



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

BOSNIA AND HERZEGOVINA

EU support to public financial management



Action summary

The overall objective of this action is to improve public financial management in BiH. To achieve this objective, this action will support the improvement of the budget planning and execution process through strengthening indirect taxation system, improving the process of medium-term policy planning at all levels of government in BiH and alignment with the process of program budgeting. By means of this action the legal basis for the full implementation of programme budgeting will be prepared.

Further, the action will enhance the civil servants' capacities for policy planning and programme budgeting at all government levels in BiH.

The interoperability of Indirect Taxation Authority IT systems with the EU VAT Information Exchange System and the EU transit system will be enabled by upgrading its IT platform. Providing on-the-job training for further harmonisation in the area of indirect taxation will result in strengthening indirect taxation system in BiH.

Action Identification	
Action Programme Title	Annual Action Programme for Bosnia and Herzegovina for the year 2017
Action Title	EU support to public financial management
Action ID	2017/040-524.02
Sector Information	
IPA II Sector	Democracy and governance
DAC Sector	15111 Public finance management
Budget	
Total cost	EUR 5 100 000
EU contribution	EUR 5 100 000
Budget line(s)	22.020101
Management and Implementation	
Management mode	Direct management
<i>Direct management:</i> EU Delegation <i>Indirect management:</i> National authority or other entrusted entity	EU Delegation to Bosnia and Herzegovina
Implementation responsibilities	EU Delegation to Bosnia and Herzegovina
Location	
Zone benefiting from the action	Bosnia and Herzegovina
Specific implementation area(s)	Bosnia and Herzegovina
Timeline	
Final date for concluding Financing Agreement(s) with IPA II beneficiary	At the latest by 31 December 2018
Final date for concluding delegation agreements under indirect management	N/A
Final date for concluding procurement and grant contracts	3 years following the date of conclusion of the Financing Agreement, with the exception of cases listed under Article 189(2) of the Financial Regulation
Final date for operational implementation	6 years following the conclusion of the Financing Agreement
Final date for implementing the Financing Agreement	12 years following the conclusion of the Financing Agreement

(date by which this programme should be de-committed and closed)			
Policy objectives / Markers (DAC form)			
General policy objective	Not targeted	Significant objective	Main objective
Participation development/good governance	<input type="checkbox"/>	<input type="checkbox"/>	X
Aid to environment	X	<input type="checkbox"/>	<input type="checkbox"/>
Gender equality (including Women In Development)	<input type="checkbox"/>	X	<input type="checkbox"/>
Trade Development	X	<input type="checkbox"/>	<input type="checkbox"/>
Reproductive, Maternal, New born and child health	X	<input type="checkbox"/>	<input type="checkbox"/>
RIO Convention markers	Not targeted	Significant objective	Main objective
Biological diversity	X	<input type="checkbox"/>	<input type="checkbox"/>
Combat desertification	X	<input type="checkbox"/>	<input type="checkbox"/>
Climate change mitigation	X	<input type="checkbox"/>	<input type="checkbox"/>
Climate change adaptation	X	<input type="checkbox"/>	<input type="checkbox"/>

1. RATIONALE

PROBLEM AND STAKEHOLDER ANALYSIS

The Indirect Taxation Authority (ITA) is the most important collector of revenues in Bosnia and Herzegovina (BiH). The scope of its operations is in the area of indirect taxes (custom duties, value added tax (VAT), tolls and excise duties). The introduction and implementation of new procedures in the area of indirect taxation require adequate IT tools. Currently the ITA is having two main software applications used in its everyday operations with business community, one for VAT called ALICE and one for custom declaration processing – ASYCUDA World (AW). The new upgraded customs software (AW) has been in use since July 2016. It is designed to enable modernisation of ITA operations related to custom procedures and duties and faster flow of goods in and out of BiH, as well as submission of customs declarations in electronic form, using electronic signatures. The AW also ensures faster and more secure customs clearance, which leads toward increase of revenues collected in the national budget. Financed from the national budget, the ITA is currently developing a new VAT application and application for national transit. Design of the new VAT software is in its first phase. It will enable submission of VAT and excise duties using electronic form, including electronic signatures, which will improve previous operations of ITA in parallel with improving risk analysis and collection of indirect taxes.

Due to the degradation of the existing hardware platform of the Information System, everyday operations of the ITA related to processing data and information on indirect taxes are performed at a slow rate and affect the performance of existing business applications-customs and tax software. At the existing hardware platform, security and maintaining of the data is compromised and this could result in permanent loss of data from the archives. In order for the new customs and taxes software to be used optimally and new procedures to be applied, it is necessary for the entire hardware infrastructure to be modernised so to enable the efficient functioning of the ITA, better delivery of services to final beneficiaries and to improve the quality of the fiscal policy in BiH. The last major investment in information technologies in the ITA was at the time of establishment of the ITA in 2004. The supply of equipment was financed by the EU.

In addition to the procurement of new IT platform, there is a need to continue with the activities related to further alignment of BiH legislation with the EU *acquis* in the area of indirect taxation. Through IPA 2014, funds have been secured for development and implementation of international transit (NCTS – New Computerised Transit Procedure). Implementation of the Convention on Common Transit Procedure in BiH, interoperability and compatibility with EU tax and customs systems, as well as implementation of newly introduced procedures in accordance with EU systems, also require adequate IT support. The new IT platform will enable the implementation of NCTS, will enable interoperability with EU VAT Information Exchange System (VIES) and will provide adequate technical support for implementation of certain procedures aligned with EU regulation and practices.

Activities supporting the stable mobilisation of indirect tax revenues, as the most important revenues in BiH, represent one element in the process of fiscal consolidation. The other element is represented by the adequate and efficient distribution and spending of total public revenues on priority goals and programmes through the process of designing a mid-term budget framework and annual budgets.

In the area of managing public finance in Bosnia and Herzegovina in the previous period, significant progress has been made, but there is need for further improvement. On 29 December 2016 the Council of Ministers of Bosnia and Herzegovina adopted the PFM Reform Strategy in the Institutions of Bosnia and Herzegovina with an Action Plan. The Strategy envisages the introduction of programme budgeting within the framework of the measure of improving planning of funds in the medium term and annual budget documents in accordance with strategic documents.

In the previous period, ministries of finance at the level of the Institutions of Bosnia and Herzegovina (BiH), Federation of BiH (FBiH) and Republika Srpska (RS) and the Finance Directorate of Brčko District (BD) were supported through a number of projects financed by the Office for International Development of the Government of Great Britain (DFID, SPEM I, II and III) in the area of public finance management, with the aim of improving the budget planning process. Main achievements of previous reforms are: adopted budget planning approach in 10 steps, introduction of the obligation of preparing the Medium Term Budget Framework (MTBF) for a three-year period prepared each year and adopted by the competent Government, improved procedures, instructions and forms and training related to the concept

and introduction of programme budget. The following step was introduction of the information budget planning and management system (BPMIS) connecting all budget users in FBiH, RS, BD and BiH, financed from the Public Administration Reform Fund.

At the level of the Institutions of BiH, adoption of the Law on Amendments to the Law on Financing the Institutions of BiH (“Official Gazette of BiH”, No. 49/09) introduced into the legal procedures the idea of programme budgeting. Article 6 of the Law on Financing stipulate that, in addition to the Draft Budget, the Ministry of Finance and Treasury of BiH is obliged to submit to the Council of Ministers of BiH and the Parliamentary Assembly tables representing an overview of requests of budget users in the programme format, as additional information supporting the budget. In addition, adoption of the Decision on the procedure of medium term planning, monitoring and reporting in the Institutions of BiH (“Official Gazette of BiH”, No. 62/14) introduced strategic planning in the Institutions of BiH, representing a further step in establishing programme budgeting. However, majority of budget users provided their programme structure mostly based on their organisational structure, thus causing these to be almost identical to their administrative organisation. As such, the programme structure arises from the organisational structure of budget users and not from the strategic framework (strategic and operational goals), sectoral strategies and other relevant documents (economic policy, development plans and alike). Therefore, the link between appropriation of budget funds and government priority policies remains weak. It is evident that there is a significant difference between the institutions when it comes to quality of defined programs and accompanying indicators. Strategic planning and budgeting processes are not completely synchronised at all levels of government. Strategic planning is established only at the level of the Institutions of BiH.

New Laws on Budget in FBiH in 2013 introduced programme budgeting and budget users are obliged to submit their requests in programme format and to align them with strategies and medium term planning documents. The Law on the Budget System and the Law on the Treasury of RS mention programme classification as one of the standard budget classifications, but still lack the description of the meaning of programme classification (relationship between programs, projects and activities) and its application. Actual provisions regulating preparation of budget, submission of budget request, monitoring of budget execution and reporting are not based on programme classification. Therefore, there is no legal basis for introduction of programme budgeting. In Brčko District, the Law on the Budget of Brčko District of Bosnia and Herzegovina from July 2008 stipulates submission of requests of budget users in programme format and introduces the medium-term budget-planning framework (Framework Budget Document). At the moment, the new regulation on budget is being prepared with the aim of encompassing additional provisions for introduction of programme budgeting.

This action implies a wider scope of users since, in addition to ministries of finance of the Institutions of BiH, FBiH, RS and the Finance Directorate of Brčko District, it includes ministries of finance of Cantons in FBiH and 32 selected local self-government units in RS, since these were poorly, if all, represented in previous projects. The basic criteria for selection of the local self-government units in RS will be the size of the budget and regional representation. It is necessary to note that implementation of the project of introduction of BPMIS (USAID through Project “Fiscal Sector Reform Activity in Bosnia and Herzegovina” FAR) to cantonal levels of government will represent important assistance in implementation of programme budgeting, which is in line with the Road Map for programme budgeting. Main users of this Action are: Indirect Taxation Authority of BiH, ministries of finance on all levels of government (BiH, FBiH, RS, and Cantons), Finance Directorate of Brčko District and Departments for Budget of selected local self-government units in both Entities.

OUTLINE OF IPA II ASSISTANCE

Interventions in two areas are planned under this action: In the area of indirect taxation and in the area of programme budgeting, thus assisting BiH authorities in producing a more effective public financial management system. As such, the action will have a significant economic influence, exercised through strengthening links between economic policy priorities, strategic planning and budgeting with the aim of more efficient utilisation of resources.

In order to have simplified and EU aligned procedures implemented, besides support in legislative reforms and capacity building of the ITA, support is needed for upgrade of IT infrastructure of the ITA BiH. Procurement of a new IT platform, together with newly developed customs and tax software is aimed to support implementation of certain procedures in the area of indirect taxation, aligned with

relevant EU regulation and procedures. This will significantly improve efficiency of ITA operations towards business community in BiH and will help removing numerous obstacles as the result of outdatedness of the existing hardware currently used by ITA. The new platform will improve ITA operations enabling better and faster reporting to the ITA management as well as fighting tax and customs frauds and support to introduction of e-documents within the ITA. As a result, the ITA will be implementing electronic submission of the VAT and excise duties using digital signature as well as submission of electronic customs declarations. Moreover, improvements will be made in the area of risk analysis and preparatory work for future exchange of information with EU VIES. These tasks will have to be supported by full implementation of the electronic signature. The new IT platform will also support implementation of NCTS on national and international level.

The action will ensure further strengthening of indirect taxation systems in terms of aligning relevant BiH legislation in the field of indirect taxation, which will provide the necessary preconditions for implementation of the Convention on a Common Transit Procedure in BiH, and support towards interoperability and compatibility with the EU tax and customs systems. In addition, the action will contribute to introduction and practical application of new procedures, such as certain simplification of procedures, risk analysis systems improvement and introduction of single customs guarantee. The action will enable implementation of e-VAT, e-excise duties, NCTS and e-customs declarations, thus supporting BiH e-Government Project.

Appreciating the results of the previous projects, recommendations and the Road Map, this action will represent continuation of activities in programme budgeting establishment phases, through establishment/strengthening of strategic planning, creation/upgrade of legal framework for programme budget and introduction of lower levels of government (cantons and chosen local communities) into the reform. In this phase, detailed training on the concept of programme budgeting, definition of program structure and implementation of program budgeting methodology, organised in line with the previous project, is envisaged for employees of Sectors and Departments for budget and employees of other ministries (Services and Units) taking part in budget preparation of cantons and selected local communities.

The implementation of this action will enable methodology and the concept for preparing more quality programme budget documents and better presentation on how planned funds will be used at all levels of government. Furthermore, the envisaged intervention under this action will help the executive and legislative bodies at all levels of government in adopting adequate decisions on priorities in terms of allocation of limited funds in accordance with performance and effects, i.e. in accordance with the results. Budget planning based on a programme format will enable a more transparent adoption of decisions on allocation of funds and widen the scope of responsibilities of executive bodies and managers of the public sectors institutions in terms of budget spending effects and results. Programme budget ensures presentation of information so as to establish a clear connection between the levels of allocated budget funds and programmes implemented by budget users, which should be directly connected with the defined policy goals. Budget documents will be comprehensive, with all sources of financing stated under organisational, economic, and functional and programme classification, in accordance with strategic documents and mid-term work programmes of the institutions. This will enable efficient monitoring of indicators of successfulness of programme budgets. In this way, a connection will be established between planning and monitoring of realisation of public investment projects and the budgeting process.

The objective of the action in the area of budget planning is to introduce programme budgeting, strengthen organisational frameworks and human resources for strategic planning in individual institutions, develop detailed budget users structure, define goals of individual programmes and create performance indicators or other methods for measuring the results of achieving programme objectives, as well as ensure budgeting based on results on Government policies and expenditure ceilings stated in the Budget Framework Document (BFD).

RELEVANCE WITH THE IPA II STRATEGY PAPER AND OTHER KEY REFERENCES

Article 111 of the **Stabilisation and Association Agreement (SAA)** concluded between BiH and the EU in June 2008, stipulates cooperation of Parties to the Agreement in improving development of effective and responsible public administration. In the most part, the cooperation will be directed towards development of institutions, encompassing all levels of public administration in Bosnia and Herzegovina.

Article 97 stipulates establishment of cooperation in the area of customs duties in order to align the customs duties system of BiH with the EU system, as well as customs laws of BiH with the EU *acquis*. Article 98 stipulates establishment of cooperation in the area of taxation, including measures of further tax system reforms with the aim of ensuring more efficient tax revenues collection and combating tax fraud.

The Indicative Strategy Paper for Bosnia and Herzegovina (ISP) 2014-2017 underlines the need for further public administration reform, including, inter alia, comprehensive public financial management reform. It has been concluded that Public Administration Reform is being implemented very slowly, showing weaknesses in different areas including policy planning and coordination, human resources management, budget planning, transparency and vertical coordination. Different public finance sub-systems still show certain weaknesses. There is a need for defining timely, upgraded and efficient fiscal policies. Therefore, as the result of IPA financing between 2014 and 2017, it is expected for the public financial management capacities of BiH to be strengthened, including more efficient management and collection of revenues, as well as budget preparation and execution.

SIGMA Baseline Measurement Report for Bosnia and Herzegovina dated April 2015 states that medium-term budget planning is based more on the legal obligation on the expenditures side than on future costs and planned policies goals. Neither Global Framework of Fiscal Balance and Policy (GFFBP) nor MTBFs contain information on strategic plans for development of policies; therefore there is no connection between strategic plans for development of policies and budget projections. Annual budget preparation is defined by laws, but information provided to Parliaments as basis for their discussions of budgets is not comprehensive. Bearing in mind these shortages, the Public Finance Management Reform Strategy in the Institutions of BiH, adopted by the Council of Ministers of BiH contains activities related to widening the budget scope and improving comprehensiveness of information included in budget documents and establishment of program budgeting through amendments to the Law on Financing the Institutions of BiH, and, in this regard, adoption of appropriate by-laws, widening the scope of budget users register and training of budget users in relation to implementation of legal documents and by-laws.

In the EC Report for Bosnia and Herzegovina for 2016, the EU concluded that BiH is still in the initial phase of public administration reform. In the following period, BiH is expected to implement recommendations of the European Commission in view of preparing a comprehensive public finance management reform program in line with new strategic public administration reform strategy. Ministries of Finance on all levels (BiH, Entities and BD) stated their readiness to prepare a comprehensive public finance management strategy upon adoption of separate strategies on all levels of government.

The Action is linked to Pillar 5-Growth-oriented Governance of the **SEE Strategy 2020**, more particularly to key actions in Dimension N-"Effective Public Services", N.5 "Upgrade policy and regulatory capacities, and Dimension O "Anti-corruption", O.4 "Introduce regular audits of all government programs and projects and independent financial audit".

One of ten integrated guidelines, **Europe 2020** is ensuring quality and sustainability of public finance. In this regard, in their Document on Enlargement Strategy for 2013-2014, the EC announced the new approach to further enlargement policy with emphasis on economy (economic governance, competency and growth) with the aim of enabling better coordination and convergence of economic and fiscal policies between candidate countries and potential candidate countries and the EU. It is intended for the countries in the process of enlargement to connect more with the new system of economic governance in the EU based on the European Semester, through annual presentation of national economic reforms programmes and public financial management action plans.

In the BiH Reform Agenda 2015-2018, measures are envisaged for improvement of collection of tax revenues, including improvement of exchange of information between tax administrations and introduction of e-Services for VAT. Likewise, BiH should support increase of excise duties on tobacco and alcohol representing direct revenues of the Health Insurance Fund. It is stated that implementation of the new Law on Customs Policy will be ensured, thus simplifying customs processing and decrease the number of administrative requests, resulting in facilitation of trade. In addition, it is envisaged for the renewed Public Administration Reform Strategy to be prepared, under which the Public Financial Management Reform Strategy represents one of the main pillars of the Public Administration Reform Strategy.

Introduction of programme budgeting represents one of the reform measures under the **Public Financial Management Reform Strategy of BiH Institutions** that was adopted by the Council of Ministers of BiH in December 2016. Activities are focused on preparation of amendments to the Law on financing of the BiH institutions to ensure conditions for adopting and monitoring the budget of BiH institutions in the program format, and on the training of civil servants (greater coverage of trainers) for the implementation of a reform measure and Program Budget Manual. Program budgeting as a reform measure is contained in the draft strategies of FBiH, RS and DB.

LESSONS LEARNED AND LINK TO PREVIOUS FINANCIAL ASSISTANCE

In the last six years (2010-2016), with the help of well-designed and focused projects financed under IPA, the ITA made good use of the funds approved through three allocations: IPA 2008 “Support to further EU *acquis* alignment of Indirect Taxation Authority”, IPA 2010 “Strengthening the customs sector within Indirect Taxation Authority” and IPA 2011 “Further harmonisation to EU practices and EU *acquis* on customs and taxation”. As the result of these three projects, ITA succeeded in achieving significant and sustainable results in building capacities and competencies for assuming responsibility for the process of implementation of the relevant EU legislation in the area of custom duties and taxes, as well as for performing their tasks in the context of implementation of foreign trade agreements.

The last two ROM Monitoring Reports prepared in the end of 2014 and in the beginning of 2015, clearly confirm the fact that ITA gradually developed its capacities through absorption of IPA assistance.

As a continuation of previous IPA assistance through Twinning projects, which have helped in the drafting of laws and bylaws harmonised with the EU legislation and the application of best practices in the EU, through the IPA 2014 twinning project “Improving capacity of Indirect Taxation Authority, the EU continued support the ITA in further alignment with the EU *acquis* and in legal preparations for joining the Common Transit Convention. Within IPA 2014 assistance for development and implementation of international NCTS (NCTS New Computerised transit System – level of Common Transit Convention) will be provided and also supply of equipment for customs laboratory is foreseen. **"Strengthening Public Financial Management"** project (SPEM), financed by DFID since 2005 until March 2011, offered technical assistance to all ministries of finance in BiH, in three stages (SPEM I, II and III), with the aim of defining an integrated mid-term budget planning and preparation framework, designed to improve consistency between Government policy goals and budget allocations. SPEM I (2002-2004) helped in introducing mid-term budget planning through establishing a Budget Framework Document for the period of three years, at the level of the entities. SPEM II (2005-2008) introduced the methodology in 10 steps and prepared a Manual for budget preparation. SPEM II has further institutionalised and deepened the procedure of budget planning, connecting it with the process of adopting policies at all levels of government, in particular leading the programme budgeting reform.

"Development of Central Authority Bodies in BiH"- Financed by the EU, had the aim of improving capacity of State and Entity administrations in the area of policy development, planning and coordination. The project contributed to the main PAR Strategy goals, improvement of central policy capacities at all levels of government and strengthening links between policy development and budgeting.

"Development of Capacities in BiH and Entity Ministries of Finance for Effective Public Investment Management"- Financed by the Swedish International Development Cooperation Agency (SIDA) between March 2013 and June 2015, enabled simultaneous and synchronized development of Public Investment Programmes in the ministries of finance of the entities and of the State and linking Public Investment Programs with the mid-term planning process. The Swedish Public Administration Institute FCG SIPU International evaluated the project and concluded that it was relevant in view of resolving one of the key issues of public financial management and its links to the overall public administration reform, as well as mid-term planning and allocation of funds. The evaluator proposed for the support to be continued with emphasis on the mid-term planning process and budget planning.

"Strengthening Public Financial Management in BiH"- Financed under IPA and implemented between 2013 and 2015 (Component 1) enabled intensive on-job training in 32 pilot budget users at all levels of government (10 on each, the state level, FBiH and RS and 2 in Brčko District), focused to re-defining budget programme and performance indicators as result-oriented, including defining of sources of information for monitoring these performance measures. In collaboration with the Ministries of

Finance the project, has prepared manuals on the program budget which strongly emphasises practical examples at all levels of government.

In addition, the previous project presented the Road Map with practical steps for establishment of programme budgeting. In accordance with the Road Map for introduction of programme budgeting, legal basis (including by-laws) and building of capacities need to take place before the modifications and upgrades of IT applications (BMIS and Financial Management Information System-ISFU in the Treasury). Decisions on concepts, processes and forms have to be made before modifications of existing IT applications or introduction of new applications. Public finance experts from all levels of government, with the technical assistance provided under this action, will perform detailed functional analysis of requests.

The main lesson under this project is that strategic planning, programme budget, performance monitoring and capital budgeting should be linked. This is a multi-annual process that cannot be easily achieved and that requires a strong basis under the Public Administration Reform, including accompanying legislation. Therefore, this action will contribute to linking strategic planning and programme budgeting (including public investment planning) with performance monitoring.

2. INTERVENTION LOGIC

LOGICAL FRAMEWORK MATRIX

OVERALL OBJECTIVE	OBJECTIVELY VERIFIABLE INDICATORS (*)	SOURCES OF VERIFICATION	
To improve public financial management in Bosnia and Herzegovina	Extent to which fiscal planning, expenditure policy and budgeting is carried out in a multi-year perspective. Progress made towards meeting accession criteria in the area of public finance management	PEFA assessment EC reports on BiH	
SPECIFIC OBJECTIVE	OBJECTIVELY VERIFIABLE INDICATORS (*)	SOURCES OF VERIFICATION	ASSUMPTIONS
To improve the budget planning process	Extent to which the legal basis for the full implementation of programme budgeting is in place	Annual Budget (for revenue and expenditure forecasts) and budget execution report for actual revenue and expenditure Official Gazette at all levels Annual reports of the Ministries of Finance at all levels	Commitment of all levels of government to the reforms; Mutual cooperation of different levels of government during implementation of the action
RESULTS	OBJECTIVELY VERIFIABLE INDICATORS (*)	SOURCES OF VERIFICATION	ASSUMPTIONS
1. Indirect taxation system in BiH is strengthened 2. Medium-term policy planning at all levels of government in BiH is improved and aligned with the process of programme budgeting 3. Human resources capacities for policy planning and linking with programme budgeting enhanced at all government levels in BiH	1.1. % of legal acts and procedures in the area of indirect taxation aligned with the EU <i>acquis</i> and with EU MS best practices. 1.2. Growth rate of indirect taxes 2.1. Number of institutions (state and entity level) with programme budget defined; 2.2. Number of pilot budget users at the cantonal level in FBiH and local self-government units in RS with programme budget defined; 3. Number of trainers / instructors for the programme budgeting and link with strategic planning trained	ITA annual reports Budget execution report for actual revenue and expenditure; GDP data in the Economic Reform Programme Training material; Participating records	Implementation of electronic signature in BiH enabled Active participation of budget users during the implementation of the action

DESCRIPTION OF ACTIVITIES

Main Activities related to **Result 1: Indirect taxation system in BiH is strengthened**, are the following:

Activity 1.1: To deliver, install and to test upgraded IT platform of the ITA IT System,

In order to procure upgraded IT platform, technical specification will be prepared by the beneficiary and will include: hardware, networking items and software specifications. Delivery, installation, testing and training for the users will be implemented within this activity. The new IT platform will be located in the Central Office and in ITA Regional Centres. It will have adequate characteristics in terms of processor speed and memory capacity.

Activity 1.2: To further align relevant legislation in the area of indirect taxation with the EU *acquis* and best practices and to contribute to implementation of NCTS in BiH

It is necessary to prepare a proposal for amending indirect tax legislation with the aim of further alignment with the EU *acquis*, improving tax discipline and collection of revenues. In the area of customs, it is necessary to prepare operation manuals and instructions for practical implementation of newly adopted laws and procedures, and improve forced collection functions, risk analysis and other departments within ITA. Assistance will be necessary in practical implementation of NCTS in BiH.

Main Activities related to **Result 2: Improved process of medium-term policy planning at all levels of government in BiH and alignment with the process of program budgeting**, are the following:

Activity 2.1: To prepare methodologies of the integrated system for planning public policies at all levels of government,

Under this activity, it is necessary to prepare the methodologies of the integrated system for planning public policies at all levels of government defining the method of determining work plans of ministries and other organisations in accordance with the executive authority work plans.

The methodologies regulate the process of strategic planning, starting from determining priorities and objectives of executive authorities, through strategic plans of administrative bodies representing the basis for preparing Annual Work Plan of the executive authorities and Annual Report of the executive authorities. Methodologies should ensure links of the stated process with the programme budgeting process.

Activity 2.2: To improve institutional capacity and procedures for ensuring alignment of mid-term strategies, investment plans and mid-term fiscal framework,

This activity covers preparation and implementation of action plans at the level of executive authorities (Institutions of BiH, Entity and Cantonal Governments and District Brčko) and appropriate local authority bodies on defining budget programme on the basis of policies and service providing area, as well as improvement of budgeting framework (the Law on the Budget System, the Law on the Treasury and the Law on Accounting). By organising and delivering trainings, skills of the employees of Budget departments will be improved to provide further training to other budget users and transferring knowledge, preparation of framework for the new budget approach, including table of revenues and expenses with comprehensive sources of financing aligned with programs, needs analysis for upgrading software for budget preparation BPMIS and treasury system, and reviewing programme structure of budget users in line with the medium-term strategies, investment plans, medium-term work programs and the fiscal framework.

Activity 2.3: To define objectives and individual programmes and create performance indicators or other methods for result measuring of programme objectives, as well as ensure budgeting based on results and policies at all government levels,

This activity will support the budget users and ministries of finance at all levels of government (BiH Institutions, entity and cantonal governments and Brčko District) in the determination of the program and its elements as well as help in the analysis of programs and program elements (objectives, projects, results, indicators, cost estimates) and their finishing. Provide support to the ministries of finance at all levels to implement the methodology of measuring performance indicators, measuring the results of meeting program objectives and providing budgeting based on performance and policies of the government. Analysis of the

needs for more effective monitoring of measuring performance indicators and measurement results of meeting program objectives.

Main Activities related to **Result 3: Human resource capacities for policy planning and link with programme budget enhanced at all government levels in BiH**, are the following:

Activity 3.1: To improve administrative capacities in the domain of programme budgeting,

All previous trainings on programme budgeting have been implemented at the level of the Institutions of BiH, Entities and BD, while the Ministry of Finance and Treasury of BiH, Federal Ministry of Finance, Ministry of Finance of RS, Finance Directorate of BD and pilot budget users benefited the most from individual workshops, defined programs and performance indicators. Previous IPA project implemented a two-day training of lecturers/instructors for program budget encompassing 10 participants from Ministries of Finance (3 from MFT BiH, 3 from FMF and 4 from MF RS). Since the training was exclusively based on the concept of program budget and not on its connectedness with strategic/medium-term plans developed thereafter, it is necessary to organise new training of lecturers/instructors in this view. This action envisages additional training for a number of lecturers/instructors and it will encompass not only employees of Ministries of Finance, but also a certain number of budget users' employees. Training would include a series of three-day workshops for at least 4 groups of 20 participants. The second part of training on concepts and methodology of program budgeting, including implementation of Program Budgeting Manual will include FBiH Cantons and 32 selected local self-government units in RS since these were not included in previous training.

RISKS

At the level of measures and related activities of this action, the assumptions are as follows:

- Commitment of all levels of government to the reforms;
- Mutual cooperation of different levels of government during implementation of the action;
- Active participation of budget users in implementing the action.

Risks that may arise during the implementation of the proposed activities are:

- Electronic signature still not being implemented in BiH;
- Relevant legislation (necessary to implement simplified procedures) not adopted or implemented;
- Lack of capacities and understanding of the local level institutions of programme budgeting;
- Complex fiscal structure and the scope of the action require stable relations and cooperation between experts and close mutual cooperation between experts and users for the needs of achieving action objectives.

Mitigation measures are as follow:

- The ITA (through its Governing Board) will have communication with the Council of Ministers of BiH and will advocate for implementation of e-signature and adoption of legislation;
- The ITA will proactively support the adoption of implementing regulations necessary for the implementation of simplified procedures
- The third risk will be mitigated through creating sustainable capacities through comprehensive training programme and active participation of budget users in establishing the process;
- Selection of a team of experts and engagement of sufficient number of additional experts (non-key experts) possessing detailed understanding of the administrative structure and all aspects of public finance in BiH.

CONDITIONS FOR IMPLEMENTATION

To ensure effective and timely implementation of activities 1.1 and 1.2 of the action, the implementation of electronic signature in BiH has to be ensured before the action starts. There are no conditions for effective and timely implementation of programme budgeting.

3. IMPLEMENTATION ARRANGEMENTS

ROLES AND RESPONSIBILITIES

The main beneficiary of the action in area of indirect taxation is the Indirect Taxation Authority of Bosnia and Herzegovina. In 2003, the Parliamentary Assembly of Bosnia and Herzegovina adopted the Law on Indirect Taxation System, thus securing the legal basis for establishment of the Indirect Taxation Authority (ITA), the largest State-level institution with more than 2400 employees. ITA is an independent administrative body responsible for its activities to the Council of Ministers of BiH through its Governing Board. Operations of ITA cover the area of indirect taxes (customs duties, VAT, tolls and excise duties).

Main stakeholders when it comes to programme budgeting are the ministries of finance at all levels and staff responsible for strategic planning. Main beneficiaries of the action are budget users of the Institutions of BiH, FBiH (including Cantons), RS and 32 selected local self-government units in RS, and BD. The main criterion for the selection of the local administration in RS will be the size of the budget and regional representation.

Steering Committee will be established to oversee implementation of the action.

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

The EU Delegation to Bosnia and Herzegovina will be responsible for the overall management and implementation of the action under direct management mode. The action will be implemented through three contracts:

- One procurement contract for supply of upgraded IT platform enabling interoperability of BiH with EU VIES and transit system;
- One Twinning contract for support to further alignment with the EU *acquis* on indirect taxation;
- One contract for provision of services (TA) related to implementation of programme budget activities.

The choice of twinning for support to further harmonization with the EU *acquis* on indirect taxation is based on Indirect Taxation Authority's positive experience with other twinning projects under previous IPA projects and adequate ITA capacity for its absorption. TA has been assessed as the most appropriate implementation method for the activities on programme budgeting since the project lasts for two years and it requires a significant number of expertise on all levels of government and full engagement of three key experts experienced in introducing and implementing program budgeting. We believe that no member country can provide such an expert calibre over the long term. In addition, we focused on the fact that users from lower levels of government (Cantons in FBiH and local self-government units in RS) have no previous experience in twinning programs, resulting in unsatisfactory level of their maturity and capacities for absorbing the twinning contact.

4. PERFORMANCE MEASUREMENT

METHODOLOGY FOR MONITORING (AND EVALUATION)

In line with the IPA II Implementing Regulation 447/2014, an IPA II beneficiary who has been entrusted budget implementation tasks of IPA II assistance shall be responsible for conducting evaluations of the programmes it manages.

The European Commission may carry out a mid-term, a final or an ex-post evaluation for this action or its components via independent consultants, through a joint mission or via an implementing partner. In case a mid-term or final evaluation is not foreseen, the European Commission may, during implementation, decide to undertake such an evaluation for duly justified reasons either on its own decision or on the initiative of the partner. The evaluations will be carried out as prescribed by the DG NEAR guidelines on linking

planning/programming, monitoring and evaluation¹. In addition, the action might be subject to external monitoring in line with the European Commission rules and procedures set in the Financing Agreement.

¹ https://ec.europa.eu/neighbourhood-enlargement/sites/near/files/pdf/financial_assistance/phare/evaluation/2016/20160831-dg-near-guidelines-on-linking-planning-programming-vol-1-v0.4.pdf

INDICATOR MEASUREMENT

Indicator	Baseline (2016) (2)	Target 2020 (3)	Final Target (2022) (4)	Source of information
Indicators for the Overall objective				
Progress made towards meeting accession criteria in the area of public finance management	At an early stage	Moderately prepared	Moderately prepared	EC reports for BiH
Extent to which fiscal planning, expenditure policy and budgeting is carried out in a multi-year perspective	D+ (2013)	C+	B	PEFA assessment
Indicators for the Specific objective				
Extent to which the legal basis for the full implementation of programme budgeting is in place	Budgets are based on economic classification	Legal basis (including secondary legislation) for implementation of the programme budget is prepared	Budgets are based on economic and program classification where both economic and programme classification are legally binding	Draft annual budgets of the institutions in BiH, FBiH, RS and Brcko District
Results indicators				
1.1. % of legal acts and procedures in the area of indirect taxation aligned with the EU <i>acquis</i> and with EU MS best practice	10%	30-40%	50-60%	ITA Annual Report EC reports on BiH
1.2. Growth rate of indirect taxes	3.6%	3.2%	3.2%	ITA Annual Report OMA bulletin
2.1. Number of institutions (state and entity level) with programme budget defined;	32	162	247	Final Project Report Annual Ministries of finance Reports
2.2. Number of pilot budget users at the cantonal level in FBiH and local self-government units in RS with programme budget defined	0	82	164	Final Project Report Annual Ministries of Finance Reports
3. Number of trainers / instructors for the programme budgeting and link with strategic planning trained	10	90	90	Final Project Report; Training material; Participating records

5. SECTOR APPROACH ASSESSMENT

All three levels of government in BiH started preparing Public Finance Management Reform Strategy with an Action Implementation Plan, and will represent consolidated Public Finance Management Reform Strategy in BiH, prepared on a modular principle, observing specificities of BiH organisation and level of achievement of different levels of government in particular areas. Following the recommendations of the EC in the Country Report for BiH for 2015, these strategies represent one of the key areas and pillars of public administration reform in BiH, and they will be integrated in the framework of the new Public Administration Reform Strategy in BiH. Preparation and adoption of the consolidated Public Finance Management Reform Strategy in BiH represents the basis for further support under IPA instruments and one of the preconditions for using sectoral budget support under IPA. Implementation of measures from the single Strategy will improve the public financial system in order to ensure better functionality, transparency, responsibility and efficiency in public financial management, thus contributing to increased macroeconomic stability in BiH.

The individual strategies of institutions of BiH, FBiH, RS and DB are at varying degrees of development. In December 2016, the Council of Ministers adopted the Public Finance Management Reform Strategy 2017-2020, with an Action Plan, while strategies at lower levels of government are still being prepared.

Public Finance Management Reform Strategy in the Institutions of BiH defines the method of monitoring Strategy and Action Plan implementation. On the occasion of adoption of the Strategy by the Council of Ministers, the Working Group for preparation of the said Strategy was additionally instructed to monitor implementation of the Action Plan in terms of its objectives and results and to report on the same. At the initiative of the Ministry of Finance and Treasury of BiH, and in their organisation, the Group will hold semi-annual meetings during which progress will be assessed on the basis of reports provided by its members. In turn, the Ministry will prepare a report on the same. These meetings will also represent an opportunity for analysing political, administrative, institutional or financial risks related to achieving reform objectives. In case of difficulties or delays in implementation, certain measures will be agreed upon. Starting from February 2018, the Group will submit an annual report on implementation of the Strategy Action Plan to the Council of Ministers. The Group will determine the date for assessment of Strategy implementation which will result in medium-term analysis of achievements, further development of indicators and necessary modification of activities.

The Federal Ministry of Finance prepared the Strategy document and submitted it for comments to IMF and SIGMA. It is expected for the Strategy to submit to the Government for adoption in March 2017. The same applies for the Public Finance Management Reform Strategy of BD.

At its 77th session held on 9 June 2016, the Government of RS adopted a Decision on appointment of a Working Group for preparation of the 2016-2020 RS Public Finance Management Reform Strategy. The Work Group is instructed to analyse public finance management in RS, to identify key public finance management reform areas for the period between 2016 and 2020, and to prepare a Public Finance Management Reform Strategy Document for the same period, including an Action Plan for its realisation and submit it to the Government of RS for their consideration and adoption. The Strategy is currently under preparation and its adoption is expected in the first quarter of 2017.

Responsibility for coordinating of donors in Bosnia and Herzegovina is divided between the Directorate for European Integration (DEI) for EU donors and the Ministry of Finance and Treasury (MFT) BiH for other donors, in coordination with relevant entity institutions, and joint responsibility is shared with relevant entity Ministries when it comes to international financial institutions (IFIs). MFT BiH regularly organises meetings of the Donor Coordination Forum and publishes annual reports on donations, representing donors active in Bosnia and Herzegovina and determine their contribution under sectors. Moreover, EU Delegation holds regular coordination meetings with EU member countries in order to exchange political views and direct the coherent and complementary EU assistance and member countries assistance for BiH.

EU Delegation cooperates with other donors through its regular participation in Donor Coordination Forum organised by MFT two or three times a year.

6. CROSS-CUTTING ISSUES

GENDER MAINSTREAMING

It is expected that gender equality objectives will be fully observed in drafting the legislative framework and regulations. Regarding all capacity building activities, these will be available and accessible equally to men and women. Envisaged training(s) will be equally available to men and women. Gender sensitive language will be maintained throughout the entire project cycle. All analyses and drafting legislation will be conducted using gender-sensitive methodologies, and gender will be mainstreamed in all activities and deliverables related to the implementation of this action. In general, gender perspective will be maintained ensuring that the results of the project impact positively on gender equality as well.

EQUAL OPPORTUNITIES

Based on the fundamental principles of promoting equality and combating discrimination, the benefits of the action will be guaranteed on the basis of equal access regardless of sex, racial or ethnic origin, religion or belief, disability, age or sexual orientation.

The principles of equal opportunities are duly taken into account throughout the project cycle and the action will promote an environment that is conducive and enabling to gender equality, ensuring equal participation of women and men in all action activities, as well as taking into account promotion and participation of people with disabilities.

MINORITIES AND VULNERABLE GROUPS

Bosnia and Herzegovina is committed to a policy of social inclusion of minority and marginalised social groups, notably Roma, persons with disabilities, young persons, internally displaced persons. During implementation of activities anticipated in the action, full respect of minorities and vulnerable groups will be ensured. Thus, during the implementation of the action, there shall be no direct or indirect discrimination against any person based on gender, age, marital status, language, sexual orientation, political affiliation or conviction, ethnic origin, religion, social origin or any other status.

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

Civil society organisations have been consulted throughout the design of the intervention which is supposed to represent the basis for the action development. When it comes to the implementation of this specific action, all envisaged activities will be open to cooperation and setting of synergies with CSOs and other interested non-state stakeholders.

ENVIRONMENT AND CLIMATE CHANGE (AND IF RELEVANT DISASTER RESILIENCE)

The Action aims at strengthening public finance management in order to ensure efficient, transparent and responsible public administration in BiH. As such, the action is environment and climate change-neutral. The activities deriving from this action will be delivered in the most environmentally friendly possible way.

Climate action relevant budget allocation: EUR 0

7. SUSTAINABILITY

The action represents continuation of assistance provided in the previous period through IPA projects in the area of strengthening ITA capacities, as well as continuation of efforts of ITA aimed at further alignment of BiH legislation with the EU *acquis* in the area of taxes, customs duties and excise duties. Installation of the new IT platform will improve efficiency of ITA operations through further strengthening of capacities and transfer of acquired knowledge to other institutions, thus resulting in removing certain obstacles represented by current outdated technology. Likewise, it will ensure efficiency of the indirect taxation system and improved collection of indirect tax revenues, representing one of the main objectives of the action.

Implementation of this action will enable preparation of more quality programme budget documents and strengthening capacities of budget users, in particular the ministries of finance, for preparation of budget documents in programme format in the future. In addition, improving staff skills enables creation of capacities for training to be provided for other budget users and transfer of acquired knowledge. Improvement of the legal framework and a wider range of users under the action will contribute to faster

establishment of programme budgeting and transition from conceptual to practical reform implementation. Continuation of improvements related to public financial management will enable further improvements of the efficient budget management and result in more efficient public administration and achieving better value for money. Continuation of EU assistance through technical assistance envisaged by this action is of great importance, since it directly facilitates realisation of activities from PFM reform strategy, improves results of previous projects in the same area and enables continuity in terms of introduction of program budgeting. Proposal for this action will not only improve effectiveness and efficiency of public finance management through strengthening dependencies between priorities of economic policies, strategic planning and budget with the aim of efficient exploitation of spending resources, but will also result in strengthening of sectoral approach necessary for utilisation of IPA funds.

8. 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 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. These measures include three press conferences: one at the beginning and one at the end of the action implementation. The third press conference will be held after the realisation of the supply contract and testing of upgraded IT platform enabling future interoperability of BiH with EU VIES and transit system. For seminars and workshops, communication and visibility will be provided through the printing of corresponding leaflets and brochures, all in accordance with the Communication and Visibility Manual for EU External Actions Additional Visibility Guidelines developed by the European Commission (DG NEAR) will have to be followed.

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 and will promote transparency and accountability on the use of funds.

