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KOSOVO | GROWTH AND FISCAL STABILITY INITIATIVE

QUARTERLY REPORT
30 SEPTEMBER 2011

Contract Number EEM-I-00-07-00005-00, Task Order 09

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1 CHIEF OF PARTY REPORT

The September quarter was dominated by activities to support the government implementation of the Economic Development and Vision Action Plan (EDVAP). GFSI provided direct support to the Ministry of Finance (MoF) to conduct a Strategic Expenditure Review (SER); examining current budget settings, conducting an analysis of regional and international comparisons of budget structure; and, the full costing of all EDVAP initiatives. The Project team also analyzed the establishment of a public policy unit within the MoF consistent with the EDVAP recommendations. The Minister has endorsed the report which recommends an expansion of the current macro-economic unit into a broader economic and public policy department.

During the quarter, the government also moved substantially to meet the conditions precedent in the task order regarding the provision of technical assistance to the Privatization Agency of Kosovo (PAK), with the passing of key legislation governing the Privatization Agency, Special Chamber of the Supreme Court and liquidations processes. It is expected that the package of legislation will be a catalyst in releasing approximately 500 million Euro from the PAK Trust Fund through a more streamlined liquidation process, with a significant portion of the Trust Fund potentially being released to the government (once claims have been resolved). Another implication of the revised legislation is the simplification of the processes to resolve the Trepca complex. PAK will now be able to undertake the role of Administrator of Trepca and resolve creditor claims and propose restructuring under the supervision of the Special Chamber.

Another significant outcome in the quarter was confirmation of GFSI previous activities working with municipalities on improving the quality of their financial statements of 2010. The Auditor General published the municipality audit reports which showed that a total of twelve (12) municipalities achieved unqualified audit reports in 2010, up from two (2) in 2009. GFSI has now undertaken a thorough analysis of the 2010 municipal reports and is developing an intervention strategy, similar to the previous year, with close cooperation with the Treasury and Auditor General.

Project support to municipalities also continued during the quarter with the launch of six new Public Expenditure and Financial Accountability (PEFA) assessments. The GFSI team also assisted in the development of an Action Plan for the municipalities included in the initial PEFA assessments to improve financial management practices for these municipalities.

In Budget, the government reached an agreement with the International Monetary Fund (IMF) on the budget structure for 2012 and the government is continuing to develop the budget within these parameters. A future reform program for budget reform will be recommended in the SER report.

In Public Private Partnerships (PPP), GFSI has now focused more heavily on the development of training materials to support a comprehensive training agenda to be rolled out across Kosovo on all aspects of PPP while continuing to support the live transactions underway in various municipalities.

Within Information Technology (IT), the Ministry of Public Administration has now confirmed the allocation of accommodation to the MoF within the government building for a dedicated server room to house all MoF IT server applications. A term of reference has been developed to procure a firm to undertake the necessary fit out and it is expected that all MoF servers will be housed in the one location early in 2012. The MoF IT organizational structure has also been approved and options for its implementation are under discussion with the Permanent Secretary.

2 CROSS-CUTTING THEMES

The core areas of USAID/Kosovo's Strategic Plan 2010-2014 identifies cross-cutting factors as having a profound effect on the development environment in Kosovo. They are: 1) youth integration; 2) gender equality; 3) full participation of minorities; and 4) protection of Kosovo's environment. Cross-cutting themes have been taken into account during the work planning phase and are addressed where possible in day to day activities and program design.

Twelve (12) municipalities received unqualified audit reports in 2010, up from two in 2009. Enhancing the quality of end of year audited accounts enhances transparency in public finances.

New legislation governing the liquidation process, will aid clarity and transparency in liquidation and restructuring processes.

Training was conducted for the PPP Unit and Ministries/municipalities on PPPs and the environment. Follow up assistance was provided to the Ministry of Environment on their policies and processes as they applied to PPP projects.

2.1 REPORTS AGAINST RESULT AREAS

2.2 OBJECTIVE 1

Support private sector participation through Public-Private-Partnerships and through support to the Privatization Agency of Kosovo

A – Public-Private-Partnerships: Strengthen the ability and capacity of central and local institutions to identify, develop and implement Public-Private-Partnership (PPP) projects as an important private sector funding mechanism for meeting Kosovo's public infrastructure investment priorities.

PROGRESS/SUCCESS AGAINST THE WORK PLAN

The Public-Private-Partnership component team continued to make progress against the work plan during the reporting period:

Framework Strengthening: To strengthen the PPP program, GFSI advisors worked on multiple fronts to strengthen the legal, institutional and policy framework for PPP. We continued drafting a new PPP Law and secondary legislation (Directorates) in accordance with the PPP framework strategy and work plan. The new PPP Law, which was adopted by the Government and approved by the Budget Committee of the National Assembly, is currently under review by the National Assembly. The PPP Inter-ministerial Steering Committee also adopted Directive No. 3/2011 that addresses the review and approval process of municipal projects. The passage of the new PPP Law and Directive No. 3 aims to streamline and increase the efficiency of PPP application process for municipalities, while creating greater procedural and legislative clarity for passage of all PPPs.

GFSI advisors also completed most of the legal "due diligence" of all laws that could affect the implementation and operation of a PPP. The "due diligence" included review of general laws, as well as sector specific laws that may affect PPP transactions. A GFSI advisor also participated in the drafting and/or reviewing the Inter-municipal Cooperation Law and the Waste Law.

As part of the framework strengthening, the GFSI is currently developing PPP Guidelines that will be used by the PPP Unit within the MoF, the line ministries, municipalities (when acting as contracting authorities) and ultimately private sector investors, operators and technical/transaction advisors. During the development of the environmental component of the guidelines, GFSI advisors identified significant challenges in the implementation of the environmental laws and sector specific directives. These issues will impact the implementation of PPP's and other development opportunities in Kosovo. Dialogue is continuing with the government to further understand and address these issues.

Transaction Support: As of the end of the quarter, the PPP Unit with the support of the GFSI PPP Team, had in excess of twenty-five (25) potential municipal and central government PPP transactions in the pipeline. The projects range in size from 1 billion Euro in capital investment (Route 6 BOT) to projects just below 1 million Euro (e.g. Peja Urban Transport). Although most projects are in the prefeasibility study stage, six projects are either in the full feasibility study stage or beyond. Some of the projects that are beyond the prefeasibility stage include the following:

- Draft procurement documents -- Request for Qualifications (RfQ), Request for Proposals, draft contract -- were submitted to the Municipality of Pristina for three underground parking facilities with commercial premises. An RfQ was issued and four qualified bidders were identified (short-listed) during the pre-selection phase. Publication of Request for Proposals is pending. Each parking facility, which range in capital value 2 and 7 million Euro, will be awarded separately to local and regional private operator and investor groups.
- A feasibility study and options analysis was prepared by the IFC, as transaction advisors, on entering into a PPP on four existing solid waste landfills and one existing transfer station. The GFSI team recommended that the options analysis be revised and expanded upon considering the very high level of Government risk the IFC expects under the recommended structure. The structure of the project is expected to be determined within the next quarter and assuming an acceptable structure is identified, the projects will be awarded to one or more domestic and/or international private entities during the following year.
- Draft procurement documents -- Request for Qualifications, Request for Proposals, draft contract -- and a feasibility study were completed for Peja urban transport project. The project was presented to and approved by PPP-ISC in September.
- Draft procurement documents -- Request for Qualifications, Request for Proposals, draft contract -- and a feasibility study were completed for a Waste Collection and Separation project in the Municipality of Suhareka. Although the PPP-ISC determined that all conditions to approve the project were met, final approval was delayed until the next PPP-ISC meeting.

Two noteworthy projects within the prefeasibility study stage are the Mitrovica Solid Waste Management (collection, recycling and landfill) and the Pristina Urban Bus System. Progress is expected to move forward through the next quarter.

PPP Contract Governance and Oversight: The GFSI Team assisted the PPP Unit in preparing a procurement/tender dossier with the following documents in compliance with local legal norms and international best practices:

- PPP-ISC adopted standard "Request for Qualifications" form.
- Adoption of standard form "Request for Proposals" and standard "concession contract for municipal projects" is pending PPP-ISC decision.
- Standard financial prefeasibility document format and financial models have been developed and are waiting for PPP-ISC review and approval.

- Standard financial feasibility study, financial models and Public Sector Comparator have been developed and are waiting PPP-ISC review.

Training: During the quarter the combined GFSI and PPP Unit Team were active in both individual training and developing a sustainable training program. The Team trained 126 central and municipal officials in the 5 Kosovo regions on PPP in general, the procurement process and contracts. In addition, the GFSI-PPP Unit Team organized custom training programs for Peja and Suhareka. The sector specific training was on the tendering process (RFQ, RFP, contract) and contract management/monitoring.

The PPP Unit, with the support of GFSI advisors, is establishing formal relations with the Kosovo Institute of Public Administration (KIPA) to develop a sustainable PPP training program that will focus on civil servants engaged in PPP activities. In addition to supporting curriculum development, GFSI advisors will develop PPP training modules based on the PPP Guidelines described above. GFSI will also assist in the hiring and training of technical experts.

ISSUES/OBSTACLES

Although municipal and central government responsibilities are clearly set forth by law, mistrust and misunderstanding continues to exist among both levels of government that needs to be overcome with the support of senior central and municipal government management.

Lack of clarity for the issuance of Environmental Permits and a lack of a clear policy delineating economic development and environmental protection goals are likely to result in delays for the development and implementation of PPP projects and other capital project.

A PMU for the Pristina International Airport concession has still not been established, more than a year when it was required. The PPP Unit is not acting with any urgency to resolve this matter, especially since the PPP-ISC has appointed the PPP Unit as the interim PIA PMU.

COORDINATION

GFSI coordinated activities with the European Commission and European Commission Liaison Office, and the following USAID funded projects BEEP, SEAD and DEMI.

B – Privatization: Targeted technical assistance to the Privatization Agency of Kosovo (PAK) will be provided with the intention of bringing the liquidation of the more than 600 privatized SOEs to timely closure, putting the nearly €440 million of privatization proceeds currently held in trust and invested outside Kosovo to work in the Kosovo economy.

PROGRESS/SUCCESS AGAINST THE WORK PLAN

In the quarter, the Government, with substantial project assistance, met most of the conditions precedent to this activity by developing and submitting to the Assembly a new Law on the Privatization Agency of Kosovo (PAK Law), a new Law on the Special Chamber (Special Chamber Law) and a new Law on the Reorganization of Certain SOEs (Reorganization Law); and all three were adopted by the Assembly with only minor, workable, changes. The new legislation, which deviates somewhat from the applicable provisions of the Comprehensive Proposal (CP), was reviewed and approved by the ICR; the ICR invoked his absolute authority to interpret the CP and found that the deviations were necessary and therefore acceptable under the CP.

The projected time to complete the liquidation of an enterprise is now reduced considerably from an average of 46 months which has been the experience to date.

The new legislation also authorizes the PAK to begin the process of transferring “surplus” funds (funds that are identified as not being necessary to satisfy worker, owner or creditor claims) from the trust funds and into the Kosovo Consolidated Fund. The Law also authorized the PAK to transfer a small percentage from trust fund into a new dedicated revenue account of the PAK, in order to compensate PAK for the costs it incurs in administering SOEs (normal practice in Europe, the US and elsewhere). This new “dedicated revenue” provision will not only assist PAK to become self-funded, it will also provide PAK with the resources needed to engage a team of outside international professionals to assist PAK implement the new legislation (see discussion immediately below).

ISSUES/OBSTACLES

Notwithstanding the major step forward taken with the adoption of the new legislation, substantial issues – which are principally personnel issues - remain if the opportunity created by that legislation is to be realized. PAK currently lacks sufficient quality professionals (legal, liquidation and reorganization) to implement the new legislation effectively. Both the new PAK Law and the new Reorganization Law have clearly anticipated this issue and require PAK to procure the services of a team of outside professionals: (1) to take over the leading role (from the ICO) of each of the five regional liquidation committees; (2) to provide leadership in PAK’s litigation of claims before the Special Chamber; (3) to represent Trepca before the Special Chamber and to develop and advocate a plan of reorganization; (4) to organize and review the thousands of claims that have been received by PAK; and (5) to provide other expert advice to PAK as needed.

Coordination

The Project closely coordinated its assistance during the quarter with the senior management of PAK, the senior staff of the ICO and the team leader of the ECLO project at PAK providing liquidation assistance.

2.3 OBJECTIVE 2

A – Fiscal Stewardship: Build professionalism and expertise in sound public financial management in municipalities so that they become institutions capable of autonomously and efficiently stimulating local economic development while providing a high standard of public services.

PROGRESS/SUCCESS AGAINST THE WORK PLAN

The Municipal PFM component continued to make progress against the work plan during the quarter:

Local Government PEFA Self-Assessment: This reporting period concluded the work with the first round of PEFA municipalities (Pristina, Shtprce, Podujevo, Vushtri and Mumusha). After the completion of individual PEFA reports for all five municipalities, meetings were organized and final reports in hard copies and CDs were delivered to mayors and municipal teams. GFSI advisors suggested that the report be sent to the Assembly for information; posted on official municipal web site; and introduced to local media through a press release. Some municipalities already undertook these actions. The concluded assessments were followed with extensive preparatory work to develop a Municipal PFM Reform Action Plan to address weaknesses in

public finance management identified during the assessments, while taking into consideration the National Government PFM Reform Action Plan produced in 2009.

Municipal counterparts participated in a workshop (September 6, 2011) in Pristina and, together with GFSI advisors, worked on the Municipal PFM Reform Action Plan. The transfer of the final Municipal PFM Reform Action Plan to respective municipalities is scheduled to take place at the beginning of the next reporting period. Municipalities are expected to implement action plan recommendations supported by GFSI advisors and the dedicated team appointed by each mayor.

During this reporting period, the official launch of second round of local PEFA assessments in additional six municipalities (Peja, Istog, Novoberde, Ferizai, Gjillan, and Glakova) was followed by a two day PEFA methodology training workshop for municipal practitioners appointed by Mayors and commencement of the evaluation of PEFA activities. GFSI advisors established weekly PEFA sessions in each municipality to facilitate collaboration with municipal counterparts, building capacity and relevant skill development are a key product of these efforts. The next reporting period is expected to mark the completion of assessment for 28 PEFA indicators by municipal counterparts and GFSI advisors in all six municipalities.

In addition to work with municipal counterparts, the GFSI Team conducted series of meetings and consultations with key stakeholders in the PFM area -- MOF Treasury Department, MOF Property Tax Department, and EU-PIP project under the EU Support to Improving the Quality of Public Investments in Kosovo and Preparing the Ground for EU Funding -- to solicit input into the assessment process.

Municipal MTEF: In anticipation of the 2013 budget cycle, the Project Team initiated planning for the next phase of GFSI support to the implementation of municipal MTEF by the Municipal Budget Department in MoF and municipal budget practitioners. Taking into account the 2012 budget experience, further amendments to the MTEF technical guidance and templates were considered. Additional materials on MTEF approach for municipalities will be finalized by the end of next reporting period. A train the trainers initiative will be delivered for Municipal Budget Department analysts to strengthen outreach, roll out, and support for the implementation in all municipalities.

ISSUES/OBSTACLES

GFSI activities did not encounter any major obstacles during this quarter. The cooperation with six PEFA counterpart municipalities was excellent and activities progressed in accordance with the work plan. Municipal staff deserves credit for their engagement, enthusiasm, and professional contributions.

COORDINATION

The GFSI dialog with other donors included EU Twinning project and DFID project supporting the decentralization of social services. GFSI advisors were asked to contribute a presentation on challenges and opportunities of decentralization of social services at the annual Conference on Social Services organized by Ministry of Labor and Social Policy with the support from Kosovo Social Services Decentralization project. The Conference will be held in November 2011 and will gather the key stakeholders in the area of planning and delivering municipal social services.

B - Assist the Office of the Auditor General (OAG) so that their ability to review and assess the fiscal operations of the municipalities is strengthened and made more timely and effective.

PROGRESS/SUCCESS AGAINST THE WORK PLAN

The objective of the GFSI support is to assist the Municipalities improve the quality and content of their Annual Financial Statements to increase the number of Unqualified Audit opinions of the 2011 Financial Statements. Of the 2010 Annual Financial Statements, 12 Municipality statements received an “Unqualified with an Emphasis on Matter” Opinion while the remaining 25 Municipalities statements received a “Qualified Opinion” (16 Municipalities) or “Disclaimer of Opinion” (9 Municipalities).

The GFSI team conducted an analysis of the 2010 Auditor-General’s reports, summarizing findings and identifying common themes. The common themes include:

- inadequate systems;
- the lack of good record keeping;
- poor business practices;
- lack of procedures and controls;
- lack of knowledge of procurement processes and reconciliation processes.

The next stage is to identify practical strategies to help overcome shortcomings identified in the 2010 statements, and to increase the number of Unqualified opinions in the 2011 Financial Statements.

C – Assist the MOF to develop and implement an action plan to enable data sharing among the various legacy IT systems in the ministry

PROGRESS AGAINST THE WORK PLAN

Key meetings were held with the Minister of Finance and Permanent Secretary on the way forward to develop the IT department and infrastructure for the long term needs of the MoF. The Minister expressed his support and delegated authority for dealing with IT issues to the Permanent Secretary.

As follow up on this meeting, the IT Advisor prepared a comprehensive document describing the current IT Organizations within the MoF; outlining the problems with the current state of IT organizations; and proposing a new single IT Organization for the MoF HQ supplemented with detail description of the responsibilities of the key staff within the proposed organization. The document also contains a high-level roadmap for executing the IT Transformation at the MoF that will lead to better ICT Services, including solutions for data exchange and utilization of data from different systems for operational and management purposes. One of the goals of IT Transformation is to build an Integrated IT Infrastructure for the entire Ministry (including TAK and Customs) and shared services for its support and maintenance.

A separate document containing: (1) proposed position levels, as per the new law on civil servants, for key staff within the proposed IT Organization; and (2) skills requirements for each position was also created. The purpose of this document was to serve as a source for carrying out recruitment activities. Both documents were accepted by the Permanent Secretary. Work continued on the implementation of the proposed organizational structure and initiating recruitment for recommended key positions.

During the reporting period the Property Tax department opened accounts for staff of the TAK and trained them how to access the system, search, and retrieve data (*follow up from previous*

reporting period). The IT advisor also analyzed the reporting capabilities of the Property Tax System and designing a set of operational and management reports to be developed.

During the reporting period a set of IT Policies and Procedures was finalized and submitted to the legal division for formatting in required form and translating in Albanian and Serbian, before formally approved and distributed to all MoF employees.

ISSUES/OBSTACLES

Confusion over the IT leadership within MoF remains an obstacle to IT Transformation and continues to delay significant milestones necessary for the IT Transformation at the Ministry.

COORDINATION

GFSI organized a meeting between LOGOS, a Switzerland project, and SIDA Property Tax Project. The meeting was held on-time to ensure consistency of actions and efficiency of work, supplementing not overlapping.

D – Assist the MOF to assess remaining priority capacity building needs in the Ministry's Budget and Treasury functions and design and conduct training programs to address those needs ties.

PROGRESS/SUCCESS AGAINST THE WORK PLAN

The third quarter was dominated by negotiations with the IMF and the requirement to meet fiscal targets set out in the IMF Staff Monitoring Program. Funding of election promises and subsequent expenditure commitments affected the budget and required a major exercise to identify cost savings.

A strategic expenditure review (SER) was commenced in the third quarter, under the auspices of GFSI and in cooperation with DFID. The SER will be completed in October, and is expected to influence the government to focus on the need for stronger central control over the planning framework and greater commitment to the medium term budgetary framework.

Fundamental to stronger planning and coordination capacity will be a rationalization of the budget's program structure, which is currently based on units within Budget Organizations rather than around sectoral spending areas. This exercise will need to be supplemented with the specification of performance indicators for each program, and a linking of programs to a high level classification structure of government goals/targeted outcomes. To this end, a new Budget Advisor commenced work in mid-September 2011, whose major focus is to develop a proposal for government to rationalize the budget's program structure and to develop a program performance indicator monitoring framework that links with national strategic planning and organizational corporate planning.

The 2012 budget preparations continued during the quarter, with GFSI providing overarching assistance in budget structure and the development of the 2012 Appropriations Law.

Also during the reporting period, GFSI advisors assessed the training needs for internal auditors in all budget organizations in relation to the decentralization of the KFMIS Expenditure Management from Treasury. GFSI advisors supported the Treasury training coordinator in developing associated educational and training materials. A total of 126 representatives (71 males and 55 females) from different budget organizations received training in seven KFMIS functions (commitment, internal control, internal audit, goods receiving, expenditures, and certifying) during the quarter.

ISSUES/OBSTACLES

Budget execution in 2012 will need to be tightly controlled if the Kosovo budget is to be prevented from slipping into breach of the IMF agreed expenditure and revenue targets.

COORDINATION

GFSI coordinated during budget preparations with the United States Treasury Advisor for debt issues.

DFID will fund an international advisor to work with the Strategic Planning Unit (SPU) in the Office of the Prime Minister. It will be important that the performance monitoring framework at the national planning level dovetails with the performance monitoring framework developed for programs. Meetings will be arranged in the next quarter to ensure an adequate level of coordination takes place.

E – Assist the MOF to ensure that the Ministry's property tax department and supporting systems remain robust and capable of meeting the own-source revenue needs of municipalities.

PROGRESS/SUCCESS AGAINST THE WORK PLAN

GFSI Advisors continued efforts to enhance the capacity of Property Tax Department (PTD) to perform quality audits. As per the initial plan developed in cooperation with the PTD, the reforms were successfully implemented in three pilot municipalities (Pristina, Shtime and Shterpce). The focus of the reforms was unifying and improving the underlying audit processes, reporting and the introduction of a feedback mechanism. The audit of the remaining municipalities will be conducted on a full annual basis and performed during the period of January – March 2012.

The GFSI team continued to assist municipalities in preparing for the implementation of the new appraisal model. Training was provided to Finance Directors and Property Tax Managers in more than half of municipalities in the use of the tool developed in cooperation with SIDA. The tool enables simulation of projected revenues with the implementation of the new appraisal model. Analysis of the data acquired from the resurvey suggested that the implementation of the new model would result in the decline in overall valuation and taxation in 2012 in all municipalities if the 2011 tax rates were applied. Municipalities were advised to increase their valuation of properties or tax rates for year 2012, register unregistered properties and collect previous debt. Training and support will continue until all municipalities have implemented the new model.

Following GFSI and SIDA recommendations, the MoF officially approved the PTDs request for procurement procedures to retain the IT Developers of the PTS System. The procedures are set to start during October and conclude by the end of the year, before SIDA funding for the staff expires. This will ensure sustainability of the Property Tax Project and further maintenance and development of the PTS System.

The GFSI team, in cooperation with SIDA, trained staff from TAK in the usage of the PT System and coordinated efforts to enable their access. In addition to the earlier implementation of FIN (Financial Identification Number) in PTS, the training will further increase TAK ability to identify delinquent taxpayers and enforce collection.

ISSUES/OBSTACLES

The property resurvey process has started for 24 municipalities and has been completed for 68% of all properties. While most of the municipalities are in final stages of completion there are still 8 municipalities, including Pristina, that have not undertaken the resurvey. The resurvey

continues to be a challenge in Serbian majority municipalities. Due to the new appraisal model being dependent on the data acquired during the resurvey process, there is a risk that the new model will not be implemented in 2012 in the municipalities where resurvey is not finished.

2.4 OBJECTIVE 3

Economic Policy Assistance – Development and implementation of an action-oriented Government strategy for profitable private sector growth and the attraction of foreign direct investment through technical assistance provided to the relevant counterpart institutions and closely coordinated with other USG-funded development initiatives.

PROGRESS/SUCCESS AGAINST THE WORK PLAN

The GFSI project assisted the MoF's SER Team in accordance with the Government's approved terms of reference for the SER. A review of Kosovo's historical and planned functional expenditure from 2007 to 2014 was conducted, which confirmed that past and future expenditures are aligned with economic policy priorities contained in the Economic Development Vision Action Plan (EDVAP). This confirms that the government is implementing policy initiatives that create better conditions for the functioning of a competitive market, strengthening private sector, supporting employment generation, improving the image of Kosovo for investment, and creating a more secure and stable environment for business.

Further, Kosovo's recent functional expenditure was reviewed against OECD and regional countries (Slovenia, Hungary, Germany, United Kingdom, Macedonia, Albania, Montenegro, and Serbia). The review showed that compared to the benchmark countries Kosovo allocates a higher percentage of its budget expenditure to public order and safety, economic development and education and less to environmental protection, health and social protection.

The SER Team undertook a complete costing analysis of EDVAP, including start-up/construction costs and ongoing costs, and determined funded and unfunded initiatives of EDVAP based on the 2012 Budget Circular Ceilings. This was a significant task given that at the start of the SER only 28% of EDVAP's 277 initiatives had been costed. At the same time, an improved process (methodology) for costing new policy initiatives was developed, and a process and criteria for the prioritization of policy measures contained in EDVAP, EPAP, and sector strategies into a National Development Plan were established.

The SER Team drafted sections of the SER Report covering sector and functional expenditure analysis, economic policy prioritization, costing EDVAP initiatives, and the situation analysis of the budget process. The reporting period included a dedicated workshop for the SER team in Tirana that was conducted to: examine the Albanian approach to budget development and government approval (lessons learned); discuss the results of the EDVAP costing exercise, the analysis of SER budget process and sector/ministerial reviews; agree on the structure and content of the sector/ministry review write-ups to be included in the body of the SER Report and annex; and discuss and agree on key recommendations to be included in the SER Report.

ISSUES/OBSTACLES

Efforts to obtain the information on the cost of the individual EDVAP initiatives from the line ministries proved a difficult task given a lack of previously issued methodology and guidance material covering this important process. While the SER process will result in all 277 EDVAP initiatives being costed, it is clear that more guidance and training needs to be circulated by the MoF to budget institutions on how to perform this critical task prior as part of the 2013 Budget process. Recommendations to achieve this outcome will be contained in the SER Report.

A weakness in the Kosovo Government's budget planning process is the lack of an established mechanism to prioritize new policy initiatives contained in EDVAP, EPAP and sector strategies into a fully funded National Development Plan that is consistent with the fiscal targets contained in the MTEF and the IMF's SMP. For example, none of the 277 initiatives contained in EVAP were prioritized against each other in terms of the expected impacts on job creation, revenue generation, export generation and import substitution, FDIs, PSI and environmental impacts. The SER report will contain recommendations to overcome the current lack of prioritization which is particularly important as Kosovo transitions from a period of 21.5% annual average growth in Budget expenditures over the period 2007 to 2011 to a planned 2.4% over the period 2012 to 2015.

Kosovo is in the transition to a Program and Perform Budget (PPB) Framework. The strength of the current budgeting system lies in its relative simplicity, lack of ambiguity, and effective control of expenditures through easy comparisons with prior years input usage. However, until PPB becomes fully operational, there will continue to be a lack of information on the impact of government programs. The SER Report will contain a recommended 3 year action plan for the implementation of PPB based on successful international implementations.

COORDINATION

Throughout the SER process, the GFSI advisors collaborated extensively with a DFID team of international advisors and regional advisors from Albania. Under the agreed division of responsibilities, the GFSI advisors focused primarily on the review of the MOF's central budgeting processes and supported the finalization of the Medium Terms Fiscal Framework as part of the IMF SMP discussions in September. The PER advisor consulted with EU advisors responsible for the Public Investment Program, the European Accession Plan and the Public Administration Development Program. DFID advisors provided effective support to the individual ministry expenditure reviews that used the recent WB PER as a basis for assessing areas of potential improvements in cost effective delivery of Government Programs. Advisors from the USAID Agriculture Project provided valuable assistance in the review of the Ministry of Agriculture's current programs and new expenditure initiatives proposed under EDVAP.

3 PROBLEMS, ISSUES AND PROPOSED ACTIONS/SOLUTIONS

| Objective | Problem/Issue | Migration Plan | Status |
|--|--|---|---|
| Central Government and Municipal Government PPP reform | Municipal vs. central government responsibilities are clearly set forth by law, however mistrust and misunderstanding continues to exist | The PPP Law and resulting directives are designed to clearly support the segregation of responsibilities where appropriate. | The new PPP Law or recently passed Directives; a) provide the municipality, as contracting authority, with a veto right on the ISC; b) sets forth the conditions to be considered by the ISC in reviewing municipal projects. |

4 MAJOR UPCOMING ACTIVITIES

| Objective | Upcoming Activity | Counterpart(s) | Planned Dates |
|---|--|--|-------------------|
| Municipal Government PPP Transactions | Awarding of one to three Pristina underground parking concessions. | Pristina Municipality | December 2011 |
| Issuance of urban transport PPP tendering documentation | Issuance of RfQ | Peja Municipality | November 2011 |
| Central Government PPP Transactions | Issuance of PPP procurement Solid waste landfill projects. | Republic of Kosovo | November 2011 |
| Financial Sector PPP Roundtable | Roundtable | MoF; Private sector financial institutions | October 2011 |
| Approval of Suhareka SWM project | October PPP-ISC meeting | MoF, Suhareka Municipality | October 2011 |
| Municipal PFM | Workshop to review 18 out of 28 PEFA indicators assessed | Six PEFA municipality counterparts | October 19, 2011 |
| Municipal PFM | Local Government PEFA Concluding Retreat | Six PEFA municipality counterparts | November 21, 2011 |

ANNEX 1: FINANCIAL STATUS

The table below summarizes financial status of the GFSI program as of the end of September quarter 2011, and includes: (1) budgeted amounts by line item, (2) amounts committed, disbursed and expended (with disbursements plus accrued amounts shown separately) and (3) estimated costs to complete the contract)

| Budget Cost Elements | Budgeted Amounts | Disbursed Amount | Accrual Amount | Expended Amount (Disbursed + Accrual) | Remaining Budget to Complete |
|--------------------------|------------------------|-----------------------|--------------------|---------------------------------------|------------------------------|
| Fixed Daily Rate - Labor | \$3,262,592.45 | \$910,248.75 | \$0.00 | \$910,248.75 | \$2,352,343.70 |
| TCN - Labor | \$3,409,097.04 | \$1,166,399.53 | \$0.00 | \$1,166,399.53 | \$2,242,697.51 |
| CCN - Labor | \$2,564,070.82 | \$798,917.41 | \$42,570.88 | \$841,488.29 | \$1,722,582.53 |
| Other Direct Costs | \$3,551,385.13 | \$1,131,962.69 | \$41,085.00 | \$1,173,047.69 | \$2,378,337.44 |
| G&A | \$709,118.59 | \$247,098.38 | \$8,405.99 | \$255,504.37 | \$453,614.22 |
| Total | \$13,496,264.03 | \$4,254,626.76 | \$92,061.87 | \$4,346,688.63 | \$9,149,575.40 |