



Brussels, 22.11.2017
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COMMISSION IMPLEMENTING DECISION

of 22.11.2017

**adopting an Annual Action Programme for Kosovo* for the year 2017 – Part II – Sector
Budget Support**

* This designation is without prejudice to positions on status, and is in line with UNSCR 1244/1999 and the ICJ Opinion on the Kosovo declaration of independence.

COMMISSION IMPLEMENTING DECISION

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adopting an Annual Action Programme for Kosovo* for the year 2017 – Part II – Sector Budget Support

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 236/2014 of the European Parliament and of the Council of 11 March 2014 laying down common rules and procedures of the implementation of the Union's instruments for financing external action¹ and in particular Article 2(1) thereof,

Having regard to Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, Euratom) No 1605/2002² and in particular Article 84(2) thereof,

Whereas:

- (1) The Regulation (EU) No 231/2014³ lays down the objectives and main principles for pre-accession assistance to beneficiaries listed in Annex I to that Regulation.
- (2) In accordance with Article 7 of Regulation (EU) No 231/2014, the assistance should be implemented through annual or multi-annual, country-specific or multi-country programmes. These programmes should be drawn up in accordance with the framework for assistance referred to in Article 4 of the Regulation (EU) No 231/2014 and the relevant country or multi-country indicative strategy papers referred to in Article 6 of that Regulation.
- (3) The Council established an Accession Partnership or a European Partnership for all beneficiaries listed in Annex I to Regulation (EU) No 231/2014. The Commission adopted an indicative strategy paper for Kosovo for 2014 - 2020 on 20 August 2014 which provides indicative allocations for the sectors for pre-accession assistance⁴.
- (4) Considering the proposals for action submitted by the beneficiaries concerned, the Annual Action Programme for Kosovo for the year 2017 – Part II – Sector Budget Support aims at providing assistance for actions in the following sector: democracy and governance.

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¹ OJ L 77, 15.03.2014, p. 95.

² OJ L 298, 26.10.2012, p.1.

³ Regulation (EU) No 231/2014 of the European Parliament and of the Council of 11 March 2014 establishing an Instrument for Pre-accession Assistance (OJ L 77, 15.03.2014, p. 11).

⁴ C(2014) 5772, adopted on 20.08.2014.

- (5) It is necessary to adopt a financing decision, the detailed rules of which are set out in Article 94 of Commission Delegated Regulation (EU) No 1268/2012.⁵
- (6) The maximum contribution of the European Union set by this Decision should cover any possible claims for interest due for late payment on the basis of Article 92 of Regulation (EU, Euratom) No 966/2012 and Article 111(4) of Delegated Regulation (EU) No 1268/2012.
- (7) Pursuant to Article 94(4) of Delegated Regulation (EU) No 1268/2012, the Commission should define changes to this Decision which are not substantial in order to ensure that any such changes can be adopted by the authorising officer responsible.
- (8) The action programme provided for by this Decision is in accordance with the opinion of the IPA II Committee set up by Article 13 of Regulation (EU) No 231/2014⁶,

HAS DECIDED AS FOLLOWS:

Article 1

Adoption of the programme

The Annual Action Programme for Kosovo for the year 2017 – Part II – Sector Budget Support under the Instrument for Pre-accession Assistance (IPA II) as set out in the Annex, is hereby approved.

Article 2

Financial contribution

The maximum amount of the European Union contribution for the implementation of the programme referred to in Article 1 is set at EUR 25 000 000 and shall be financed as follows:

EUR 25 million from the budget line 22.02.01.01 of the general budget of the EU for year 2017.

The financial contributions referred to in the first sub-paragraph may also cover interest due for late payment.

Article 3

Implementation modalities

This programme shall be implemented by direct management.

A Financing Agreement shall be concluded between the Commission and the Government of Kosovo in conformity with the Framework Agreement concluded between the same parties on 16 April 2015.

⁵ Commission Delegated Regulation (EU) No 1268/2012 of 29 October 2012 on the rules of application of Regulation No 966/2012 of the European Parliament and of the Council on the financial rules applicable to the general budget of the Union (OJ L 362, 31.12.2012, p. 1).

⁶ the Member States have declared, recalling the Council Conclusions of 18 February 2008, that the adoption of this programme does not prejudice the position of each individual Member State on the status of Kosovo, which will be decided in accordance with their national practice and international law.

Article 4

Non-substantial changes

The following changes shall not be considered substantial provided that they do not significantly affect the nature and objectives of the actions:

- (a) increases or decreases for not more than 20% of the maximum contribution set in the first paragraph of Article 2, and not exceeding EUR 10 million;
- (b) cumulated reassignments of funds between specific actions not exceeding 20% of the maximum contribution set in the first paragraph of Article 2;
- (c) extensions of the implementation and closure period;
- (d) within the limits of 20% referred to in points (a) and (b) above, up to 5% of the contribution referred to in the first paragraph of Article 2 of this financing decision may serve to finance actions which were not foreseeable at the time the present financing decision was adopted, provided that those actions are necessary to implement the objectives and the results set out in the programme.

The authorising officer responsible may adopt such non-substantial changes in accordance with the principles of sound financial management and proportionality.

Done at Brussels, 22.11.2017

For the Commission
Johannes HAHN
Member of the Commission

ANNEX

to Commission Implementing Decision adopting an Annual Action Programme for Kosovo* for the year 2017 – Part II – Sector Budget Support

1 IDENTIFICATION

| | |
|--|---|
| Beneficiary | <i>Kosovo</i> |
| CRIS/ABAC Commitment references | 2017/040 507 |
| Total cost | EUR 25 000 000 |
| EU Contribution | EUR 25 000 000 |
| Budget lines | 22.02 01 01 |
| Management Mode/ Entrusted entities | Direct management by the European Commission |
| Final date for concluding <u>Financing Agreements</u> with the IPA II beneficiary | At the latest by 31 December 2018 |
| Final date for concluding <u>procurement and grant contracts</u> | 3 years following the date of conclusion of the Financing Agreement, with the exception of the cases listed under Article 189(2) Financial Regulation |
| Final date for operational implementation | 6 years following the date of conclusion of the Financing Agreement. |
| Final date for implementing the Financing Agreement | 12 years following the conclusion of the Financing Agreement. |
| Programming Unit | NEAR D3 The former Yugoslav Republic of Macedonia, Kosovo |
| Implementing Unit/ EU Delegation | European Union Office in Kosovo |

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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 implementation of the Annual Action Programme for Kosovo for the year 2017 – Part II - Sector Budget Support shall be supported under the sector of **democracy and governance**.

EU Support for Public Financial Management Reforms will support the implementation of Kosovo's Public Financial Management (PFM) Reform Strategy 2016-2020.

The overall objective of the programme is to contribute to sound financial management and improved service delivery in Kosovo through improved fiscal discipline and strategic allocation of resources. It will support the following pillars of the PFM Reform Strategy 2016-2020:

1: Strengthened budget planning and execution

This support contributes to the PFM Reform Strategy Pillar II (Allocation Efficiency), in particular to the development of Medium Term Expenditure Framework (MTEF) and to the credibility and execution control of the annual budget. In many cases, sectorial strategies have tended to be treated as separate documents and their costs have not been integrated within the macro-fiscal framework of MTEF. Budget planning is often subjected to changes by the government or some ministries. Very often the adjustments of expenses are carried out through ad hoc changes which may occur within a short period of time, and these usually occur in capital investments. The strategic plans, the MTEF and the annual budget do not contain any appropriate risk assessments that would prevent or decrease the need for such ad-hoc decision making. The activities foreseen under this objective will aim at addressing the afore mentioned challenges. Relevant tools and mechanisms will be developed in order to enable close link between MTEF, policy development and budget planning and execution processes. Complementary assistance will be provided in order to carry out the capacity building of relevant departments in the Ministry of Finance related to these processes and their improvements.

2: Realistic and sustainable domestic revenue forecast and collection

This support contributes to PFM Strategy Pillar I (Fiscal Discipline), in particular to the accuracy of the macroeconomic indicators and revenue forecasting as well as sustainable revenue collection. In order to improve the accuracy of the macroeconomic indicators that are used for the overall macroeconomic assessment in Kosovo and also for the revenue forecasting in the budget planning process, the Ministry of finance will develop a set of standardized indicators, the methodology for their calculation usage and dissemination. An Administrative Instruction will define all these elements and their development and usage. In addition, both the methodology and indicators will be published by the Ministry of Finance. This will contribute towards increase of transparency of the process. Furthermore, this priority aims at improving the realistic revenue forecast which will enable more realistic budget planning and execution. This will be translated in an improved MTEF and annual budget process. Support to this area as well as to sustainable revenue collection will improve the

budget credibility, strategic allocation of resources and fiscal discipline. Overly optimistic revenue forecasts lead to expenditure allocations that will eventually require an in-year reduction in spending (affecting public policies), increase of arrears or an unplanned increase in borrowing to sustain the spending level. In the context of trade liberalisation, income from customs will likely decrease, and a major change in the tax base and system to collect more from internal taxation should be planned in advance to avoid a major fiscal imbalance. This is reflected in the PFM Reform Strategy with main focus on the renewal of the IT system in tax administration and fight against informal economy. Complementary assistance will be also provided to this area in order to support larger reform in domestic revenue collection.

3: Strengthened internal control and audit

This support contributes to PFM Strategy Pillar III (Operational Efficiency), in particular to internal control and audit. In terms of internal audit, the Central Harmonisation Unit (CHU) within the Ministry of Finance will improve the guidelines and templates for internal auditors in order to increase their efficiency. Communication with the budget organisations (ministries, agencies, municipalities), both at central and municipal level should be intensified and continuous risk management should be applied. Complementary assistance will aim at supporting the CHU in this regard. Regarding to the internal control systems the link between efficient use and spending of public funds (mainly through public procurement) and efficient internal control and monitoring mechanisms will be identified and supported through this programme.

4: Increased effectiveness of external control and oversight

This support contributes to PFM Strategy Pillar III (Operational Efficiency), in particular to external audit and oversight. While the capacities of the National Audit Office (NAO) are at sufficient level, the communication with budgetary organisations and the parliament should be intensified in order to increase the level of addressed NAO recommendations. Furthermore, the NAO should further develop its capacities for specialised audits and this is where the complementary assistance will be also focused.

5: Increased efficiency and transparency of public procurement in Kosovo

This support contributes to PFM Strategy Pillar IV related to public procurement. Although within the PFM Reform Strategy it is linked with overall transparency of public spending, this programme will aim at linking the public procurement with internal control, accountability and efficiency as well. In terms of public procurement, Kosovo institutions are faced with the challenge of implementation of the e-procurement throughout central and municipal institutions. Furthermore, business community or economic operators are faced with the same challenge but from different perspective. Further technical and human resource capacities are needed to meet this challenge. Complementary assistance will aim to tackle this issue as well as other aspect of public procurement which will contribute to increased efficiency, accountability and accountability of public administration.

6: Increased transparency in the management of public funds

This support contributes to PFM Strategy Pillar IV related to budget transparency. In terms of budget transparency, Kosovo government aims at applying International Monetary Fund Government Finance Statistics (IMF GFS) standards. Furthermore, the Ministry of Finance is working on developing and publishing the citizen friendly budget. This will contribute towards increased transparency and provide wider opportunities for all-inclusive discussions on budget planning and spending. Kosovo is still not part of the Open Budget Index (OBI) assessment, but the efforts are made in order to have Kosovo included in 2018 or 2019. This will indeed contribute towards budget transparency and increased dialogue between civil society and the government in the PFM area.

- **Overview of past and on-going EU, other donors' and/or IPA II beneficiary's actions in the relevant sectors:**

The actions under **democracy and governance** build on past EU assistance which were delivered through IPA I and IPA II 2014 - 2016: lessons learned from past evaluations and audits were taken in account when designing the actions herein, as well as complementarity with actions financed from other donors.

In the sector of **democracy and governance** previous EU assistance focused on strengthening the capacity of Kosovo institutions, including the assembly, in transposing, applying and implementing the EU acquis, especially in areas covered in the Stabilisation and Association Agreement (SAA). Furthermore, a Sector Reform Contract in the area of public administration reform has been adopted under the Action Programme for Kosovo for the year 2016. Additional support was provided for the effective and efficient management and absorption of IPA funds for the implementation of the EU facilitated dialogue aimed at the normalisation of relations between Belgrade and Pristina and for increases in effectiveness, independence and accountability of the civil service.

List of Actions foreseen under the selected Sectors/Priorities:

Democracy and Governance

| DIRECT MANAGEMENT | |
|---|-----------------------|
| Action 12: "EU Support for PFM Reforms" | EUR 25 000 000 |
| TOTAL | EUR 25 000 000 |

2.2 DESCRIPTION AND IMPLEMENTATION OF THE ACTIONS

| SECTOR | Democracy and Governance | | EUR 25 000 000 |
|------------------|-----------------------------------|--------------------------|---|
| Action 12 | EU Support for PFM Reforms | Direct management | EUR 21 000 000 (budget support) EUR 4 000 000 (complementary technical assistance) |
| | | Total | EUR 25 000 000 |

Sector Budget Support

a) Eligibility for budget support

Public policy: EU Support for PFM Reforms will be linked to the objectives of Kosovo's PFM Reform Strategy with an action plan and a cost estimate adopted in June 2016. The strategy is currently under implementation. The strategy is relevant since it addresses shortcomings and weaknesses within the sector as identified under analytical studies such as Public Expenditure and Financial Accountability assessment - PEFA, the OECD Support for Improvement in Governance and Management (SIGMA) baseline assessment and Tax Administration Diagnostic Assessment Tool - TADAT. SIGMA has helped to draw an architecture for the monitoring and evaluation system (M&E), which is used for producing the first annual report of the PFM reform Strategy. In addition, PFM sector in Kosovo is addressed through the Public Internal Financial Control (PIFC) Strategy 2015-2019 and the Public Procurement Strategy 2017-2021 as well. Both these strategies are considered credible and relevant. As their main objectives are incorporated within the PFM Reform Strategy, it is expected that the progress in the PFM area in Kosovo is monitored through coordinated M&E of all three strategies. Capacity constraints within the Ministry of Finance, but also other relevant institutions for the PFM area, appear to be one of the main risks for the implementation and appear to relate to financial constraints, adequate staffing of the implementing agencies as well as technical capabilities. Technical assistance is proposed to address the gaps.

Macroeconomic policy: A Stand-By Arrangement between Kosovo and the International Monetary Fund (IMF) was signed on 29 July 2015. Under the arrangement Kosovo authorities pursue a credible macroeconomic policy oriented at continuing fiscal stability and sustainability. This is contributing towards fiscal stability and debt management in Kosovo. Economic governance between the EU and Kosovo was further strengthened since 2015 through the elaboration of annual Economic Reform Programmes (ERP) submitted to the European Commission. Kosovo has since elaborated three ERPs with the key objective to

strengthen economic growth and competitiveness by accelerating economic reforms and further improving the business environment conducive to private sector growth.

Public financial management: The PFM reform programme is relevant, because the approved PFM Reform Strategy updates the status in crucial PFM areas, defines the areas of attention and weaknesses and presents the reform measures to address these weaknesses. The programme ensures full coverage of the weaknesses identified in the 2015 SIGMA baseline assessment, 2016 PEFA and other available PFM assessments. The PFM reform process is well sequenced, there is a high level of political commitment to reforms and clear leadership by the Ministry of Finance and there are clear arrangements for coordination and monitoring. Nonetheless, some of the main challenges Kosovo is facing include enforcement of existing PFM legislation, deviations from planned spending, poor revenue collections at municipal level and a weak link between the MTEF and annual budget that benefits ad-hoc decision making. Much has been invested by Kosovo to build institutional and professional capacity setting up the essential aspects of sound PFM.

Budget transparency and oversight of the budget: The entry criterion for budget transparency has been met by Kosovo – the annual budget is published online (<https://mf.rks-gov.net/en-us/Budget>) once the Law on the Budget is adopted. Budget transparency and oversight roadmap is embedded into the PFM strategy. Kosovo does not yet appear in the Open Budget Index Survey (OBI), but efforts are made to include it as of 2018 or 2019. Domestic non-government watchdogs affiliated to the International Budget Partnership are active and regularly produce analysis pressing for improvements.

b) Objectives

The **overall objective** of EU Support for PFM Reforms is to contribute to sound financial management and improved service delivery in Kosovo through improved fiscal discipline and strategic allocation of resources.

The **specific objectives** are:

- Specific Objective 1: To strengthen budget planning and execution;
- Specific Objective 2: To enable sustainable domestic revenue collection;
- Specific Objective 3: To strengthen internal control and audit;
- Specific Objective 4: To increase effectiveness of external audit and budgetary oversight;
- Specific objective 5: To increase efficiency and transparency of public procurement in Kosovo;
- Specific Objective 6: To increase transparency of the management and usage of public funds.

c) Expected results

- Increased accuracy of macroeconomic indicators and revenue forecasting (linked to Specific Objective 1).

- Further advancement of the role of the Medium-Term Expenditure Framework (MTEF) as a liaison document between Kosovo's strategies and fiscal processes (linked to Specific Objective 1).
- Increased annual budget credibility for central government (linked to Specific Objective 1).
- Expanded revenue base by fighting fiscal evasion (linked to Specific Objective 2).
- Increased efficiency of the revenue collection agencies in order to contribute towards sustainable revenue collection (linked to Specific Objective 2).
- Strengthened internal audit function as value added service towards accountable management (linked to Specific Objective 3).
- Strengthened internal controls within budgetary organisations (linked to Specific Objective 3)
- Efficient oversight of public funds is ensured by the Assembly Committee for Oversight of Public Finances, National Audit Office and the government (linked to Specific Objective 4).
- Public procurement contributes towards efficient and transparent use of public funds (linked to Specific Objective 5).
- Compliance of Kosovo information with the IMF 2014 Government Finance Statistics Manual is ensured (linked to Specific Objective 6).
- Budget planning and execution data made accessible to the public (linked to Specific Objective 6).

d) Main sector 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

Essential elements of the action

Assistance complementing the budget support operation will be used for:

- supporting Kosovo institutions to coordinate the overall PFM reform and its implementation, through efficient monitoring, evaluation and reporting mechanisms, which requires close coordination and collaboration with stakeholders, including civil society organisations;
- supporting key Kosovo institutions in improving domestic revenue collection;
- supporting the Central Harmonisation Unit and other relevant government institutions in strengthening of internal control and audit functions;
- supporting key public procurement bodies in their regulatory, advisory, monitoring and oversight role with the aim of effective implementation of the public procurement law in Kosovo;

Procurement:

- a) the global budgetary envelope reserved for procurement: EUR 3.3 million
- b) the indicative number and type of contracts: 4-6 Service or Framework Contracts.
- c) indicative time frame for launching the procurement procedure: Q2 2018

Grant – Twinning – Call for proposal: Twinning: Support to National Audit Office

- a) Objectives and foreseen results: To strengthen the outward communication and relation of the National Audit Office with Budget Organisations and the parliament;
- b) The essential eligibility criteria: applicants must be EU Member State administrations or mandated bodies;
- c) The essential selection criterion is the operational capacity of the applicant;
- d) The essential award criteria are technical expertise of the applicant, and the relevance, methodology and sustainability of the proposed action;
- e) Maximum rate of EU co-financing: The maximum rate of EU financing will be 100% of the total cost of the action.
- f) Indicative amount of Twinning contract: EUR 0.7 million;

The maximum possible rate of EU financing may be up to 100% of the total cost of the action in accordance with Article 192 of Financial Regulation if full funding is essential for the action to be carried out. The necessity for full EU funding will be justified by the responsible authorising officer in the award decision, in respect of the principles of equal treatment and sound financial management.

- g) Indicative date for launching the selection procedure: Q2 2018.

- **3 BUDGET**

3.1 INDICATIVE BUDGET TABLE - ACTION PROGRAMME FOR KOSOVO

| | | Direct Management | | | |
|--|---------------------------------------|--------------------------|--|--------------------------|---------------|
| | | EU Contribution | IPA II beneficiary Co-financing | Total expenditure | MM |
| Objective 1 2017 /040 507 | 01: Democracy and Governance | EUR 25 000 000 | | EUR 25 000 000 | direct |
| | Action 12: EU Support for PFM Reforms | EUR 25 000 000 | | EUR 25 000 000 | direct |
| Total Budget for Objective 1- budget line 22.02 01 01 | | EUR 25 000 000 | | EUR 25 000 000 | direct |
| TOTALS | | EUR 25 000 000 | | EUR 25 000 000 | direct |

- **4 IMPLEMENTATION MODALITIES AND GENERAL RULES FOR PROCUREMENT AND GRANT AWARD PROCEDURES**

This programme shall be implemented by direct management by the EU Office in Kosovo in accordance with article 58(1)(a) of the Financial Regulation and the corresponding provisions of its Rules of Application.

Procurement shall follow the provisions of Part Two, Title IV Chapter 3 of the Financial Regulation No 966/2012 and Part Two, Title II, Chapter 3 of its Rules of Application.

Grant award procedures shall follow the provisions of Part Two Title IV Chapter 4 of the Financial Regulation No 966/2012 and Part Two Title II Chapter 4 of its Rules of Application.

Under the Financial Regulation, Parts One and Three of the Financial Regulation and its Rules of Application shall apply to external actions except as otherwise provided in Part Two, Title IV.

The Commission may also use services and supplies under its Framework Contracts concluded following Part One of the Financial Regulation.

Twinning:

Twinning projects shall be set up in the form of a grant agreement, whereby the selected Member State administrations agree to provide the requested public sector expertise against the reimbursement of the expenses thus incurred.

The contract may in particular provide for the long-term secondment of an official assigned to provide full-time advice to the administration of the IPA II beneficiary as resident twinning advisor.

The twinning grant agreement shall be established in accordance with relevant provisions of Part Two Title IV Chapter 4 of the Financial Regulation and Part Two Title II Chapter 4 of its Rules of Application. Parts One and Three of the Financial Regulation and its Rules of Application shall apply to external actions except as otherwise provided in Part Two, Title IV.

- **5 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 Kosovo.

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 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 Sectorial Monitoring committees, which will ensure a monitoring process at sector level.