurements will contribute to achieving all results of the action. The action provides flexible support to the national authorities aimed at addressing specific needs identified in the course of the implementation of IPA II, including ad hoc requests. Scope covered by the procurement will depend on the specific request of the beneficiary.

The global budgetary envelope reserved for procurement: EUR 1 000 000.

Grants

a) **Purpose of the grants:**

Potential grants would address all objectives and results of the action depending on the specific request of the beneficiary.

In case of twinning contracts the result targeted would be to provide support to legislative and institutional capacities of Montenegrin administration for transposition and implementation of the EU *acquis* and capacities for leading and carrying out the accession negotiations.

b) **Type of applicants targeted:**

In case of grants:

Legal entities, natural persons or groupings without legal personality, local authorities, public bodies, international organisations.

In the case of Twinning:

Applicants must be EU Member State administrations or their mandated bodies.

The global budgetary envelope reserved for grants: EUR 715 000.

(4) Scope of geographical eligibility for procurement and grants

The geographical eligibility in terms of place of establishment for participating in procurement and grant award procedures and in terms of origin of supplies purchased as established in the basic act and set out in the relevant contractual documents shall apply, subject to the following provisions.

- a) The Commission's authorising officer responsible may extend the geographical eligibility on the basis of urgency or of unavailability of products and services in the markets of the countries concerned, or in other duly substantiated cases where the eligibility rules would make the realisation of this action impossible or exceedingly difficult.

SECTOR	Education, employment and social policies	EUR 28 300 000
Action 2	Support to COVID-19 crisis response in Montenegro	EUR 28 300 000

(1) Description of the Action, objectives, expected results and key performance indicators

- The Action consists of a new budget support contract (Resilience Contract).²
- The *objective* of the action is to mitigate the impact of the COVID-19 crisis in Montenegro.
- The *specific objectives* are three-folds: to reduce the negative effects of the crisis on the economy; to preserve vulnerable social groups from the disruptive effects of the crisis and guarantee their continued access to basic social services; to increase access of vulnerable business to economic relief.
- Expected results and key performance indicators
The *expected results* of this action are:
 - R1: *The negative effects of the crisis on the economy are reduced*
 - R2: *Vulnerable social groups are preserved from the disruptive effects of the crisis*
 - R3: *Access of vulnerable business to economic relief is increased*

² NB: This action concerns, in addition to the AAP 2016, also AAPs 2019 and 2020. Funds are drawn from three different decisions: AAP 2016 (Decision C/2016/8226): EUR 5 334 025; AAP 2019 (Decision C/2019/8343): EUR 28 300 000; AAP 2020 (Decision C/2020/447): EUR 6 865 975. Total amount for the action is EUR 40 500 000 (EU contribution).

The achievement of the results envisaged by the action will be measured by the following *indicators*:

For R1:

- Number of subsidised wages
- Number of beneficiaries of the Government response measures

For R2:

- Number of Social Card beneficiaries *
- Number of cases entered in the Case Management System
- Amount of social allowances as % of the state budget
- Number of unemployed people*

For R3:

- Number of beneficiaries of grant schemes*
- Number of enterprises who can accede to credit instruments*
- Number of enterprises who can accede to non-financial services*

(* Indicator will be disaggregated by gender and ethnicity, whenever possible)

(2) Assumptions and conditions

Assumptions for this action are:

- The country remains politically stable
- The promised IMF and World Bank interventions and the EU Macro-financial support will materialise before the end of 2020.
- The national authorities have the capacities to conceive and quickly implement a grant scheme in favour of micro and small enterprises.
- Notwithstanding possible situations of *force majeure*, the circumstances should allow technical assistance to continue and help finalise the actions launched in 2019.
- Montenegrin authorities will use the funds provided through this budget support programme to increase the country resilience to external shocks and to preserve the access of population to basic services

Failure to comply with the requirements set out above may lead to a recovery of funds under this programme and/or the re-allocation of future funding.

(3) Implementation modalities:

(3)(a) Indirect management with an international organisation

Under this Budget support action, a complementary activity will be implemented under indirect management with the International Labour Organisation (ILO).

This implementation entails that budget implementation tasks are entrusted to the entity. ILO, in close cooperation with the beneficiaries, will implement activities aimed at strengthening the capacities of the Ministry of Labour and Social Welfare, of the Employment Agency of Montenegro, and of other institutions (e.g. the Ministry of Education,

the Centre for Social Welfare, the Labour Inspectorate, the Social Council, the Competitiveness Council, and others) concerned with improving access to the labour market of the vulnerable population categories identified in the COVID-19 response. Additionally, ILO will deliver new policy measures targeting vulnerable groups.

The envisaged EU contribution will be EUR 200 000.

The entrusted entity has been selected on the basis of the following criteria:

- The ILO office for Central and Eastern Europe (CEE) provides advisory services to governments, employers' and workers' organizations in the region. The ILO operates a wide range of programmes and projects in Central and Eastern Europe focusing on international labour standards, job creation, social security, social dialogue and equality and discrimination at work.
- ILO has a long-term commitment with the Montenegrin authorities and the European Union Delegation to Montenegro.
- In terms of operational capacity, it has a positive record of working specifically on: support to public employment services for vulnerable groups such as persons with disabilities, long term unemployed or youth; modernisation of labour market administration processes through digitalisation; strengthening labour inspectorates and establishing social and economic councils. In addition, ILO will assist in laying the foundations for peaceful mediation of labour conflicts, and supporting Employers' organizations in improving the business environment. Ongoing ILO project includes an EU funded Project 2018/403-957 "Improving Labour market governance through effective social dialogue over labour reforms" thus additionally corroborating its competence in this field, which brings added value. The action foreseen under the present sector budget support programme would have a leverage effect on cooperation with the beneficiaries, would increase efficiency and reduce transaction costs. They would also benefit from the acquired know-how and the networks already established by the ILO at national and international level.
- ILO will ensure a complete alignment with the work already undertaken and strengthen complementarities and synergies among the activities implemented by the partners in the sector.

In case the envisaged entity would need to be replaced, the Commission's services may select a replacement entity using the same criteria.

(ii) If negotiations with the above-mentioned entrusted entity fail, that part of this action may be implemented in direct management in accordance with the implementation modalities identified in section (3)(b).

(3)(b) Direct management (project approach)

Procurement:

- **Visibility and communication for budget support** (horizontal activity)
Description: visibility and communication actions will aim at highlighting to the relevant target audiences the benefit and impact of the EU's interventions and will promote transparency and accountability on the use of funds.

Value: EUR 10 000

- **Mid-term/final evaluation of budget support** (horizontal activity)

Description: the evaluation will be carried out for accountability and learning purposes at various levels (including for policy revision), taking into account in particular the impact of public expenditure on final beneficiaries identified in the action and the capacity of government authorities to respond to the unknown challenges set by the pandemic crises.

Value: EUR 90 000

The global budgetary envelope reserved for procurement: EUR 100 000.

Should contribution agreement with ILO fail, detailed under (3)(a) *Indirect management with an international organisation*, direct management is to be used as the fall-back option and a procurement procedure will be launched with the same objective, in the amount of EUR 200 000, in which case the global budgetary envelope reserved for procurement shall be: EUR 300 000.

(3)(c) Direct management through Budget Support

a) Eligibility for budget support

- Satisfactory progress in the implementation of the government response measures to COVID-19 and continued credibility and relevance thereof;
- Maintenance of a credible and relevant stability-oriented macroeconomic policy or progress made towards reducing imbalances;
- Satisfactory progress in the implementation of reforms to improve public financial management, including domestic revenue mobilisation, and continued relevance and credibility of the reform programme;
- Satisfactory progress with regard to the public availability of accessible, timely, comprehensive and sound budgetary information.

Summary of the eligibility criteria:

- Public policy

Following the outbreak of COVID-19 pandemic, the Government reacted to the health emergency with a “Country Preparedness and Response plan”, which was presented on 27 March, with an overall cost of EUR 59 million for the first three months of implementation. The plan, prepared in collaboration with the World Health Organisation, covered immediate health priorities, with some focus on the social implications of the crisis. The plan outlined the necessary sanitary and health measures, including actions to enhance the core capacities under International Health Regulations and to reinforce the early detection and monitoring capacities of the public health services and of other partners.

The national authorities adopted two fiscal stimulus packages, with the aim to mitigate the crisis’ substantial disruptive effects on growth and employment. On 19 March, the government adopted a first package of measures with an estimated cost of ca. 2.1% of GDP. The measures mainly focused on improving supplies and health sector capacity by cutting daily budget spending, the deferral of tax and social security payment obligations for 90 days. It included delayed payments for the lease of state-owned property, a moratorium on loan repayments of up to 90 days and giving companies access to subsidised credit through the Investment Development Fund to improve their liquidity.

A second package of measures was adopted on 24 April and its estimated budget cost is around EUR 75 million (or ca. 1.5% of GDP). It provided for two-months wage subsidies of up to 100 % of the minimum wage for companies in lockdown sectors, 70% of wage subsidies for employees on paid leave, quarantine or isolation, 50% of the minimum wage for companies in the affected (vulnerable) sectors, six-month wage subsidies of 70% of the minimum wage for newly reported employment, and proportional exemption of taxes and contributions to those wage subsidies. It also included support to agriculture and fisheries sector, and one-off assistance for pensioners, registered unemployed and vulnerable groups. Along with the second package of measures, the government cut wages of the highest public officials for two months with the aim to free resources for crisis response measures.

A third complementary package of measures has been announced for mid-June 2020, following adoption of 2020 budget rebalance. The new package of measures is planned to focus on investments and financial support for the real economy, in particular the tourism sector. Given informal economy's large scale, estimated between 25% and 30% of GDP, new support measures should include employees and companies from this segment of the economy in order to ensure their formalization and social inclusiveness.

- **Macroeconomic policy**

Already before the Covid-19 crisis outbreak, economic activity has started to slow as investment growth declined markedly. After strong real GDP growth in 2017 and 2018, the rate of economic expansion decelerated to 3.6% y-o-y in 2019. The deceleration reflects a slowdown in investment as large infrastructure projects were completed. Meanwhile, private consumption has become the main driver of growth, boosted by a strong tourism performance, growing employment and increasing household loans. Strong domestic demand and a high import-dependence continued to fuel a very large current account deficit. In 2019, the current account deficit totalled 15.2% of GDP, a substantial increase compared to a 10.1% of GDP gap recorded in 2015. Despite the faster increase of merchandise exports, the trade deficit expanded by 2 percentage points over the last five years, to 42.1% of GDP, reflecting a highly import-dependent economy and the impact of the investment cycle. Inflation decelerated in 2019 and early 2020. Economic growth, reform of social benefit schemes for mothers and support for young unemployed helped improve labour market conditions. However, the halt of economic activity introduced in March to contain the COVID-19 had a negative impact on the labour market. The unemployment rate rose to 17.4% in April, up from 15.3% in March and 16.4% a year earlier.

Significant underspending in public investment and recovery of tax arrears reduced the budget deficit. The budget balance improved considerably in the last two years owing to fiscal measures introduced since 2017. The budget deficit narrowed to 2% of GDP in 2019, down from 3.9% a year earlier owing to improved tax revenue collection. The 2020 budget, adopted on 27 December 2019, introduced a series of ad-hoc expenditure increases totalling 2% of GDP, including a 9% increase in public health and education salaries, extra funds for the purchase of medicines, writing-off debts owed by the national air carrier and the carryover of underspent funds for the highway construction. Overall, the 2020 budget targeted a deficit of 1% of GDP, well below the fiscal rule ceiling of 3%, but a noticeable deviation from the 0.2% surplus planned in the 2019 Economic Reform Programme (ERP). However, the COVID-19 derailed budget plans, confronting public finances with a triple shock: the collapse of tax revenue due to the interruption of economic activity, a sudden surge of healthcare expenditure, and the need to finance support measures to preserve the economy. The public debt ratio continued to increase from an already high level, partly due to liability management operations, which reduced refinancing risks. Following the adoption

of the new medium-term debt management strategy in April 2018, the government has more actively managed its public debt portfolio.

Overall, the COVID-19 pandemic is expected to push Montenegro into a deeper recession than the global financial crisis in 2009. Travel and tourism, as critical driver of country's growth accounting for some 25% of Montenegro's GDP in total, will be particularly affected. Public debt growth would be partially limited in 2020 owing to the use of government reserves that were built-up to pay maturing debt in 2020 and 2021. According to 2020 budget rebalance, the estimated shortfall in the government coffers will amount to EUR 877.5 million, including funds needed for the repayment of maturing obligations in 2021. Out of that amount, around EUR 500 million will be provided through arrangements with financial institutions, and EUR 250 million World Bank-guaranteed syndicated loan has been already secured.

The planned EU support in the amount of EUR 100 million (EUR 40 million budget support and EUR 60 million Macro-Financial Assistance) will be therefore crucial to support the balance of payments and further close the financing gap.

The response to the crisis is assessed as relevant and credible to restore key macroeconomic balances. Close monitoring of the situation will be performed in coordination with the IMF and other partners like the World Bank and UNDP.

- Public financial management

Montenegro adopted a multiannual Public Finance Management Reform Programme (2016-2020) in December 2015 which addresses several key weaknesses of the budget system. The objectives of the strategy are twofold: a) strengthen the capacities to identify, prevent and manage fiscal risks, excessive fiscal deficits and harmful macroeconomic imbalances b) Ensure that public spending is structured in a way that maximises the development impact on the national economy and ensures better quality of life for the citizens.

Montenegro underwent a new PEFA assessment in 2019, covering the PFM system performance in fiscal years 2016, 2017 and 2018, conducted by the World Bank, using the most recent PEFA methodology. Compared to PEFA 2009 and 2013, PEFA 2019 results show an overall tendency of improvement. Main performance progress is observed in (i) budget reliability (ii) extent of unreported government operations (iii) taxpayer registration and tax assessment (iv) procedures for contracting and reporting debt and issuing guarantees (v) improved procurement management (vi) effective internal controls (vii) strengthened internal audit, external audit and parliamentary scrutiny. Monitoring of fiscal risks arising from local governments by the central government has deteriorated.

Main weaknesses are related with medium-term budgetary planning, poor link with strategic planning and lack of monitoring and reporting of potential fiscal risks. Budget execution suffers from weak commitment and cash management, limited management of public assets and capital investments. The PFM Reform Programme 2016-2020 has shown a moderate rate of implementation during the first years, however it continues to address some of the key weaknesses of the PFM system and remains therefore relevant, as confirmed by the results of the ongoing PEFA exercise. Main achievements since 2019 are reported in the following areas: increased capacity for public internal financial control, external audit and debt management; the macroeconomic model was improved; tax administration and revenue collection operations became more efficient. Montenegrin authorities continue working on some crucial reform activities, strongly supported by existing external assistance, and there is

reasonable evidence that this budget support and the parallel macro-financial support operation may further encourage them to continue on the reform path.

- Budget transparency and oversight of the budget

The entry point for Budget Transparency continues to be met, as the Government of Montenegro published 5 basic budgetary documents available to the public in due time:

1. The annual budget proposal for 2020 was submitted by the Government to the Parliament on 15.11.2019 and complete documentation was published on the website of the Parliament on that day.
2. The Budget Law for 2020 was adopted on 27.12.2019 and published on 30.12.2019 in the Official Gazette of Montenegro no 7/4/2019.
3. In-year budget execution reports are made available to the public with nearly two months delay (last one published in late April 2020)
4. The annual budget execution report for 2019 was published on the Ministry of Finance website in March 2020.
5. The audit report for the final accounts for the 2018 budget was published on State Audit Institution website on 14.10.2019.

In addition to the above, Government of Montenegro also issues other relevant documents, such as: pre-budget statements, other external audit reports (SAI reports) and summary of budget proposals.

Overall, PEFA 2019 assessed that fundamentals of the PFM system are in place with main functions performance measured with high-ranking scores. This refers to the budget preparation and reliability, transparency of budget and fiscal information, revenue mobilization and budget execution, internal control and internal audit, external audit and parliamentary scrutiny. Nevertheless, more advanced components of PFM demonstrate needs for further improvement and constant reinforcement.

Montenegro scored 44.43 out of possible 100 in the Open Budget Index being classified as a country with limited budget openness and overall belonging to the group of countries with insufficient budget transparency. Yet, the scores are over the average recorded in the region. In November 2018 Montenegro regained its active status in the Open Government Partnership (OGP) Initiative.

The COVID-19 crisis and the upcoming election in September 2020 may cause delays in the budget approval process. Exceptional procedures or derogations used by the authorities during the COVID-19 crisis should be closely monitored and the necessary safeguards/oversight measures applied in accordance with the regulatory framework. Expenditures have to be properly recorded, as they will most likely lead to payment arrears. The same applies to revenue, as a result of tax relief granted to businesses. Transparency on exceptional measures should be ensured and oversight/anticorruption/fraud bodies should be involved in monitoring and reporting on their implementation.

b) Objectives

The *overall objective* of the action is to mitigate the impact of the COVID-19 crisis in Montenegro.

The *specific objectives* are three-folds:

- To mitigate the negative effects of the crises on the economy;

- To preserve vulnerable social groups from the disruptive effects of the crises and guarantee their continued access to basic social services;
- To support the recovery and development of SMEs of vulnerable business, in particular owned by women.

c) Expected results

The *expected results* of this action are:

- R1: *the negative effects of the crisis on the economy are reduced*
- R2: *Vulnerable social groups are preserved from the disruptive effects of the crisis*
- R3: *Access of vulnerable business to economic relief is increased*

d) Main budget support activities

The main activities to implement the budget support package are policy dialogue, financial transfer, performance assessment, reporting and capacity development.

Engagement in dialogue around conditions and government reform priorities, the verification of conditions and the payment of budget support.

e) Complementary actions

Under the total amount of mobilised funds for this budget support action, a total of EUR 500 000 are foreseen to be spent for complementary actions as well as for horizontal activities, e.g. communication/visibility action and evaluations. Within **this Annual Action Programme**, a total of EUR 300 000 should be covered as explained under points (3)(a) and (3)(b) above.

The total amount allocated for the budget support, including complementary and horizontal actions, is EUR 40.5 million. Within **this Annual Action Programme**, a total of **EUR 28 million** is foreseen for covering the fixed tranche of the budget support action.

(4) Scope of geographical eligibility for procurement and grants

The geographical eligibility in terms of place of establishment for participating in procurement and grant award procedures and in terms of origin of supplies purchased as established in the basic act and set out in the relevant contractual documents shall apply, subject to the following provisions.

- a) The Commission's authorising officer responsible may extend the geographical eligibility on the basis of urgency or of unavailability of products and services in the markets of the countries concerned, or in other duly substantiated cases where the eligibility rules would make the realisation of this action impossible or exceedingly difficult.

3 BUDGET

3.1 INDICATIVE BUDGET TABLE - ANNUAL ACTION PROGRAMME FOR MONTENEGRO

		Indirect management		Direct management	Total EU contribution (EUR)	IPA-II beneficiary or other third party contribution (EUR)	Total (EUR)
		with IPA-II beneficiary	with entrusted entity				
		EU contribution (EUR)	EU contribution (EUR)	EU contribution (EUR)			
Objective 1	01 Democracy and Governance	0	0	1,715,000	1,715,000	0	1,715,000
	Action 1- EU Integration Facility	0	0	1,715,000	1,715,000	0	1,715,000
Objective 2	07 Education, employment and social policies	0	200,000	28,100,000	28,300,000	0	28,300,000
	Action 2 <i>Support to COVID-19 crisis response in Montenegro</i>	0	200,000	28,100,000	28,300,000	0	28,300,000
	TOTAL	0	200,000	29,815,000	30,015,000	0	30,015,000

4 PERFORMANCE MONITORING ARRANGEMENTS

As part of its performance measurement framework, the Commission shall monitor and assess progress towards achievement of the specific objectives set out in the IPA II Regulation on the basis of pre-defined, clear, transparent measurable indicators. The progress reports referred to in Article 4 of the IPA II Regulation shall be taken as a point of reference in the assessment of the results of IPA II assistance.

The Commission will collect performance data (process, output and outcome indicators) from all sources, which will be aggregated and analysed in terms of tracking the progress versus the targets and milestones established for each of the actions of this programme, as well as the Indicative Strategy Paper.

In the specific context of indirect management by IPA II beneficiaries, National IPA Coordinators (NIPACs) will collect information on the performance of the actions and programmes (process, output and outcome indicators) and coordinate the collection and production of indicators coming from national sources.

The overall progress will be monitored through the following means: a) Result Orientated Monitoring (ROM) system; b) IPA II Beneficiaries' own monitoring; c) self-monitoring performed by the EU Delegations; d) joint monitoring by the European Commission (DG NEAR) and the IPA II Beneficiaries, whereby the compliance, coherence, effectiveness, efficiency and coordination in implementation of financial assistance will be regularly monitored by an IPA II Monitoring committee, supported by Sectoral Monitoring committees, which will ensure a monitoring process at sector level.

5 EVALUATION

Having regard to the importance of the action, a mid-term evaluation will be carried out for this action or its components via independent consultants contracted by the Commission.

It will be carried out for problem solving, and learning purposes, in particular with respect to inform future programming in the same sector.

The Commission shall inform the implementing partner at least three months in advance of the dates foreseen for the evaluation missions. The implementing partner shall collaborate efficiently and effectively with the evaluation experts, and inter alia provide them with all necessary information and documentation, as well as access to the project premises and activities.

The evaluation reports shall be shared with the IPA II beneficiary and other key stakeholders. The implementing partner and the Commission shall analyse the conclusions and recommendations of the evaluations and, where appropriate, in agreement with the IPA II beneficiary, jointly decide on the follow-up actions to be taken and any adjustments necessary, including, if indicated, the reorientation of the project.