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Evaluation of the Economic Management for Stability and Growth Program

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Evaluation of the Economic Management for Stability and Growth Program

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The authors' views expressed in this document do not necessarily reflect the views of the United States Agency for International Development or the United States Government.

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1. Executive Summary

The current EMSG Program, which began in June 2007 and will end in June 2010, continues to be effective. It has already achieved many of its intended results and is on target to achieve most others. This helps further validate the long-term resident advisor model followed by the EMSG Program. This model contrasts with that used by some other projects, whose work is less directly integrated on a daily basis with that of the government offices and functions they support.

The continued effectiveness of the EMSG Program is threatened by its reduced scope and vulnerability to external factors:

- By sharing insights and coordinating communications with the Kosovo government, the project team has multiplied its effectiveness in ways that technical assistance efforts of narrower gauge cannot. As the scope of the EMSG Program has narrowed, there has been a growing risk it will lose some of the synergy that has helped define its approach to crosscutting issues. This risk to the project's continued effectiveness can best be addressed through closer coordination between USAID and other donors to ensure their technical assistance efforts are complementary and closely synchronized.
- The increased capacity in major governmental institutions is fragile because the number of internationally trained professionals in senior management positions is small, and the merit systems for recruiting, training, and promoting professional staff is not well developed. USAID can work with other international projects to develop a new, combined strategy to ensure management training that meets international standards for a sustained senior cadre of managers and technical specialists, who are integrated into a permanent civil service structure and funded in the budget through annual appropriations for salaries.
- The core processes for managing government finances – including budgeting and treasury functions – are vulnerable to political interference. If the budget process is routinely bypassed, as was the case in 2008, or if there should be a turnover of senior leadership in the Budget and Treasury, as there has been in Tax Administration, many of the gains in governing capacity of the past few years could be quickly lost. USAID should work with other international donors to reduce these risks by supporting broad strengthening of capacity in the budget organizations and by endorsing the efforts of international organizations to strengthen basic government processes, including those for personnel systems reform, procurement reform, and strengthened financial management.

Specific findings and recommendations for each of the five areas/institutions supported by the EMSG Program are as follows:

1.1 For Budget, Treasury, and Economic Policy

- We find that the Budget and Treasury Departments are highly professional, well-managed operations. Further training of staff and systems development is needed, but the needs are identified and owned by two managers. They can proceed, within resource constraints, to make needed improvements, with occasional consultation and expert advice from the EMSG Program or other international projects. Both are receptive to such continuing advice and support. The Macroeconomic Policy unit retains a core of professional economists who continue to perform excellent quantitative and qualitative analyses of policy options. The integration of their work with the budget analysts has increased through a restructuring of the MTEF process.
- We recommend that USAID encourage the MFE to explore options and seek expert, neutral advice on requirements for an integrated Budget and Treasury system, linked electronically with MPS for personnel and payroll, to Tax Administration and Customs for revenues, and to CBK for debt

management. As part of this review, expanded capacities to support fiscal decentralization should be considered. (Note: This responds to questions 14 a. i., ii., and iii. in the Statement of Work.)

- We recommend that the EMSG Program give highest priority to reestablishing the MTEF this year as the Government's vehicle for turning policies into concrete multi-year plans and targets for collection and use of resources to advance the Government's highest priorities.
- We recommend that EMSG Program advisors revive a previous emphasis on training and procedures for incorporating performance and program budgeting information into budget decision-making both centrally and in the preparation by budget organizations of budget proposals for the coming year(s).
- We recommend that efforts of the new EMSG Program advisor in Treasury focus on developing regulations for internal financial controls and stronger auditing functions, on support for linking Treasury, Budget, and payroll systems, and on other priorities established by the Treasury director.

1.2 For Tax Policy and Administration

- We find that Kosovo has made tremendous strides since 1999 in developing a modern tax system. An adequate legal framework exists and there is at least a core of well trained managers and staff. Finally, a comprehensive (if somewhat unfocused) plan to modernize and strengthen TAK has been agreed upon and is being implemented. Under the EMSG Program, USAID/BearingPoint advisors are making good progress in achieving most tax-related results identified in the statement of work. TAK's performance, while not stellar, is in line with that of some other countries in the region—with the exception of a seemingly under-performing personal income tax.
- We recommend that assistance to TAK be held steady over the remainder of Task Order 6. The assistance being provided at present is well targeted. Advisors are focusing their efforts on helping TAK better target audits, improve collections, better coordinate business registration, and strengthen its IT system (SIGTAS). Gains in these areas have the potential to improve TAK's revenue performance. Between now and June 2010, it would be prudent for USAID/BearingPoint advisors to continue to focus on the priorities identified above and thus avoid being spread too thin across the full gamut of needs identified in the Strategic Plan.
- We support the decision to end EMSG assistance relating to property tax as of November 2009.
- We recommend that USAID assistance to TAK beyond June 2010 continue the downward trend established over the last few task orders. We recognize that TAK could likely improve its revenue performance by adding roughly 100 additional staff¹—if these staff were sufficiently educated and trained. If TAK decides to move in this direction, USAID might consider supporting the development of training programs that ultimately enhance TAK's revenue generation potential.

1.3 For the Central Bank of Kosovo

- We find that the assistance to the CBK has largely accomplished its objectives, and we agree with the decision to end further long-term support to the institution. Significant support from other donors is being programmed.
- We recommend that USAID continue to monitor developments in the CBK through consultations with the US Treasury Advisor during his periodic visits and with other donors for potential problems that might require additional assistance.

¹ Given Kosovo's population, the size of TAK's staff is relatively low when compared with most other countries in the region and even when compared with higher income countries.

1.4 For Commercial law development

We find that the EMSG Program's commercial law program has a number of strengths: (1) It builds on an ambitious USAID-supported effort over the past five task orders aimed at helping Kosovo put in place the commercial law framework needed to foster private sector-led growth as well as corresponding legal capacity; (2) It uses an innovative and relatively hands-on approach to training; (3) It emphasizes building and using local training capacity; and (4) It at least partially institutionalizes this training within KJI and KCA.

- We recommend that USAID/BearingPoint support the development and implementation of a methodology to assess the actual impact on the performance on judges and lawyers of the training being provided by USAID/BearingPoint.
- We note the importance of agreeing upon and developing a certification process for judges/lawyers.
- We note the importance of ensuring that commercial law training is sustainable. The current absence of admissions fees for trainees means that such training is not inherently sustainable (absent donor or Ministry of Justice funding) and does little to ensure that the training is targeted as effectively as possible.
- Finally, we suggest the benefits of the types of legal training provided under the EMSG Program may be limited in the absence of broader efforts to streamline court procedures and develop alternative dispute resolution mechanisms.

1.5 For public/private partnerships

- We find that progress on the Pristina Airport concession process is quite satisfactory at present, and is consistent with awarding a concession by early 2010. We find that the Public-Private-Partnership (PPP) unit in the Ministry of Finance and Economy is making good progress toward institutionalization, and that the new PPP law, expected to pass second reading during May 2009, will constitute a major step forward to creating conditions for widespread use of PPP's to attract foreign investment for Kosovar infrastructure. Nevertheless, we find that USAID support for a substantial period – perhaps 4-5 years beyond the end of the current Task Order – is likely to be needed to fully institutionalize PPP in Kosovo
- We recommend that USAID continue to support the incipient effort to promote PPP in Kosovo, with particular attention to the Pristina Airport concession. Short-term support should be made available at key stages in the process of awarding the concession.
- We recommend that USAID begin the process of planning for significant long-term support to the PPP unit of the MFE for several years beyond the end of the current Task Order. Particular attention needs to be given to creation of a regulatory framework that would provide assurances to both the government and to future concessionaires of fair adjudication of contract disputes.
- We recommend that USAID consult widely among political leaders about PPP in order to determine the extent to which commitments to concessionaires would be regarded as commitments by Kosovo, and not just of one administration.
- We recommend that USAID condition its future PPP-related support on both a national consensus on the desirability of this vehicle, and on a commitment to staff enlargement and development and institutionalization plan for the PPP unit in the Ministry of Finance and Economy, and for suitable staffing plans in line ministries responsible for implementing PPP programs.

2. Responses to Specific Question in the Statement of Work

1. What has been the impact of the EMSG Program?

The EMSG Program has had continuing positive impact on the institutional capacities of the Government of Kosovo. Resident advisors continue to identify specific areas where their expertise can be most effective in improving procedures. As a result, there has been a continued maturing of the budget process at both the central and municipal levels, further development of the systems for tax collection and property tax assessment, completion of the planned support for CBK, continued strengthening of the legal framework for commerce, and rapid progress in establishing new capacities to support public/private partnerships.

During the year of independence, the EMSG Program leveraged its presence and expertise to assist the new Government of Kosovo in meeting the challenges of organizing new ministries and functions capable of drafting and implementing a host of new laws. Some of this work may have displaced more routine advice and assistance, representing a pragmatic approach that served the interests of both USAID and the Government of Kosovo.

2. What specific impacts did the program have on the capacities of the ministries/institutions assisted?

Specifics are provided in discussions of each area/institution that has received program support.

3. Has the assistance provided had sustainable results?

The question of sustainability is a complicated one. For its part, the EMSG Program has recognized the need to look ahead to a point when continuing technical assistance is no longer provided. The EMSG Program has taken specific steps – such as its advice to the Government in support of the Brain Fund and its co-sponsorship of AUK’s new Public Policy Master’s Degree program for government managers – to build broader, lasting institutional capacity.

4. This current program emphasized increasing capacity of Kosovars. Has this been well-implemented and effectively carried out?

Particularly in the MFE when compared to the preceding period, its advisors have been more inclined to step back into coaching and consultation roles in order to permit Kosovar principals and staff to take the lead. Successful design and implementation of the Brain Fund will help increase and sustain the capacity of the Government of Kosovo.

5. Did the activities carried out under each objective contribute to the achievement of the goals? If so, how? If not, why not? Would other activities have been more appropriate?

By and large, the activities carried out under each objective were appropriate and contributed to achievement of the EMSG Program’s goals. Specifics are given in discussion of each area/institution. It is difficult to second-guess the prioritization of activities by resident-advisors in each area/institution.

6. Is the program meeting stated objectives?

Yes, but the gains are inherently fragile as noted elsewhere in this report.

7. Were the established targets reasonable, relevant, and achievable?

Yes. In the future, however, it would be useful to agree in advance on indicators for the various results (or targets) established for EG programs so that progress in achieving these results can be more easily tracked.

8. Can any identified deficiencies in the program's current target areas be remedied in the remaining life of the program, and what are recommendations?

At the broadest level, the diminished scope of the current program, relative to previous USAID/BearingPoint projects, has reduced synergies and probably the overall capabilities of the project team to coordinate and combine their efforts to address cross-cutting issues. This can only be remedied going forward by strengthening coordination between the EMSG Program and other donor technical assistance projects.

As noted, training and capacity building to support performance or program budgeting approaches was set aside during the year of independence. This is a continuing need the current budget advisor intends to address in the coming year. More broadly, building and sustaining capacity in the key GOK institutions that the EMSG Program works with should be a priority during the remainder of the program.

9. Are there other areas where USAID assistance is needed, in the short term that will result in greater impact in improving institutions?

This is a difficult question. Clearly, direct support to these institutions is essential to such improvements. Another aspect of strengthening such institutions is the creation of demand for their effective management. Business associations, economists' groups, academic entities and public-policy oriented think tanks and NGOs, and journalists can all play useful roles on the demand side for improved government institutions. A stronger public reaction by some of these non-governmental actors to the abandonment of the MTEF framework in the 2009 budget might have created political pressures to avoid a repetition. Nevertheless, it is difficult for short-term evaluators to judge which institutions are best served to promote greater demand for governmental effectiveness. Efforts to improve the functioning of the real economy can complement the institution building carried out under the current EMSG Program and previous task orders.

10. Is the program properly addressing and prioritizing *ad hoc* needs and requests for assistance? Are these requests more or less critical and priority use of resources compared to the main stated objectives?

As noted, the EMSG Program continues to show laudable flexibility and pragmatism in responding to requests for assistance, including *ad hoc* requests from USAID and the Government of Kosovo. In this regard, the demands on the project's legal advisor for advice on draft laws or even for help in drafting new laws has displaced other critical work, including training and technical assistance to support implementation of existing laws.

11. What is the level of participation/coordination with other donors?

Based on limited conversations with other international donors, there is less coordination than would be optimal given the close relationships and potential synergies between various technical assistance efforts. An underlying problem may be distrust of USAID's efforts stemming from a perception that it pursues its interests at times without regard for others. The Government of Kosovo also has some responsibility for coordinating donor assistance; however, its nascent capacity for donor coordination, including integration with the budget process, has been weakened by a recent decision to merge this function with others.

12. Does the program coordinate sufficiently and effectively with other programs on related issues?

See above. While there is a good deal of coordination, it appears to be less than optimal. At the same time, we recognize that "donor coordination" also has costs. Trying to link one donor's activities with those of others can lead to delays, misperceptions, and other obstacles to effective assistance. The more pressing issue is often the fact that some donors produce ineffective projects, either because of poor

diagnoses, long lags between project decisions and effective implementation, or from poor choices of personnel to carry out projects. There is no amount of coordination can prevent these ills.

13. What are key lessons learned from the EMSG Program?

As noted elsewhere, the EMSG Program has further validated the strengths of a broad-scale resident-advisor model for capacity building in this setting. However, as evidenced by the slower development of tax administration than of treasury or budget, gains have been greatest in the institutions that have had stable local leadership.

Viewed in retrospect, the current program has continued to build capacity on a foundation of professional procedures and management created in a few short years in a country with almost no recent experience in self-government. At the same time, the limitations of such efforts are apparent. The foundation is fragile both because governing processes are not rooted in tradition and because of the small numbers of senior professionals in government who understand their institutional responsibilities. These make the gains to date vulnerable to quick reversal.

14. Specific questions to be considered during your review

Specific questions are summarized under discussion of each area/institution in the body of the report. Recommendations regarding individual items are summarized below:

- Regarding 14.a: An independent technical assessment of system development options is recommended.
- Regarding 14.b: No advisory support for insurance supervision is recommended, given pending help support from other donors.
- Regarding 14.c: The main focus of the next Treasury advisor should be in support of new central functions and other priorities set by the Treasury director, which could include the items mentioned.
- Regarding 14.d: We note the demands on the legal advisor and a continuing need for such assistance and for assessment of the current training approach.
- Regarding 14.e: We see a potential increase in demand for PPPs and need for continuing advisory support to the new function.
- Regarding 14.f: We note the mature performance of Kosovar staff and see no need for a resident international advisor.
- Regarding 14.g and 14.h: We note both the growing capacity of the MFE and its fragility; we propose conversations between USAID and the Minister about a strategy anticipating future termination of long-term advisory support to the Ministry.

15. Based on a review of implementation and results for the EMSG Program, what recommendations do you have for possible future USAID programming in the economic institution area?

For most areas/institutions we recommend continuing support by USAID but on a reduced scale, especially if that would allow more USAID economic growth-related assistance to the real economy. With regard to MFE Budget and Treasury, we see a continuing need for resident advisor support, with renewed focus on training of budget staff and on development of regulations and procedures to support new Treasury functions identified by the Treasury director. We believe that when a new general budget director is selected there will be a need for an advisor to support the new role and coordination between

central and municipal budget functions. However, this need can be met by reassignment rather than adding a new advisor position.

Concerning tax administration, many of the major improvements in information systems, better procedures, risk-based audits, and improved taxpayer identification should be largely in place by mid-2010. Moving forward, USAID assistance should focus on helping TAK develop the capacity to increase its revenue performance.

As noted elsewhere in this report, the PPP unit in the MFE is small and young in an activity where both are serious liabilities. Effective PPP requires that potential private investors have confidence that the rules of the game will not change during the life, or at least the early years, of their concession, and that effective government oversight of concessionaires will not be prevented by the politically-powerful. Substantial USAID involvement for the next 4-5 years in this area as the “honest broker” is likely to be crucial to the success of PPP in Kosovo.

3. Introduction and Background

3.1 Background to USAID Assistance

During the 1970s, Kosovo gained considerable autonomy as a province in Serbia, with its own parliament, the establishment of Albanian as the language of instruction at the University of Pristina, and with the Albanian-speaking majority assuming key roles in the economic, political and social institutions of the province. By the mid-1980s, this process began to be reversed, with Serbian control from Belgrade gradually reducing Kosovo's autonomy. By 1991, the reversal became almost complete, with Albanian-speakers pushed out of leadership positions in politics, economic institutions, and educational and health institutions. For the following decade, conflict escalated as increasing Serbian centralization of control was met with resistance by Albanian speakers. This culminated in the 1999 NATO bombings of Serbian infrastructure that led to the uneasy return of Kosovar autonomy, though still as a part of the Serbian republic.

With the departure of the Serbian authorities, Kosovo needed to begin to rebuild its government institutions from scratch. At that time, Kosovo lacked both a legal and regulatory framework for governance and experienced Kosovars to manage it.

This was the background to the onset of USAID assistance in 1999, aimed at creating economic governance institutions for Kosovo that would collect taxes, manage government spending, control financial institutions, and move the economy from a reliance on planning to markets. Over the next decade, USAID contracted consulting services to carry out these tasks through a series of six Task Orders. All six were carried out by BearingPoint. The individual Task Orders were developed sequentially in response to changing conditions on the ground. Initially, expatriates were placed in the top management positions of the newly-formed Kosovar economic governance institutions. Over time, the tasks assigned to the consultants gradually shifted control of these institutions to Kosovars, with the attendant training and advising of both senior and mid-level professions in the key institutions supported by USAID through its contractor. The assisted institutions included the Ministry of Finance and Economy, the Tax Administration of Kosovo, the Kosovo Central Bank, and the Kosovar Trust Agency (charged with privatization of socially owned enterprises).

3.2 Results from Previous Activities

The first four Task Orders were evaluated in 2003 (Skogstaad, et al., November, 2003). That evaluation applauded the speed with which resources were mobilized and the program put in place, stating that it “set an exceptionally high standard.” Overall, the evaluation concluded that the four Task Orders “followed a logical and practical sequence, and were meticulously crafted,” adding that the USAID strategy was appropriate to the country's circumstances.

Still, the evaluation found several weaknesses in the program. It suggested that expectations of the ability of Kosovars to take over highly-specialized professional and technical functions had been overestimated, arguing that a shortage of personnel with appropriate foundation education had only been gradually identified as a serious problem. Implicitly, the evaluation suggested that more advanced skills training would have been useful in the earlier stages of the program. The evaluation also suggested that more emphasis on informing and educating the public on the directions being pursued under the program would have been valuable.

In terms of coordination with other donors, the report praised the performance of the project and the donor community in general for working together to achieve the purposes of the assistance with a

minimum of conflict and inconsistency of approach. Finally, the report made seven recommendations for follow-on activities:

- There should be one more year of assistance on banking, with a continued emphasis on training in bank supervision and regulation, including major formal training of professionals.
- Further assistance for one more year on fiscal reform is warranted, prior to transfer of leadership to Kosovars.
- Continued assistance on pensions for another year would build on a highly-successful effort.
- Commercial law reform is well established, and further assistance could come from other sources.
- On privatization, logjams currently limit progress, but considerable further assistance would be warranted if they are addressed.
- Great progress has been made on insurance, and further assistance in this area seems unnecessary.
- Although USAID appears ready to withdraw from assistance for public utilities reform, further work on telecommunications privatization and the power sector might yield high payoffs.

Overall, these recommendations suggested a relatively modest follow-on program after Task Order 4. Nevertheless, Task Order 5 was considerably more ambitious when implemented, with the number of resident advisors declining only from 29 under the previous task order to 25. (Annex 1 shows the number of resident advisors under each of the six task orders by area of specialization.)

For Task Order 5, no final evaluation was undertaken. The contractor, BearingPoint, submitted a final report (BearingPoint, 2007) in June 2007, and there was a mid-term program review that dealt broadly with the USAID economic growth portfolio (Singletary, 2006) in May 2006. The Singletary report dealt at considerable length with the activities under Task Order 5, as well as other parts of the USAID economic growth portfolio.

The Singletary report termed the activities under the task order “highly successful,” but proposed a “scaling down or phasing out of USAID’s technical assistance to these [i.e., the Ministry of Finance, the Kosovo Trust Agency, the Central Bank of Kosovo, and the Kosovo Pension Savings Trust] institutions, with some exceptions designed to provide insurance against backsliding or to enable certain new functions.” Instead, the report suggested shifting USAID attention toward infrastructure, public utility reform, enforcement of contracts and addressing legal claims, and improving connectivity among government institutions and greater transparency through connectivity with the general public. Overall, the Singletary report reinforced the conclusion of the Skogstaad evaluation that a shift from high levels of technical assistance to the economic governance institutions to other areas was warranted.

As discussed below, USAID continues to provide substantial, although reduced technical assistance to the core economic governance institutions during the current Task Order 6. The number of resident advisors was reduced from 25 under Task Order 5 to 18 under Task Order 6. And these numbers declined during implementation, with 12 on the ground at the time of this evaluation (March 2009) and with further reductions expected to occur in the near future.

Given that no final evaluation was carried out for Task Order 5, the question of whether and to what extent resources might be better deployed in other areas was not addressed at the end of the project. The only document available from this time period is the end-of-project report by BearingPoint (Smith, June 2007). The end-of-project report could not be expected to address these issues, as the contractor was only reporting on its degree of achievement of the tasks that USAID had set out for it. The status of the institutions being assisted by USAID at that time is well described in the end-of-project report. The main

features of the situation at the outset of Task Order 6 are described briefly below, and in more detail in each of the sections of Chapter II.

3.3 Situation at the Outset of Task Order 6

The USAID/BearingPoint Chief of Party concluded that all benchmarks established by USAID for the task order had been met, and many exceeded. Broad achievements included:

- More than half of socially owned enterprises had been privatized, with substantial investments by the new owners.
- The capacity of the Kosovo Pensions Trust was fully developed, and USAID assistance withdrawn.
- The Ministry of Finance and Economy and the Central Banking Authority have local staff that is firmly entrenched in management, and undertaking all functions independently of foreign advisors.
- A vast array of laws are firmly in place to underpin the Kosovo economy, with an established process for future legal development.
- A professional development program at the American University of Kosovo (AUK) for government professionals was running, with results exceeding expectations.

The report described three outstanding issues for the future:

- A need to deepen professional capacity in the future, in part through the AUK professional development program.
- A need to address salary issues in the government for high-level professionals.
- A need to implement processes across government institutions for performance management and accountability.

The following sections of the report look in depth at five areas/institutions assisted by the Economic Management for Stability and Growth (EMSG) Program. These are: (1) the Budget, Treasury, and Economic Policy units of the Ministry of Finance and Economy; (2) Tax Policy and Administration and Property Tax, also in the MFE; (3) the Central Bank of Kosovo; (4) commercial law development; and (5) the Public/Private Partnership Unit of MFE, including plans to commercialize Pristina International Airport. Each section begins with a summary of the EMSG Program objectives for that area/institution, followed by a review of conditions at program initiation in summer 2007, progress under the current program, and findings regarding current level of development, noting both strengths and weaknesses. Each section concludes with the identification of possible next steps to improve the program's performance during its remaining months.

4. Assessment by Area / Institution

4.1 Budget, Treasury and Economic Policy

The current project is the continuation of a sustained effort to build capacity and strengthen the organization of the core budget and financial management functions of the government of Kosovo, centralized in the Ministry of Finance and Economy (MFE).

4.1.a Objectives

Broadly, the goal of the current project is to ensure these institutions and processes are mature, professionally managed, compliant with law and requirements of the status settlement document, and performing competently. The specific objectives include:

- Enactment of legislation relevant to MFE and its functions.
- Formulation of new policies and procedures required for fiscal decentralization (to municipal governments) including new grants procedures.
- A macroeconomic strategy for Kosovo that is fiscally sound, feasible and promotes economic development over the medium to longer term.
- A level of proficiency in the budget, treasury, and economic policy units that can be sustained without need for full-time technical assistance.
- For the Budget Department, strong analytical skill in assessing budget submissions, proactive work with budget organizations to develop better budget submissions and better conceived capital projects.
- For the Macroeconomic Policy unit (Economic Policy Department of MFE), strong analytical capacity that is evidenced by the quality of the annual updates of the Medium-term Expenditure Framework (MTEF) and by regular solicitation of its policy advice and analysis by the Minister and the Government.
- For the Treasury Department, sophisticated management applying modern and sophisticated public accounting and cash management standards, as evidenced by timely reconciliations, clean external audits, and similar indicia.
- Also for Treasury, development of new modules connecting Treasury's FMIS system with those of municipalities.

4.1.b Status in June 2007

At the start of the current EMSG Program in June 2007, the Budget, Treasury, and Macroeconomic units were each functioning at a professional level, with Kosovars directing the day-to-day operation and occasionally seeking the advice and participation of full-time EMSG Program consultants.

It should be noted that this status was in part a product of a substantial investment in building and supporting these institutions through earlier phases of the project. A 2003 evaluation of predecessor USAID technical assistance observed: "This effort has been exceptionally successful in getting the MFE up, running and efficient. Nevertheless, it too is unready for operation by Kosovars. A final year of TA should address that problem, and develop a plan for dealing with issues raised in the evaluation report, especially project evaluation in the budget function (Skogstad, et al., November 2003)."

Since then, Kosovars have assumed full responsibility for the development and execution of the budget. The budget has been generally prepared, adopted, and executed in a manner consistent with the law on

public finance drafted by internationals and providing relative autonomy to the Government, although subject to final review and approval by the UN's Special Representative prior to independence. The process now includes a role for the EU's ICO, but that role has been limited so far to monitoring.

The process now includes annual preparation of the Medium-term Expenditure Framework (MTEF), a three-year integrated fiscal and development framework that includes macroeconomic analysis and sectoral plans for development and fiscal targets for central and municipal current and capital spending reflecting sectoral priorities and strategies. The first MTEF was prepared in 2006, consistent with international standards, but was largely a product of international advisors, who worked alongside and instructed Kosovar counterparts. The next MTEF, prepared at about the time as the current EMSG Program began, was largely a Kosovar product (described below). It was used as the basis for presentation to donors of the Government's priorities for assistance as well as the starting point for the annual budget process.

At the start of the current EMSG Program, the Budget Department had recently been divided, with separate directors for central and municipal budgets. Nevertheless, the annual budget process produced a single, integrated fiscal plan for the coming year.

As of mid-2007, the central budget department was leading a well-established orderly annual budget process, including hearings with each budget organization led by budget department staff, research into specific issues such as capital under spending, and limited program or performance budgeting elements. The quality of decision-making was limited by the skills of budget analysts but more significantly by lack of basic analytical capacity and experience in budgeting in the budget organizations. In hearings, Ministries and other budget organizations could not effectively defend their spending requests.

At the time, the new municipal budget department had an inexperienced director with limited management skills. With considerable coaching and effort at coordination, however, the municipal budget department was able to communicate with municipalities and to complete its part of the budget preparation consistent with requirements of the law and established procedures.

The EMSG Program provided full-time advisors to each budget department, who sat with the director and provided regular advice and support upon request. This was a change in role from past years, when advisors had taken more initiative in drafting budget instructions and writing or heavily editing budget presentation materials.

A Public Expenditure and Financial Accountability (PEFA) assessment prepared by the World Bank for and concurred in by the Government (World Bank, March 2007) saw a fundamental weakness of the Kosovo budget process (of the prior year) as "lack of long-term direction" while noting the promise of a more policy and strategy driven three-year planning process emerging through preparation of the MTEF.

Performance in budget preparation during 2007 can be assessed by examining the 2008-2010 MTEF. This was largely the product of a five-person Kosovar staff in the Economic Policy Department (Macroeconomic Policy unit) of the MFE, a staff of young economists recruited and heavily supported – both analytically and financially – primarily by USAID. The document itself was substantially more sophisticated than its predecessors, in that it based fiscal targets on more specific prioritization and costing of alternative uses of public resources, based on negotiations between the Minister and his counterparts regarding their priorities and in some cases difficult political choices that were debated and compromised between the MFE and line ministries.

In contrast to preparation of the prior MTEF, which depended on internationals to develop and run the required macroeconomic models and to write most parts of the final document, the analysis and drafting

of the 2008-2010 MTEF was largely a Kosovar effort, with the USAID/BearingPoint advisor (who also served as the Minister's advisor) providing direct leadership and guidance. The resulting document was not only adopted formally by the Government as the three-year framework for the Kosovo budget but was presented by Kosovars, with support from the Macroeconomic Policy unit staff, at international donors' meetings as the Government's plan and basis for possible donor assistance.

Budget execution in Kosovo requires carefully planning from early in the year to ensure that appropriated amounts are fully spent and for the intended purposes. Because Kosovo cannot borrow and has limited cash reserves, it has budgeted recently on a cash basis and created systems to allow close monthly monitoring of spending. Budget analysts were receiving regular monthly reports on commitments and spending, by accounts, for the budget organizations in their portfolios. Budget and Treasury coordinated in producing the information, which was actively analyzed and used by Budget department staff.

As noted in the 2007 PEFA assessment, errors in forecasting revenues and spending, combined with limited capacity in the budget organizations to plan and execute budgeted capital projects contributed to substantial deviation between the approved 2007 budget and actual spending. A major emphasis of EMSG Program advisory support to the budget department in the period just prior to the current project was on working with budget staff to identify reasons for capital under spending and to developing a proactive approach to working with budget organizations, in cooperation with other donor technical assistance projects, to inform them of requirements and help build capacity. A Possible result from this effort is that the rate of capital execution in 2008 increased substantially.

The Treasury Department, like central budget, was led in 2007 by an experienced professional director who had benefited from previous rounds of USAID advice and support. He also was receiving regular advice and specific technical assistance at his request from one or more EMSG Program advisors.

The World Bank's PEFA Assessment (March 2007) identified weaknesses in internal financial controls and audits and in external audits (a responsibility of the Auditor-General, a UN official).

Transparency in reporting was aided by on-line availability of quarterly and annual financial statements, albeit with some months lag. Both budget preparation and transparency were weakened by the lack of donor coordination and failure to incorporate the amounts provided, in most cases, in the Kosovo budget. While both donors and Government attempted to improve information and coordination regarding donor assistance, the failure to achieve these goals as of mid-2007 has to be attributed mainly to donors rather than to the Government.

The budget document, detailing the 2007 budget as adopted was not published until late spring 2008. When presented to the Assembly in November 2006 it was in the form of legal text and detailed schedules, limiting public visibility and understanding. The 2008 budget, the first adopted after independence, was submitted within six days of the legal deadline.

At the time the current EMSG Program began, the Government faced the challenge of incorporating into its budget and financial processes new institutions, including creation of new ministries. It faced uncertainties with regard to consequences of independence, including effects on revenues and spending needs, such as possible servicing of the former Yugoslav debt. It faced new elections that could bring a new group of less experienced political leaders and put at risk the positions of experienced civil servants who had received a substantial investment of international technical assistance. Also, with independence, it needed to quickly write or revise a substantial body of basis law governing public finance and to write and adopt new laws required by the UN representative's plan for independent status, such as new laws on local government and local government finance.

At the time the current EMSG Program began, the Budget and Treasury departments and the Macroeconomic Policy unit faced several specific challenges, listed below:

- **The MTEF was not yet the intended bridge between Government policies and the annual budget process:** The MTEF is intended to inform the annual budget process by providing a three-year sustainable path for spending that reflects the Government's strategy and policy priorities. The 2008-2010 MTEF, which was focused heavily on identifying projects that might attract international donor support, was finished too late to be used as the basis for ceilings or targets for individual budget organizations to use in preparing their 2008 budget proposals. For this purpose, it must be completed earlier in the year; and, in fact, the new law on public finance adopted in 2008 requires MTEF submission to the Assembly by April 30. Also, the MTEF's content must be modified to focus less on capital projects that may possibly attract donor support and more on general ceilings and targets consistent with the fiscal outlook and Government priorities. This requires close coordination between the Budget Department and Macroeconomic policy unit. It is perhaps most important that the MTEF be preceded and shaped by clear, specific decisions about changes in policy and priorities from the prior year that are seriously deliberated and endorsed by the Government at the beginning of the process. While these can be revisited later in the process, any revisions should be such that they can be accommodated within the fiscal framework set in the MTEF.
- **The focus of budget choices needed to shift from inputs to outcomes:** For the budget process to effectively support the Government's policies and for the Government and its leaders and managers to be held accountable for outcomes that improve people's lives, the budget process must be the primary vehicle for converting policies into concrete spending plans that can be realistically executed in the coming year. This requires an informed analysis and discussion of the expected results of proposed spending, based on evidence that these will contribute to achievement of the Government's major policy goals. Further progress in this direction depends on developing capacities throughout the Government, not just in the MFE's budget departments. Weakness of the policy development process in the line ministries and municipalities, combined with absence of regular, reliable performance reporting requirements, are major obstacles to further development of this approach to budgeting.
- **Planning for and execution of capital projects needed further strengthening:** The studies by the Government's working group (led by the Budget Department) and World Bank consultant Andrew Bird reached similar conclusions in 2007 regarding steps needed to reduce under spending and improve the execution of capital projects. Implementing those recommendations must be a joint undertaking of the MFE, the procurement agencies, and internationally funded technical assistance projects. Budget organizations with major capital programs should be supported in developing their three-year capital planning procedures, with technical assistance provided by the PIP and EAR Strategic Planning projects. For multi-year projects, the full estimated cost of proposed capital projects should be included in the budget as information. Further restrictions on shifting of funds between capital projects during the year may also be needed to introduce foresight and discipline into planning as well as management of capital projects.
- **Government credit and guarantees were not clearly subject to appropriation, and their costs were not included in the budget as they arose:** Government loans to POEs have been treated as financing transactions and not included in the budget totals or appropriations. Subsidies to those entities to repay loans were not identified as such in the budget. New appropriations of credit should be anticipated to support economic development and for other purposes, so it is important to establish a sound precedent to budget for and control the cost of these obligations. Decisions to extend Government support in the form of loans or support of private borrowing incur costs that should be recognized in the budget when the decision is made to provide credit. An approach consistent with Kosovo's budget

process and capacities would recognize the expected cost of credit beginning at the time credit is extended and require the annual appropriation of a reserve for potential cash expenditures each year.

- **Procedures for monitoring and control over budget execution needed to be tightened:** The budget department's monitoring of the budget's execution and of actions which have budget implications is crucial to the integrity of the governmental process – especially due to the weakness of financial controls in many organizations. To ensure that the budget is executed as enacted and to ensure proper prior review of proposed legislation or proposed Government decisions to assess their budget impact, proper procedures must be followed. The MFE's budget department often learns about actions with budget implications long after they occur. In some cases, actions by budget organizations that are inconsistent with the budget regulation or other legal requirements has gone undetected for some period, undermining Government policies and increasing costs. The MFE must work with others to clarify the legal authorities for observed increases in compensation and must work with Treasury to draft a new administrative instruction providing budget organizations with a list of narrow circumstances under which it is appropriate to propose allowances. Uncontrolled increases in salary levels and compensation tend to undercut the budget process and accelerate spending without a corresponding gain in output.

- **The budget department's performance needed further improvement:** The capacities of the budget department were stretched thin. Department staff had received regular training in general budget processes, specific analytical techniques, and specific methods immediately applicable to their work. Progressively more responsibility has been placed on budget analysts to develop detailed knowledge of the budget organizations which they oversee and to provide informed, timely analysis of budget issues. In 2007, the analysts led reviews of capital spending and were more proactive in engaging with budget organizations about problems affecting budget execution. Further professionalization and skill development are dependent in part on having adequate staffing levels for this function; staffing was lower in 2007 than in 2006.

- **Information systems for budget and treasury needed to be integrated and strengthened:** Treasury and Budget use separate donated systems for their work, which is problematic since these systems do not connect. Moreover, there is no integration between the Treasury system and the payroll system maintained by the Ministry of Public Services. The Treasury system has an unused budgeting module with greater functionality than the current budget system, which could be the basis for an integration of budget and treasury production and reporting of financial information for purposes of both departments. Although this has been recognized for a few years as a possibility, there has yet to be a decision to move forward.

- **More active management of the Government's cash balances was needed:** Preliminary steps had been taken by mid-2007 to develop policies and apply practices of modern cash management, resulting in higher returns on balances. However, further policy development and design, with additional systems support, was needed to fully modernize this Treasury function.

- **Debt management policies and procedures had to be developed:** The need for these was clearly identified by Treasury, pursuant to the anticipated change in Kosovo's status and assumption of a portion – to be negotiated – of the old Yugoslav debt. It was recognized that international expertise would be needed to establish the necessary functions, in cooperation with the Central Bank.

4.1.c Progress under the Current Program

Several specific indicators suggest continued strengthening in the last 18 months of the budget and financial management processes and systems that are the focus of EMSG Program assistance. At the same time, surrounding circumstances have complicated the work of the Budget Department and the

Macroeconomic Policy unit in particular and may limit immediate prospects for a strong budget planning and preparation process that can serve to rationally allocate public resources based on the Government's policies and priorities.

Specific accomplishments that were identified during the March 2009 evaluation include the following (Results indicators in parentheses):

- A new law on public finance and accountability, a new law on municipal finance, and other new or revised laws required by independence were drafted with intense involvement of the EMSG Program advisors and with the advice of IMF and World Bank representatives, and enacted in short order following independence. The new law on public finance is highly specific regarding the structure and process of budget and treasury functions and therefore provides a firm foundation for continuation of orderly processes (1.1.2).

Budget and Macroeconomic Policy:

- The MTEF for 2009-2011 is an advance over the previous year's document both in the manner of its development and in its content. Its content was shaped by a very general statement of Government priorities adopted in May and showed how these could be addressed within spending totals, as well as what additional could be accomplished with specified donor support. Ceilings were finalized in June, earlier than in 2007 when they were prepared too late to serve as targets for 2008 budget planning. While the Macro unit worked on a broader economic framework and forecast, the budget analysts were given the lead in convening working groups of the relevant ministries to develop sector analyses. Recommendations of the sectoral analysis groups were given to the MFE's working group for MTEF. This parallel work required closer coordination of the two units than in the past, a challenge which was met as evidenced by the final document. Issues regarding the MTEF's use as a framework for the 2009 budget and the relationship between the budget process and other policy making processes are explored below (1.1.1; 1.1.8; 1.1.9; 1.1.12; 1.1.13).
- The 2009 budget was presented to the Assembly within three days of the statutory deadline, and with unprecedented detail describing and justifying spending proposals. The Central Budget Department staff accomplished most of this work without involvement of international advisors. The Central and Municipal Budget Departments managed the close coordination required to meet this deadline (1.1.3; 1.1.8).
- As noted, 2008 capital spending execution improved, probably for several reasons, including active efforts at both political and technical levels and improvements in procurement regulations. All capital projects are now listed in the appropriations schedules. Overall, 80 percent of the budgeted amounts were spent, although some funds were reprogrammed late in the year and thus not applied to the originally budgeted projects. No carry forward of unspent funds was permitted. The PIP system (an EU-supported effort) continues to provide incomplete information on proposed projects, in part reflecting the inability of budget organizations to adequately plan and analyze capital projects. Heavy turnover in the Budget Organization staff and weak participation by their chief financial officers in the process hampered progress. Much of the capital spending occurred at the end of the year and changes were approved from projects approved in the budget (1.1.12; 1.1.13).
- Required cost reviews of proposed legislation by MFE, conducted in the Budget Department before legislation may be presented for decision by the Government, which are being conducted with greater frequency but not in all cases (1.1.1; 1.1.10).
- The municipal budget department worked with municipalities to develop a new chart of accounts for the municipal budget that is more program and function oriented and therefore provides additional clarity to citizens regarding the use of public monies. This work was done with intensive involvement by the EMSG Program advisor (1.1.3; 1.1.5).

- The municipal budget department and advisor worked with others to develop procedures and instructions to implement the new laws on local self-government and local government finances, including new bases for central general grants and special purposes grants for health and education and clarification of the status of own-source municipal revenues, as required by the agreement for Kosovo's independent status (1.1.2; 1.1.5).
- The municipal budget department, with assistance from the EMSG Program advisor, developed and adopted a business and staff development plan for 2010 which, for the first time clearly states strategy and specific actions to be taken by the Department during the year to meet an array of performance objectives tied to the Department's mission (1.1.1; 1.1.3).
- A senior budget staff member is leading the secretariat that has drafted a PEFA self-assessment. By all accounts, this work has been effectively led by Kosovars, in contrast the 2007 PEFA assessment, under direction of the Deputy Minister of MFE and other policy officials. The government is committed to a public financial management action plan to address shortcomings identified in the PEFA assessment and other reviews (1.1.1; 1.1.12).
- The Macroeconomic Policy unit, under time constraints, developed multiple tax policy options for the Minister at his request, showing the pros and cons of each, in advance of a Government decision to adjust tax rates (1.1.7; 1.1.8; 1.1.9).

Treasury:

- Treasury, with advice from the EMSG Program and others, developed the systems and procedures needed to support decentralization of payments processing to municipalities and is ready to pilot that process with qualifying municipalities. An administrative instruction has been drafted, but not issued, to hand over responsibility in an orderly progression (1.1.5; 1.1.16).
- Treasury obtained assistance of a US Treasury advisor to guide implementation of the new law on debt and is prepared on reasonable notice to manage acquired debt and other international obligations (1.1.5; 1.1.15).
- Treasury continued to build new financial reporting capabilities and has continued to produce timely, transparent quarterly and annual reports using an internationally approved accounting scheme (1.1.14; 1.1.17; 1.1.18).
- Treasury set up a cash management unit to make projections and carry out an investment strategy (1.1.15).
- The Treasury director continued to drive improvements, based on his own analysis of the highest needs. He has identified a set of specific developmental projects needed in the coming year, including an on-line payment system, an assets module to help budget organizations keep track of their assets, interface between the Treasury and CBK systems, and improved internal controls. The last of these would be a major effort to strengthen the internal audit function and establish a new internal financial control unit. He has identified a specific need for additional international advice with regard to these planned projects (1.1.14; 1.1.19).

The established budget procedures had been used effectively in 2007 and again initially in 2008 to develop a framework for budget decisions and as a discipline during budget development for the following year, as well as to restrain various demands for new programs or other changes during the year. However, as explained below, initial use of the MTEF and budget processes was circumvented by decisions made outside and inconsistent with the initial budget framework and ceilings.

Last year, which also saw Kosovo's independence, the MTEF and budget planning for 2009 were initially shaped to influence donor decisions at a mid-year conference. Although promised donor support has not been delivered, the promise of future support distorted the timing and content of the Government's decision-making processes in 2008 as it had in the prior year.

Moreover, immediately following the donor conference, the Government announced important policy changes with major budget implications that were at odds with both the MTEF and expectations of donors. This required major adjustments prior to submission of the 2009 budget to the Assembly. More significantly, it raised doubts everywhere about the integrity of the recently established processes. The pattern of budget process circumvention established last year may have long-term implications for the sustainability of the institutions and processes that have received substantial USAID support.

Today, the Budget and Treasury Departments are highly professional, well-managed operations by all accounts. Their continued development was further validated by a forthcoming PEFA self-assessment, led by MFE staff, which shows improvement in scores since 2007 on most performance elements. The budget's credibility, transparency, and comprehensiveness have been upgraded. Budget execution receives modest upgrades, except for effectiveness of taxpayer registration, assessment, and collection (discussed in the following section). Higher scores also are given for some timeliness of some financial reporting and for the scope of external audit reports.

The Budget and Treasury Departments now use separate donated information software to support their functions. The Budget's Department's BDMS system has limited capability to support further development of performance or program budgeting approaches or to support and display multi-year capital project details. It also has limited reporting capabilities. The Treasury's Freebalance system is more sophisticated and includes a performance budgeting component – not currently used. It is maintained and updated on a regular basis by expert staff. Systems are adequate to support fiscal decentralization, including electronic submissions and reporting; however, expanded capacities could be considered as part of a review of technical options for future systems development. It is beyond the scope of this evaluation to assess the technical requirements for further systems development or the merits of alternative software solutions. However, we note that the limitations of the current system used for budgeting and see this as a constraint on further development of important aspects of the budget process.

Further training of staff and systems development is needed, but the needs are identified and owned by the two managers. Within these resource constraints, they can proceed to make needed improvements, with occasional consultation and expert advice from the EMSG Program or other international projects. Both are receptive to such continuing advice and support. However, the Treasury Director believes that future advisor support can focus less on technical training of his staff and more on policies and procedures to support stronger financial controls and internal and external auditing.

The Macroeconomic Policy unit retains a core of professional economists who continue to perform excellent quantitative and qualitative analyses of policy options. The integration of their work with that of the budget analysts has increased through a restructuring of the MTEF process. Their presentation and answers to questions by international representatives at the first fiscal surveillance meeting, held during our visit, was praised privately by IMF and ICO representatives who were present. We do not see a continuing need for an international expatriate advisor to the Macro unit as currently constituted. However, we do foresee future opportunities for short-term assistance in further developing the models for forecasting and other applications, such as revenue forecasting techniques, that would strengthen specific capacities of the Macro unit.

Recent changes external to MFE complicate the effort to establish sound sustainable budget formulation as the core of policy development and fiscal discipline for Kosovo. These include:

- Untimely intervention in last year's budget process, accompanied by a shift in locus of decision to the Prime Minister's office from MFE – this has reduced the ability of that Ministry to manage pressures on the budget. Unless accommodated in some fashion, this could undercut the integrity of the budget process as a disciplined focus for setting priorities within a negotiated overall fiscal constraint and specific targets tied to the Government's development strategy.
- Dismantling of the Government's donor coordination unit as part of a reorganization of functions – this complicates the task not only of coordinating international assistance to the Government but also of incorporating revenues from those sources in annual budgets.
- Failure to implement the Brain Fund as originally conceived – this raises doubts about whether this is a viable strategy for establishing and sustaining a top layer of professional administrators and subject experts that can outlast changes in political control and can lead and deepen the emerging culture of professionalism in Kosovo's civil service.

Development of the 2010-2012 MTEF has been slow to start. During our visit, a decision to post the central and municipal budget positions raises further questions about whether this process will proceed quickly. The prospects for a continued orderly, disciplined budget process are in question. The budget director, other senior MFE staff, and EMSG Program advisors are aligned in supporting an early review of priorities by the Government, to be approved at Cabinet level, and then used as the basis for the MTEF, which in turn will set targets for the 2010 budget. With the late start and unclear commitment to this policy process, it is doubtful that the statutory April 30 deadline for MTEF submission to the Assembly will be met and questionable if this can serve as the fiscal framework for the 2010 budget formulation.

4.1.d Recommended Next Steps

Several adjustments can be made in the short run to the EMSG Program and the work of its advisors to improve prospect of meeting the program's goals by June 2010.

1. Give highest priority to reestablishing the MTEF this year as the Government's vehicle for turning policies into concrete multi-year plans and targets for collection and use of resources to advance the Government's highest priorities.
2. Encourage the MFE to explore options and seek expert, neutral advice on requirements for an integrated Budget and Treasury system, linked electronically with MPS for personnel and payroll, to Tax Administration and Customs for revenues, and to CBK for debt management. As part of this review, expanded capacities to support fiscal decentralization should be considered. (Note: This responds to questions 14 a. i., ii., and iii. in the Statement of Work.)
3. Revive a previous USAID/BearingPoint emphasis on training and procedures for incorporating performance and program budgeting information into budget decision-making both centrally and in the preparation by budget organizations of their budget proposals for the coming year(s).
4. Focus efforts of the new EMSG Program advisor in Treasury on development of regulations for internal financial controls and stronger auditing functions, on support for linking Treasury, Budget, and payroll systems, and on other priorities established by the Treasury director. This could include limited technical assistance to municipalities in support of fiscal decentralization, in coordination with the municipal budget department. (Note: This responds to question 14 c. in the Statement of Work.)
5. Upon appointment of the new General Director of Budget, offer to provide a full-time advisor (probably by reassigning an existing advisor) to that individual to define operating procedures, policies for an integrated budget operation; and propose a training program to provide common and integrating processes for reintegration of the central and municipal budget departments as needed for coordinated, efficient budget formulation and execution.

4.2 Tax Administration (Including Property Tax)

4.2.a Objectives

In the area of tax policy/administration, the objective of the EMSG Program is to strengthen the ability of MFE/TAK to develop appropriate tax policies and administer them effectively consistent with international standards and the mandates of the settlement document. An important goal of EMSG in this area is to build and strengthen key Kosovar institutions responsible for tax policy and administration—primarily MFE and TAK—so that they have the organizational capacity and human resources needed to implement and sustain Kosovo’s tax system.

A modern and efficient tax system is essential to the development of a market-driven and self-sustaining economy in Kosovo. As a newly established country, Kosovo clearly has significant resource needs—for infrastructure, education, and social programs among others. Donor assistance and foreign investment will meet some of these needs. However to sustain its growth and development, Kosovo must raise significant resources via an efficient and well run tax system that minimizes both disincentive effects on aggregate production and distortions on the structure of production. Thus, the EMSG Program’s progress in the area of taxation should be judged primarily in terms of its contribution to the development of an efficient, well run, and sustainable tax administration in Kosovo.

4.2.b Status in June 2007

Background

At the inception of the EMSG Program in July 2007, Kosovo enjoyed a simple but reasonably well developed tax system. This system was essentially built from scratch starting in 1999 through the combined efforts of dedicated Kosovars, UNMIK, and various donors—primarily the US and EU². It is important to note that during the period covered by the previous 5 task orders implemented by USAID/BearingPoint (2000 to mid 2007) approximately 24 person years of tax-related assistance were provided by resident expatriate advisors.³ There can be no doubt that many, if not most, of the improvements in Kosovo’s tax system realized during that period were the result of this tax-related technical assistance provided by USAID and implemented by USAID/BearingPoint advisors.⁴

Data on tax revenues collected in Kosovo by type of tax between 1999 and 2008 are summarized in Table 1. It should be noted that domestic tax collections started in 2000 via simple sales, hotel/food/beverage, and presumptive taxes. In 2001, the former two taxes were eliminated in favor of a value added tax, and in 2002 wage and profits taxes were introduced and the presumptive tax was partially eliminated. By 2005, more full blown personal and corporate income taxes were adopted—incorporating previous profit and wage taxes and further reducing the presumptive tax. Equally important, tax administration was given a sounder legal basis with the adoption in April 2005 of the Law on Tax Administration and Procedures, which provides for sanctions against tax evasion, sufficient powers for collection, protection

² The tax system discussed in this section covers primarily the personal and corporate income taxes, the VAT collected on domestic economic activity, a small presumptive tax, and municipal property taxes. USAID technical assistance has been directed toward these taxes. Taxes and duties collected at the border—primarily VAT, customs, and excise (mainly on oil products)—are very substantial in terms of revenue generation (accounting for roughly 75 percent of total tax revenues collected), but have not benefited from significant amounts of USAID-provided technical assistance. Thus border taxes are not treated in this chapter.

³ See Annex A for a summary of the number of long term resident advisory supplied under the various task orders implemented by USAID/BearingPoint.

⁴ Evaluations in 2003 and 2006 of prior USAID/BearingPoint task orders support this conclusion.

of taxpayer rights, and a code of ethics for tax officials. Municipal property taxes were also collected from at least 2003 onward.

Table 1. Kosovo Tax Revenues (millions Euros)

Revenues/Year	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Total Tax Revenues⁵	15.5	125.3	324.6	501.1	526.7	555.5	568.6	629.2	724.5	817.0
Domestic Tax	-	6.5	45.7	80.0	109.4	114.1	129.0	167.4	191.5	221.6
VAT	-	-	12.5	28.7	39.5	44.7	46.4	47.8	58.8	58.4
Income		6.5	33.2	52.1	69.9	69.4	82.7	119.6	132.7	163.2
VAT Refunds	-	-	-	-	-	-	(1.8)	(3.3)	(9.0)	(21.3)
External Tax	15.5	113.9	242.4	370.1	413.8	435.9	434.4	457.5	533.7	605.0
Border VAT/Sales Tax	9.9	63.4	117.7	169.0	180.6	186.4	195.2	210.8	255.0	304.8
Customs	4.8	30.9	47.6	67.5	72.3	73.4	74.1	82.3	81.2	93.4
Excise	0.8	19.5	77.0	125.6	153.3	176.0	164.3	161.9	191.4	203.9
Other border taxes	-	-	-	8.0	7.5	0.1	0.8	2.5	6.1	3.0
Municipal and non-tax rev.		4.9	36.5	50.2	64.6	69.1	74.9	91.5	108.1	137.1
Municipal Property Tax	-	-	-	-	3.5	5.5	7.0	7.6	8.3	11.7

Source: Ministry of Finance and Economy
Government of Kosovo

EMSG Baseline

For the purpose of this evaluation, FY 2006 will be used to establish a baseline for the current EMSG Program. In that year, and as summarized in Table 1, approximately 175 million Euros worth of domestic taxes were collected. Domestic VAT, income tax (both personal and corporate), and municipal property tax accounted for roughly 27%, 68%, and 4% respectively of the total tax revenues collected.⁶

More important than the amounts of domestic tax revenues collected from different taxes is the state of Kosovo's tax administration regime as of FY 2006 since this largely determines a baseline to EMSG Program's efforts to strengthen tax administration and build capacity. Fortunately, the IMF's Fiscal Affairs Department completed an assessment of the state of Kosovo's tax administration as of November 2006.⁷ This assessment concluded that Kosovo's tax administration had made good progress in establishing a sound legal basis, developing a simplified income tax structure, and better aligning VAT legislation with the EU's Sixth VAT Directive. The IMF also concluded that there was a significant need for TAK to adopt administrative procedures more consistent with international best practices.

Recommendations of the IMF report provided much of the basis for TAK's Strategic Plan 2007 – 2010, which was adopted by the Government of Kosovo as a blueprint for reform and strengthening of TAK.⁸

⁵ Total tax revenues equal total domestic, external, and property taxes refunds.

⁶ Taxes collected at the border accounted for 457.5 million Euros in FY 2006. This was approximately 73 percent of total tax revenues. Over time, one would hope to see the share of border tax revenues in total tax revenues decline as Kosovo's economy grows and greater emphasis is placed on direct taxation of income as opposed to indirect VAT, excises, or customs duties at the border.

⁷ International Monetary Fund, "Kosovo: Opportunities for Strengthening Tax Administration", November 2006.

⁸ Further input from the IMF in early 2008 resulted in this document being revised into a Strategic Plan for 2008 – 2010.

This plan identified needed reforms in the following areas, among others:

- a. Dealing with customers
 - Improve taxpayer communications
 - Improve tax registration of businesses
 - Improve debt management (collections) procedures
 - Increase voluntary filing and identify non-filers/stop filers
- b. Organizational reform
 - Improve planning and oversight
 - Strengthen headquarters responsibilities and lines of communications
- c. Staff strengthening
 - Implement a management performance system
 - Provide needed staff training/development
- d. System improvements
 - Develop risk-based systems for direct and indirect taxes
 - Improve management information systems
 - Increase SIGTAS operational capabilities

4.2.c Progress under the Current Program

Tax revenue trends

Progress under the EMSG Program in the area of taxation can be assessed in several different ways. Total domestic tax revenues have continued to increase at a good pace since the start of the EMSG Program. Specifically, total domestic tax revenues increased by about 14 percent and 15 percent between 2006/2007 and 2007/2008 respectively, as compared with increases of 13 percent and 30 percent between 2004/2005 and 2005/2006. The share of direct tax revenues (from personal and corporate income taxes) in total domestic non-property tax revenues increased slightly from the start of EMSG—from 71 percent in base year 2006 to 74 percent in 2008—while the share of indirect non-property tax revenues (from VAT) declined from 29 percent to 26 percent. However, this slight trend is not expected to continue into 2009 due to the reduction in personal and corporate income tax rates from 20 percent to 10 percent and the increase in the VAT rate from 15 percent to 16 percent implemented on January 1, 2009. As part of total domestic tax revenues, municipal property tax revenues are small—accounting for only five percent of total domestic tax revenues in FY 2008. However, there is potential for municipal tax revenues to increase significantly in the future. To summarize, domestic tax revenue trends under the EMSG Program are “good” and represent a continuation of what was observed in prior years. That is, domestic tax revenues have been relative buoyant (growing faster than the economy) with a slight relative growth in revenue from direct income taxes. This continuity of revenue trends under the EMSG task order is not surprising since it is very much a continuation of prior USAID task orders, as well as part of a broader and on-going donor-led effort to build key economic institutions in the Government of Kosovo.

Achievement of EMSG Results:⁹

Another way to assess the EMSG Program’s achievements to date in the area of tax is to look at its performance against desired results specified in the EMSG Program statement of work. These desired results for TAK and MFE (re. the property tax), and their status to date, are discussed below.¹⁰

⁹ It is also worth keeping in mind that USAID is not the only donor providing assistance to TAK. Specifically, the EU’s CAFAO activity has provided technical assistance to TAK in the past; and additional EU technical assistance is scheduled to start later in 2009.

TAK-related Results

- Result 1.2.1 TAK is a well-functioning agency, able to competently carry out its responsibilities without full-time USG assistance.
- Status:* Partially achieved. TAK continues to make progress towards becoming a well functioning agency, although by general agreement this progress has been hampered by steady turnover among top management. Most of the necessary legal framework is in place (or expected shortly)—including a revised Law on Tax Administration and Procedures (approved in January 2009) and a revised VAT Law (approved in December 2008) --both drafted with significant EMSG Program input. TAK still needs to strengthen its management, operations, and systems if it is to come closer to meeting international best practices. According to TAK management, current EMSG Program advisors are indispensable in helping TAK develop and implement these improvements
- Result 1.2.2 TAK collects taxes in a competent, professional and even-handed manner, with the result that taxpayers are increasingly compliant, having confidence that TAK is assessing taxes accurately.
- Status:* Partially achieved. Tax payer compliance rates are up marginally. See status of Result 1.2.14.
- Result 1.2.3 TAK Headquarters managers (director, deputy directors and department heads) have strong management skills, asserting appropriate oversight of regional offices so that taxes are collected in a consistent manner across Kosovo.
- Status:* Partially achieved. Significant amounts of professional skills training have been provided to many managers. It is difficult to assess to what extent such training has led to a more consistent application of the tax system across Kosovo.
- Result 1.2.4 Secondary legislation and manuals exist for interpreting tax laws.
- Status:* Achieved. USAID/BearingPoint advisors have helped with secondary legislation/manuals over the last few task orders. Under the EMSG Program, advisors have drafted secondary legislation on implementing new tax rate, and for levies on bank accounts. This work is on-going with sub-legal act drafting underway for implementation of fiscal cash registers and enforced collections.
- Result 1.2.5 Tax legislation is amended, as needed, to comply with settlement document.
- Status:* Achieved. EMSG Program advisors have assisted with drafting amendments for the Law on Religious Freedom, the Law on Tax Administration and Procedures, the VAT Law, and the Laws on Personal and Corporate Income Taxes. EMSG Program assistance with drafting tax legislation and implementing regulations is an on-going need.
- Result: 1.2.6 TAK procedures, including selection of taxpayers for audit, are transparent and objective so that opportunities for political or other influence are minimal.
- Status:* Partially achieved. EMSG Program advisors are helping TAK develop a risk-based audit methodology that will minimize political and other influences. This methodology is not yet fully implemented.

¹⁰ The evaluation team's assessment of various results specified in the EMSG Program statement of work is hampered by the lack of agreed upon indicators for these results. Many of the specified results are rather vague or subjective, and thus their status is difficult to determine with certainty.

- Result 1.2.7 VAT refunds are made in a timely manner.
Status: Not achieved. Limited evidence suggests average VAT refund times have not declined significantly. However, the number of VAT refund claims has increased (from 23 in 2005 to 128 in 2008), which has been the focus of TAK efforts. Most refund delays are due to problems with processing by regional tax offices.
- Result 1.2.8 Procedures for VAT refunds are based on best practice, effectively utilizing risk-based audits.
Status: Not achieved. The current work of EMSG advisors is helping TAK to develop a risk-based audit methodology that applies to taxpayers overall. It will determine which taxpayers are most “risky” and thus deserving of audit. This methodology will not focus specifically on VAT refunds. However, and as noted for Result 1.2.7 above, most delays with VAT refunds result from problems in the regional tax offices, not because of slow or ill-targeted audits.
- Result 1.2.10 The Large Taxpayer Unit (LTU) effectively and transparently manages its taxpayers.
Status: Achieved. The LTU has been in operation since 2000. It services 350 taxpayers characterized by an annual turnover of at least 2 million Euros and more than 100 employees. In FY 2008, the LTU collected roughly 67 percent of total TAK revenues, with 92 percent of those revenues being paid voluntarily. The LTU is currently using an early version of the risk-based audit methodology.
- Result 1.2.11 Audit departments (particularly LTU) implement risk-based, objective audits.
Status: Partially achieved. As noted for results 1.2.6 and 1.2.10 above, a relatively sophisticated risk-based audit methodology is currently under development with the support of EMSG advisors.
- Result 1.2.12 Taxpayers have clear, understandable tax guides.
Status: Partially achieved. An all inclusive tax guide is available, but needs to be update to reflect current versions of various tax laws.
- Result 1.2.13 Management Information Systems are effectively used to guide management in assessing and improving performance.
Status: Not achieved. The current SIGTAS IT system generates various reports, but they are not used for management purposes. An upgrade of SIGTAS is underway and this upgraded system will produce most of the reports needed for effective tax management.
- Result. 1.2.14 Increased compliance is shown by improved rates of collection, with direct taxes (personal and corporate income taxes) showing an increasing proportion of all tax revenue.
Status: Achieved. The share of tax revenues collected voluntarily increased slightly from 82 percent in FY 2007 to 86 percent in FY 2008. The share of direct taxes in total domestic non-property tax increased from 71 percent in FY 2007 to 74 percent in FY 2008. As noted previously, this trend is unlikely to continue in FY 2009 due to the January 2009 reductions in income tax rates and the increase in the VAT rate.

Property Tax-related Results

Result 1.1.20 Municipalities have increased capacity to use market valuations for assessing properties for property tax

Status: Achieved. Municipalities now regularly used data on arms-length real estate transactions in their assessment jurisdiction to establish average market values (on the basis of square meter) for each property class in each valuation zone. The MFE's Property Tax Department audits the municipal property tax offices to ensure that these values correspond with available market data and the general experience of real estate agents and other professionals. While the limited amount of property data available permits only a rudimentary estimation of property values, the current approach to valuation reflects the overall market, is highly transparent, and easy to administer.

Kosovo is on the cusp of a dramatic improvement in municipalities' ability to appraise real estate according to market value. A tender is being finalized to resurvey all existing records in the fiscal cadastre. The resurvey is being coordinated with the Kosovo Cadastre Agency (KCA) and will verify existing information as well as record the external characteristics of properties, x-y coordinates, and a photograph of the property. It is expected that this effort will start with a pilot in May 2009 before being rolled-out to the rest of Kosovo's municipalities later in the summer. The entire resurvey effort will likely finish in the first quarter of 2010. Once these additional data elements are included in the fiscal cadastre, more sophisticated mass appraisal models can be developed

Result 1.1.21 Property tax collections increase yearly

Status: Achieved. As reported in Table 1, property tax revenue increased steadily from 2004 through 2008. The significant increase in 2008 was the result of major improvements in administration and enforcement efforts. In January 2008, work began on ad hoc changes to the existing property tax IT system to facilitate the outsourcing of bill production and delivery by Post & Telecom Kosovo (PTK). PTK was able to print and delivery bills at a cost of €0.247 per bill which represented a 60% savings on the municipalities' cost of service. In addition to its ability to print and deliver bills more cheaply and quickly, PTK had a 95% delivery success rate—far above what any municipality could achieve using their own staff.

Also at the beginning of 2008, the MEF Property Tax Department submitted detailed recommendations on improving enforced collections to the newly elected local government administrations. These focused on requiring taxpayers to provide their receipt of property tax payment before municipalities provide services. For example, before taxpayers could register their vehicles, register a change in property ownership, or be issued a business license or building permit, they had to prove they were up-to-date in their property tax payment. This proved to be very effective and resulted in the collection of a significant amount of arrears. The roll-out of a new IT solution for municipal property tax administration will also help to ensure that property tax revenue continues its upward trend. Among other things, it will allow municipal collectors to quickly identify delinquent taxpayers and organize their efforts to visit those taxpayers or deny municipal services when the taxpayer submits an application.

Result 1.1.22 New municipalities are certified and trained in financial management and in collection of property tax

Status: Achieved. The initial three pilot municipalities of Mamusa, Junik and Hani i Elezit established their municipal property tax offices in 2007. The MEF Property Tax Department trained these staff in all aspects of property tax administration and spent a significant amount of time providing on-the-job training. These municipalities were formally certified to administer the property tax in 2008.

Result: 1.1.23 Property Tax Department proactively works with municipalities to improve collections

Status: Achieved. See the discussion of Result 1.1.21 above. In addition, the MEF Property Tax Department conducts training on enforced collections with each municipality at least twice per year and more often with municipalities whose revenue does not increase year-over-year. Finally, in 2008, the MEF Property Tax Department and TAK, together with the Bankers Association of Kosovo, established the procedures for seizing the bank accounts of delinquent taxpayers.

Regional Comparisons

A final way to assess progress made in strengthening Kosovo's tax system is to compare its performance with the performance of tax systems in other similar or neighboring countries. Simple tax information on collections, rates, and revenue performance for Kosovo, neighboring countries, and corresponding average figures for countries at Kosovo's approximate level of per capita income are summarized in Table 2. Several salient facts are worth noting:

1. Kosovo's overall tax revenue mobilization (12.5 percent of GDP) in 2007 is comparable to (if slightly below) several neighboring countries, and well below the tax revenue mobilization found in Croatia or Serbia. Kosovo's tax revenue mobilization is slightly below that found, on average, in other countries at the same level of per capita income. More or less the same general pattern is found when it comes to tax revenues mobilized by the corporate income tax. Revenue mobilization by the VAT in Kosovo is somewhat higher than found in several other regional countries and is higher than the average for similar income countries. In contrast, revenues mobilized by the personal income tax are low in Kosovo even relative to its neighbors, let alone other similar countries.

Table 2. Tax Benchmarks in Selected Countries (2007)¹¹

Country\Benchmark	<u>Total Tax</u> ¹² GDP	<u>VAT</u> ¹³ GDP	<u>CIT</u> ¹⁴ GDP	<u>PIT</u> ¹⁵ GDP	<u>VAT</u> ¹⁶ MAX	<u>VAT</u> ¹⁷ PERF	<u>CIT</u> ¹⁸ MAX	<u>CIT</u> ¹⁹ PERF	<u>PIT</u> ²⁰ MAX	<u>PIT</u> ²¹ PERF
Albania	12.8	9.1	2.2	1.5	20	58	10	0.22	10	0.15
Croatia	20.8	13.9	3.3	3.6	22	113	20	0.17	45	0.09
Kosovo	12.5	9.7	1.7	1.1	16	75	10	0.08	10	0.06
Macedonia	12.9	8.7	1.5	2.7	18	51	10	0.06	10	0.27
Montenegro	10.5	7.2	0.8	2.5	17	74	29	0.04	12	0.21
Serbia	17.7	11.0	0.9	5.8	18	87	10	0.09	27	0.18
Average Low- Mid Income Country	13.2	6.8	3.5	2.9	15.5	65	26	0.13	28	0.11

¹¹ For more details on the tax benchmarking methodology used in Table 2 see Mark Gallagher, "Benchmarking Tax Systems" at http://www.fiscalreform.net/index.php?option=com_content&task=view&id=545&Itemid=139

2. Kosovo's tax rates for the VAT, corporate income, and personal income are relatively low—even compared with its neighbors where tax rate reductions to increase national competitiveness and improve the investment climate have been the rage recently. Such low tax rates, of course, result in lower tax revenue mobilization absent major supply side effects.
3. Table 2 also provides measures of individual tax revenue performance in Kosovo and other countries. These essentially measure how well a country does in mobilizing resources from a particular tax while controlling the tax rate. Factors relating to tax administration, such as non-compliance, avoidance, corruption, and general administrative efficiency can impact these measures of revenue performance. However, structural measures such as thresholds, allowances, exemptions, and the general nature of the tax base can also influence these performance measures. Once again, a fairly consistent pattern emerges. Specifically, revenue performance for the VAT and corporate income tax in Kosovo is comparable to revenue performance in several neighboring countries, while performance for the personal income tax in Kosovo lags well behind that found in most neighboring countries.

What tentative conclusions can be drawn from these tax comparisons? Overall, Kosovo's tax structure and performance are not drastically different than what is observed in other regional countries. However, the overall level of tax revenue mobilization is low relative to the tax mobilization found on average in lower middle income countries. The regional tendency towards relatively low tax rates may go a long way towards explaining this relatively low tax revenue mobilization in the region. Given that many of the countries in the region—especially Kosovo—have significant public expenditure needs for infrastructure, health, education and so on, low tax revenue may be a significant problem.

Finally, the personal income tax in Kosovo stands out in terms of its relatively low revenue mobilization and its low revenue performance, with the corporate income tax performing somewhat better but still below what is observed, on average, in lower-middle income countries. It might be wise to attempt to identify and address as appropriate the structural and administrative factors that are responsible. This is especially true since over time and as Kosovo develops one would expect to find direct income taxes accounting for an increasing share of tax revenues.

4.2.d Recommended Next Steps

There is no doubt that Kosovo has made tremendous strides since 1999 towards developing a modern tax system. An adequate legal framework exists and there is at least a core of well trained managers and staff. Finally, a comprehensive (if somewhat unfocused) plan to modernize and strengthen TAK has been agreed upon and is being implemented. TAK's performance, while not stellar, is in line with that of other countries in the region—with the exception of a seemingly under-performing personal income tax. This progress would not have been possible without the expert advice and hand-on training provided by technical advisors from the USG, EU, IMF and elsewhere working with TAK. It is clear that USAID/BearingPoint advisors supplied under the six task orders to date have made a huge contribution to the growth and development of TAK. Under the EMSG Program, USAID/BearingPoint advisors are making good progress in achieving most tax-related results identified in the statement of work.

¹² Total Tax revenue/GDP (percent)

¹³ Total VAT revenue/GDP (percent)

¹⁴ Total Corporate Income Tax/GDP (percent)

¹⁵ Total Personal Income Tax/GDP (percent)

¹⁶ Maximum VAT rate (percent)

¹⁷ Total VAT revenue/Total Private Consumption divided by VAT rate

¹⁸ Maximum corporate income tax rate (percent)

¹⁹ Total corporate income tax revenue/GDP divided by CIT rate

²⁰ Maximum personal income tax rate (percent)

²¹ Total personal income/tax revenue/GDP divided by PIT rate

Within this context, the following actions/next steps between now and June 2010 are recommended:

1. Stay the course. The amount of technical assistance supplied to TAK/MFE by USAID/BearingPoint advisors declined steadily—from six advisors during Task Order 2 to three advisors for Task order 6 (plus a recent arrive to work on IT issues). This level of assistance appears about right for the remainder of the current task order.
2. Assistance being supplied by USAID/BearingPoint to TAK is well targeted. Advisors are focusing their efforts on helping TAK better target audits, improve collections, better coordinate business registration, and strengthen its IT system (SIGTAS). Gains in these areas have the potential to improve TAK's revenue performance. TAK's current 2008–2010 Strategic Plan is very comprehensive and ambitious. Between now and June 2010, it would be prudent for EMSG Program advisors to continue to focus on the priorities identified above and thus avoid being spread too thin across the full gamut of needs identified in the Strategic Plan.
3. The decision to end EMSG Program assistance relating to property tax as of November 2009 makes sense. The Property Tax Department benefits from strong capable leadership and is receiving assistance from SIDA. Property tax revenues have increased steadily and methods for assessment and collection are being improved and modernized. USAID/BearingPoint's job with respect to property tax is done.
4. TAK could likely improve its revenue performance by adding roughly 100 additional staff²²—if these staff were sufficiently educated and training. If TAK decides to move in this direction it might make sense for USAID to make limited additional resources available (through USAID/BearingPoint or some other mechanism) to help structure appropriate training programs.

4.3 Central Bank of Kosovo

4.3.a Program Objectives

The Scope of Work for Task Order 6 called for the contractor to supply a full-time advisor to the bank supervision department of the Kosovo Central Bank (CBK), along with targeted short-term assistance to the pension and insurance departments. Overall project objectives from the statement of work include strengthening the ability of key economic institutions (including CBK) to support economic growth. A specific sub-objective for CBK is to strengthen its supervision departments.

Thirteen progress indicators were established for this activity. From reviewing the indicators, it is clear that the actual objective of the assistance was considerably broader: to strengthen the overall capacity of the CBK to oversee the financial sector of the country. The progress indicators were as follows:

1. CBK's supervision departments exercise strong, competent oversight and regulation of the commercial banks, insurance companies, Kosovo Pension Savings Trust and private pension companies.
2. Public confidence in the commercial banking sector is shown by an increasing level of deposits.
3. Core Basle Principles scores for CBK show annual improvement.
4. Supervision Department competently performs Basle Core Principles self-assessment and drafts action plan for remedying deficiencies.
5. Bank inspectors are knowledgeable about new banking products and changing commercial practices.
6. Supervisory profiles of all licensed banks are established.

²² Given Kosovo's population, the size of TAK's staff is relatively low when compared with most other countries in the region and even when compared with my higher income countries.

7. For both on-site and off-site examinations, bank examiners are knowledgeable, analytical and appropriately proactive in supervising banks, able to detect problems early, devise action plans and enforce appropriate corrective action.
8. Bank examiners perform meaningful analysis of commercial bank reports and update CAMELS ratings for commercial banks.
9. Bank licensing manual is updated and procedures are significantly improved.
10. CBK vigorously implements bank licensing requirements.
11. Bank inspectors rigorously enforce Anti-Money Laundering laws.
12. Bank inspectors effectively audit internal controls of commercial banks.
13. Insurance and pension supervisors competently supervise insurance companies and pension plans.

4.3.b Conditions at Program Initiation

The CBK's primary role is prudential supervision of banks, insurance companies and pension funds. As Kosovo does not have its own currency (the Euro circulates as the medium of exchange), the Bank cannot conduct monetary policy. The financial institutions in all three areas needed to be created from scratch after 1999. In all three areas, USAID advisors were involved in basic legislative frameworks and in promoting the establishment of regulatory institutions. The banking system is the most developed, with two international and five local banks, with deposits at the beginning of Task Order 6 of more than one billion Euros.

USAID assistance to the CBK had been ongoing since its establishment after the 1999 war. USAID/BearingPoint staff had gradually shifted from executive positions in the bank to advisory ones. In early 2006, the last executive position of deputy managing director staffed by USAID/BearingPoint was transferred to a Kosovar, although the managing director continued to be an expatriate funded by the IMF. The level of USAID support steadily declined from six long-term advisors under the first two Task Orders to three under Task Order 5.

The institutionalization of supervision of commercial banks was well-established, with methodologies and procedures for risk-based supervision implemented. Capacity building of CBK staff had become institutionalized, and the regulatory oversight by the CBK was being steadily upgraded.

Nevertheless, the end-of-project report for Task Order 5 also concluded that continued mentoring would be needed in the future, noted that a professional certification program for CBK staff had not been implemented, and stated that a number of prudential rules needed to be revised to bring them into closer compliance with Basle II standards.

4.3.c Progress Under Current Program

The USAID/BearingPoint advisor on bank supervision required under the current Task Order was brought on board in early 2008. He remained held this position for 13 months, departing at the end of March, 2009. Progress in improvement of bank supervision continued during this period, as discussed below. In early 2008, the position of managing director was transferred to a Kosovar who had been groomed for the position by BearingPoint.

The CBK has reached a level of professionalism and institutionalization that has allowed USAID to pull back from extensive support. There are still tasks to be done, particularly in strengthening of CBK oversight of insurance and pension funds, and in establishing a system of deposit insurance, but other donors appear prepared to provide the necessary support.

As noted below, regulation of insurance and pension funds has lagged behind bank supervision in terms of professional development. The World Bank is expected to provide a long-term advisor to help address this problem in 2009. Deposit insurance is an activity that KfW has been supporting, although progress has continued to lag because of policy disagreements over details of the insurance scheme. Legislation in this area is now expected during the last half of 2009.

In terms of the thirteen indicators established by USAID for Task Order 6, the following summarizes the current state:

Indicator 1	CBK's supervision departments exercise strong, competent oversight and regulation of the commercial banks, insurance companies, Kosovo Pension Savings Trust and private pension companies.
Assessment	Partially Achieved. The supervision of commercial banks has improved during the tenure of the long-term advisor. Oversight of insurance companies and pension funds is weaker, although improving. The World Bank has tentatively agreed to provide a long-term advisor in this area, so further USAID assistance is no longer necessary.
Indicator 2	Public confidence in the commercial banking sector is shown by an increasing level of deposits.
Assessment	Achieved. Deposits in the commercial banks have continued to rise steadily and rapidly, showing growing public confidence. Deposits rose 22% in 2008 to 1.35 billion Euros, after having risen 25% during 2007.
Indicator 3	Core Basle Principles scores for CBK show annual improvement.
Assessment	Achieved. An IMF/World Bank assessment in early 2008 found significant improvement by the CBK in complying with Basle standards. The Bank was found to be materially non-compliant with six of the 25 standards. None of these six were considered serious obstacles to the Bank's effectiveness in supervision. The BearingPoint advisor reported that further progress had been made during the subsequent year, although he did not quantify the gap beyond stating that the CBK was about two years behind Western European banks in implementing Basle II. The advisor also expressed concern that future progress might falter in the absence of external advisor in the Bank. While the European Commission provides some assistance, he reported, this tends to be short-term and focused on specific issues, rather than on overall strategies for meeting international standards.
Indicator 4	Supervision Department competently performs Basle Core Principles self-assessment and drafts action plan for remedying deficiencies.
Assessment	Achieved. An action plan for remedying deficiencies has been drafted, approved by CBK management, and is being implemented.
Indicator 5	Bank inspectors are knowledgeable about new banking products and changing commercial practices.
Assessment	Partially achieved. The entrance of international banks into the Kosovo market has led to the introduction of new products and practices. Some training has been undertaken to acquaint bank inspectors about such issues. Yet, there is some risk of the CBK falling behind developments in the future.
Indicator 6	Supervisory profiles of all licensed banks are established.

Assessment	Achieved. These profiles were established in the first half of 2008, and the CBK has continued to refine them.
Indicator 7	For both on-site and off-site examinations, bank examiners are knowledgeable, analytical and appropriately proactive in supervising banks, able to detect problems early, devise action plans and enforce appropriate corrective action.
Assessment	Substantially achieved. Skills have been upgraded, but the lack of English competency by many examiners limits their ability to obtain advanced certification and other international training opportunities.
Indicator 8	Bank examiners perform meaningful analysis of commercial bank reports and update CAMEL ratings for commercial banks.
Assessment	Achieved. CAMEL ratings for commercial banks have become institutionalized, and are being used as a tool for CBK oversight.
Indicator 9	Bank licensing manual is updated and procedures are significantly improved.
Assessment	Achieved. The manual has been updated and procedures significantly improved. Nevertheless, the continued evolution of banking practices and standards will require further revisions over time.
Indicator 10	CBK vigorously implements bank licensing requirements.
Assessment	Completed. Licensing requirements established by UNMIK were fully implemented.
Indicator 11	Bank inspectors rigorously enforce Anti-Money Laundering laws.
Assessment	Substantially achieved. The CBK examiners include anti-money laundering as part of annual examinations of commercial banks. Two specialists in this area, with extensive training, address this issue.
Indicator 12	Bank inspectors effectively audit internal controls of commercial banks.
Assessment	Completed. Regulations were drafted and approved by the CBK board, and are being implemented.
Indicator 13	Insurance and pension supervisors competently supervise insurance companies and pension plans.
Assessment	Not achieved. There is general agreement that supervision in these areas lags significantly behind supervision of commercial banks. Nevertheless, Task Order 6 did not propose a long-term advisor in this area. Given the presence of other donors, this seems a prudent decision. The World Bank is said to be close to agreement on providing a long-term advisor to help address these issues.

4.3.d Recommended Next Steps

As part of the phase-down of USAID assistance, the USAID/BearingPoint advisor on bank supervision ended his tour on March 31, 2009, with no further long-term assistance planned. Going forward, US assistance will be in the form of 8-10 visits per year from a Treasury advisor resident in Bosnia, so USAID's connection with CBK is expected to be close.

Despite the steady improvement in the operation of the institution, the CBK has requested additional assistance from USAID in the form of a long-term advisor on overall financial management. The Bank

considered the relatively limited experience of the CBK executives and professionals to be a risk at a time of huge turmoil in international financial markets. The Bank regarded an experienced foreign advisor as potentially providing important support for the Bank at a crucial time.

USAID support for the CBK has been critical to its development as a competent institution. As challenges remain, the IMF and other donors are also contributing to the deepening of the skills of the CBK. Therefore, we support the USAID decision to end long-term advisory support to the CBK, and recommend that no further long-term assistance be provided.

4.4 Commercial Law Development

4.4.a Objectives

For a country to grow, develop, and prosper in a sustainable fashion, it needs a healthy and vibrant private sector. Private sector growth depends, among other things, on the adequacy of the enabling environment within which it operates. This enabling environment is characterized by the laws, rules, regulations, and implementing institutions that establish how private sector firms operate. A key element of this private sector enabling environment is the commercial law regime. This consists of the laws, regulations, and institutions that define how firms form, register, hire labor, interact with other firms, compete, resolve commercial disputes, and dissolve. Without an adequate commercial law environment, a country's private sector will not thrive.

The overall objective of USAID/BearingPoint's work in this area under Task Order 6 is to help stimulate trade, investment, and growth in Kosovo through the development and implementation of a modern and effective regime of commercial laws, rules, and regulations. Specifically, the contractor is to train Kosovo's legal community (primarily commercial court judges, other interested judges, and commercial law attorneys) on the new commercial law regime put in place since 2000. This training is to include formal classroom training and workshops, on-the-job training, and mentoring. Finally, the contractor is to ensure training is institutionalized so that it can be sustained in the future. As described in greater detail below, the commercial law objectives established for Task Order 6 represent a clear continuation of the support to commercial law development provided in prior task orders.

4.4.b Conditions at Program Initiation

Approximately 22 years of technical assistance in the area of commercial law development have been funded by USAID and supplied by USAID/BearingPoint advisors since the first task order started. Since the earliest task orders, this assistance focused in three areas: (1) drafting of commercial legislation and implementing regulations; (2) providing support and capacity building to the Office of Legal Services Support (OLSS) in the Office of the Prime Minister aimed at improving the legislative development process; and (3) providing assistance to the Assembly to facilitate enactment of commercial legislation. This emphasis on drafting support and capacity building for the OLSS and the Assembly continued through Task Order 5, which ended in June 2007. In addition, starting with at least Task Order 5, the contractor also provided commercial law training to commercial court and other judges as well as private and public sector lawyers.

As noted in the June 2007 Final Project Report for Task Order 5 (Kosovo Economic Development Initiative), "nearly all core and commercial legislation needed to support the proper functioning of a market economy has now been promulgated." This includes laws on collateral, bankruptcy, commercial arbitration, competition, foreign trade, foreign investment, trademarks, procurement, and so on. Also, as a result of the contractor's assistance in this area, the Government of Kosovo adopted a set of standardized procedural rules to govern the drafting of legislation. These rules required stringent quality control and EU compliance checks before a draft law is submitted to the Assembly. By the end of Task

Order 5, drafting skills within the OLSS had improved to the point the contractor rarely needed to produce first drafts and instead, could focus on advising on drafts produced by counterparts.

4.4.c Progress Under the Current Program

A number of results relating to commercial law development are specified in the EMSG Program's statement of work.²³ Those results, and the extent to which each has been achieved to date, are summarized below:

- | | |
|-------------------|---|
| Result 2.0.1 | Practical material and training plans on new commercial laws have been developed. |
| <i>Assessment</i> | Achieved. Very clear and detailed training materials have been, or are being, prepared for many key commercial laws in Kosovo. These training materials are developed by local Kosovar lawyers (with project oversight), who are then engaged to provide the actual training. This approach to training appears thorough, detailed, and is very hands-on—emphasizing case studies, interactive discussions, and exercises. |
| Result 2.0.2 | Judges who hear commercial cases and commercial law attorneys understand policies and concepts underpinning the laws – how and why enforcement of these laws will support a market economy. |
| <i>Assessment</i> | Partially achieved. To date, approximately 73 Kosovar judges and 48 Kosovar lawyers have been trained under EMSG. The feedback obtained from course evaluations has reportedly been very positive, albeit no attempt has been made to assess the impact or long term benefits of the training. |
| Result 2.0.3 | Judges who hear commercial cases and commercial law attorneys understand and enforce Kosovo's new commercial laws. |
| <i>Assessment</i> | Unknown—no information. |
| Result 2.0.4 | Commercial law training is institutionalized, including a certification process; this may be in the Kosovo Judicial Institute (KJI) or some other organization identified by the Contractor in consultation with USAID. |
| <i>Assessment</i> | Partially achieved. Training for judges and lawyers is being implemented in conjunction with the KJI and the Kosovo Chamber of Advocates (KCA). To some extent, this training has been institutionalized since it is conducted in conjunction with KJI/KCA. In addition, the development of the training material has had the long-term benefit of creating a small cadre of Kosovar lawyers who are well versed in the new commercial laws and well prepared to provide training. KJI receives funds through the Ministry of Justice and various donors (including USAID). KCA is supported by membership dues. A certification process for the judiciary is under discussion, but not yet in place. |
| Result 2.0.5 | Legal community enforces commercial laws to the extent that business community, including foreign investors, is assured that rights will be protected. |
| <i>Assessment</i> | Status could not be determined. |

Besides the formal training of judges and lawyers discussed above, there are several other ways in which the EMSG Program is continuing to help strengthen the commercial law environment in Kosovo.

²³ No indicators for these results have been agreed upon.

Specifically, the USAID/BearingPoint legal advisor continues to provide legal advice and drafting assistance when requested for the steady stream of new laws that are being prepared.²⁴

Other advisors also provide substantial technical input and guidance when laws or implementing regulations relating to specific sectors are being prepared (e.g. amending the corporate tax law or revising the VAT law to bring it into full compliance with the EU's VAT directive).

4.4.d Recommended Next Steps

The main strengths of the EMSG Program's commercial law program are: (1) it builds upon an ambitious USAID supported effort over the past five task orders aimed at helping Kosovo establish a commercial law framework to foster private sector-led growth and developing the "in-house" capacity to develop, draft, implement and administer this legal framework; 2) it utilizes an innovative and relatively hands-on approach to training; (2) it emphasizes building and using local training capacity; (3) it at least partially institutionalizes this training within KJI and KCA; and (4) its apparently provides a beneficial impact—based on the very positive feedback received from trainees on the quality of the training and materials provided.

Possible next steps include:

1. Development and implementation of a methodology to assess the actual impact on the performance on judges and lawyers of the training being provided by USAID/BearingPoint. Hopefully, findings derived from this methodology will allow interested parties to better assess the on-going need, if any, for such training.
2. Support for development of a certification process for judges/lawyers once there is agreement to move forward with it.
3. Focus more on the sustainability of such training. Currently, the absence of admissions fees for trainees means that such training is not inherently sustainable (absent donor or Ministry of Justice funding) and does little to ensure training is targeted as effectively as possible.
4. Finally, a "Doing Business" study for southeast Europe in 2008²⁵ indicates that enforcement of contracts is a slow and costly business in the region. This is especially true in Kosovo, which ranks near the bottom in terms of overall ease of contract enforcement. The benefits of relatively narrow judicial training may be limited in the absence of broader efforts to streamline court procedures and develop alternative dispute resolution mechanisms.

4.5 Pristina Airport and Public/Private Partnerships

4.5.a Program Objectives

In the original scope of work for Task Order 6, the objective was to privatize or commercialize publicly owned enterprises (POEs). Principal among these was the Kosovo Energy Corporation (KEK). In addition, the Task Order requested assistance to the Government to concession the Pristina airport, and to promote divestiture of other POEs, most notably the Post and Telecom of Kosovo (PTK), but also of other "big-ticket" enterprises like the Brezovica ski area or Sharr Cement.

While the efforts to deal with the "big-ticket" POEs continued to be a major objective, the emphasis gradually shifted towards supporting the concessioning of the Pristina airport and to supporting creation of a permanent administrative unit to promote public-private partnerships (PPPs).

²⁴ More than 100 new laws were approved by the Assembly in both 2007 and 2008.

²⁵ World Bank, *Doing Business in South East Europe 2008*, pp. 16 – 18.

This evaluation was explicitly enjoined from addressing the KEK privatization, perhaps because this was regarded as so political to the degree to be beyond the influence of technical advisors. Four other program objectives were assessed. These are:

1. Pristina International Airport is operating under a concession.
2. Relevant legislation relating to the transfer of POEs and civil aviation pursuant to the settlement document is enacted.
3. Government has policies and strategies for POEs.
4. Another POE, such as PTK, is commercialized or is being prepared for commercialization (if the Government takes such a decision and after a decision by the USG to provide such assistance).

4.5.b Conditions at Program Initiation

Since the start of the current Task Order, much progress had been made in privatizing most government-owned enterprises, creating hundreds of viable private enterprises, and liquidating numerous others. Some 550 companies had been transferred to private ownership or liquidated. Nevertheless, the “big-ticket” enterprises in electricity, telecom, cement, and the ski resort, remained in government hands despite extensive efforts by the Privatization Agency of Kosovo and its predecessor KTA to privatize them.

4.5.c Progress Under Current Program

None of the “big-ticket” items have been transferred to private ownership, and one can only speculate whether any or all of them can be privatized during the remainder of the project. It seems clear that political factors well beyond the control of USAID/BearingPoint are likely to determine the future direction of these enterprises.

On the other hand, progress on the concessioning of the Pristina airport has proceeded satisfactorily, with USAID/BearingPoint intervening at times to keep progress on track. Rather than treating this concession as a “one-off” transaction, as stipulated in Task Order 6, the airport concession was considered by USAID as a model for a potential series of PPP transactions under the direction of a unit in the Ministry of Finance and Economy created for this purpose.

A number of important steps have been taken under the program. A consensus has been achieved on the process for concessioning the Pristina airport. A civil aviation law drafted with substantial support from USAID/BearingPoint has been approved, which a European Union report has described as a model for other countries in the region. A PPP law, again drafted with strong USAID/BearingPoint input, is expected to be passed by the Assembly in April 2009. While supporting PPP, the law also requires government budgets identify the possible contingent liabilities that could flow from PPP contracts.

The small PPP unit in the MFE is staffed competently, although the tasks it may face in the future will be demanding. This unit has great potential for attracting outside investment of hundreds of millions of dollars for infrastructure in Kosovo, but its current staffing of four professionals is clearly insufficient for the expansive PPP program envisioned by some government ministers. Also, it cannot be expected to address the myriad technical issues – to say nothing of the issues likely to be raised by politically connected concessionaires – without external support for at least several years into the future.

The concessioning of the Pristina airport is maintaining forward movement. A reputable company was selected as a transaction advisor by the Kosovar government in February, and is expected to produce a report outlining the various options for concessioning the airport in May 2009. It is expected that any concessionaire would be required to construct a new airport terminal, as the current one is inadequate and

there is a need to undertake some additional works to address smaller problems. The transaction advisor expects that the concession, if properly constructed, will generate considerable investor interest. Unless the process is delayed by political factors, the Pristina airport should be concessioned before the end of Task Order 6.

The USAID/BearingPoint long-term advisor for the Pristina Airport and for PPP is held in high regard by the Kosovar government officials whom she assists. Her extensive experience in PPP work, including airports, makes her a valuable asset for completion of the airport concession, and for PPP generally.

For the four results expected by USAID from this activity, the assessment of progress is as follows:

- | | |
|-------------------|---|
| Result 1 | Pristina International Airport is operating under a concession. |
| <i>Assessment</i> | Not achieved but on track for completion by June 2010, when the current task order ends. There are many possible sources of delay, but the Kosovar authorities and EMSG Program advisors have given great care to minimizing such obstacles. Nevertheless, it is possible that the global financial crisis may delay the award process. |
| Result 2 | Relevant legislation relating to the transfer of POEs and civil aviation pursuant to the settlement document is enacted. |
| <i>Assessment</i> | Partially achieved. As mentioned above, Kosovo has enacted a model civil aviation law. Nevertheless, no agreement has been reached with Serbia that would allow commercial aircraft traveling to or from Kosovo to pass through Serbian airspace. |
| Result 3 | Government has policies and strategies for POEs. |
| <i>Assessment</i> | Partially achieved, but partly beyond the contractor's manageable control. The Government of Kosovo has taken steps in this direction, but more remains to be done. The USAID contractor has little capacity to influence the ultimate outcome, as it depends on political considerations, international negotiations, and high-level Kosovar government decisions. |
| Result 4 | Another POE, such as PTK, is commercialized or is being prepared for commercialization (if the government takes such a decision and after a decision by the USG to provide such assistance). |
| <i>Assessment</i> | Unclear. This result as a measurement of contractor performance is so limited by "if's and after's" as to be bereft of value as a performance indicator. At mid-term, it is not evaluable. |

4.5.d Recommended Next Steps

Despite the high quality of the assistance being provided for the Pristina airport concession and for PPP more generally, it is clear that the need for USAID assistance is required to continue several years beyond the end of the current task order in June 2010 to reach USAID's goals. Even between now and the end of the task order, additional support, at least in the form of short-term advisors at key points in the airport concessioning process, is probably warranted, depending on how the process unfolds.

While PPP arrangements are simple in concept, they are extremely difficult in practice. The problem lies in the long-term nature of the relationship. It is not enough that the current government of Kosovo strongly embrace agreements made with a concessionaire; subsequent governments must also honor those commitments. For USAID to commit substantial resources to this activity, it would be important to gain

an indication from the principal opposition political party that it considers PPP to be in the national interest, and not just the whim of a particular government.

Governments managing PPP arrangements need to appreciate the potential issues in enforcing performance by the concessionaire. The government needs to have the monitoring capacity and authority to require that the concessionaire to fulfill the terms of the agreement. Concessionaires in some other countries have managed to use political influence and rhetoric to prevent proper oversight of their commitments.

With the expected passage of a PPP law in early April, there appears to be the potential for an explosive increase in demand, particularly from municipalities, for PPP arrangements. Acceding to this demand would be a mistake since the government needs to proceed slowly and deliberately because a single scandal about a concession could taint the entire effort. The MFE PPP unit needs to exercise great caution in proceeding with large numbers of PPP actions.

The only straightforward situation for PPP is one in which there is a long history of such arrangements, with substantial experience. In practice, this means that the concessionaire can expect the legal system to be strong enough to prevent the government from unilaterally changing the terms of the concession; that government oversight is sufficiently professional and above political influence to assure that the concessionaire fulfills the commitments made in the agreement; and that disagreements between the government and the concessionaire can be expected to be adjudicated fairly in the courts.

Clearly, Kosovo does not enjoy the country conditions that would make PPP easy. In this situation, trust by potential concessionaires must come from other sources. In the case of Kosovo, there are two:

1. First, the expectation that USAID would continue to support PPP for a substantial period into the future, acting as an honest broker between concessionaires and the government – this would make a valuable contribution to increasing the level of trust between the two parties to the agreement.
2. Second, a clear commitment on the part of the government to a steady stream of future PPP concessions that would provide comfort to investors in the early PPP concessions – failure of the government to be perceived as treating the initial concessionaires fairly would be likely to dissuade serious investors from bidding on subsequent PPP concessions.

The importance of this second factor is limited by the fact that changes in government in a young country like Kosovo are problematic. Popular resentment of an early concession could lead a new government to believe that further PPP projects would be unpopular, so it might unilaterally revise the terms of the existing concessions in favor of the government.

In sum, it is the expected support of the US government over the near term – at least the first four or five years of the initial concessions – that is likely to provide the primary source of confidence for foreign investors to undertake PPP activities in Kosovo.

1. Proper support for PPP will require another four or five years of USAID involvement. As discussed above, there is no substitute for USAID involvement as an “honest broker” in complex and long-term arrangements. Still, the hundreds of millions of dollars of potential international investment in Kosovo’s infrastructure are likely to make this a high-payoff activity for USAID.
2. At present, the success of the Pristina Airport concession is the key to future PPP effectiveness in Kosovo. USAID should be prepared to offer short-term assistance for the concession at key stages of the process to ensure its success.

5. Final Observations and General Recommendations

The EMSG Program is widely believed by those who know it best to have been effective in the period since June 2007, and our observations regarding progress in each area examined generally confirm this belief. Senior people interviewed in the Government, without exception, praise the efforts of specific USAID/BearingPoint advisors with whom they have regular contact. They also often express a desire for more similar assistance in the future.

Our evaluation tends to validate the long-term resident advisor model followed by the EMSG Program. This model contrasts with that used by some other projects, whose work is less directly integrated on a daily basis with that of the government offices and functions they support. As a result of their proximity and intimacy with the work, EMSG Program advisors have multiple opportunities both to advise on real-time decisions and to directly transfer their knowledge – both theoretical and practical – to the government employees working alongside them in their offices.

The EMSG Program is one in a series in which USAID/BearingPoint has supported a range of technical assistance across a number of ministries and other budget organizations, including those at the municipal level. The scope of the project and close communication among the advisors has increased the project's overall effectiveness. By sharing insights and coordinating communications with the government, the project team has multiplied its effectiveness in ways that narrower gauge technical assistance efforts cannot. As the scope of the EMSG Program has narrowed, the risk has grown that it will lose some of the synergy that has helped define its approach to crosscutting issues.

The capacity in major governmental institutions – while it continues to increase as a result of the EMSG Program and other efforts – is fragile, because the number of internationally trained and supported public administration in senior management positions is small and merit systems for recruiting, training, and promoting professional staff are not well developed. Moreover, the core processes for managing government finances – including budgeting and treasury functions – are vulnerable to political interference. If the budget process is bypassed routinely as it was in 2008 or if there should be a turnover of senior leadership in the Budget and Treasury, as there has been in Tax Administration, many of the gains in governing capacity of the past few years could be lost.

Observer opinions differ regarding whether USAID/BearingPoint advisors have drawn back sufficiently or quickly enough from outright conduct of administrative functions to coaching and supporting roles as their Kosovar counterparts have gained experience in their positions. It appears in specific instances, especially where counterparts have not been in their positions for a long time, advisors occasionally still direct activities and produce first drafts of instructions or key documents. However, these are increasingly exceptions rather than the norm.

We do not recommend major changes in direction at this point in the EMSG Program. However, in addition to recommendations above regarding specific project elements, we propose the following:

1. As the project's scope narrows, USAID should increase its efforts to draw the EMSG Program into closer collaboration with other donor-funded projects, in order to retain some of the synergies of coordinated technical assistance that have been inherent in the EMSG Program until recently. USAID's auspices and leverage can be used to convene donors supporting projects aimed at development of Budget, Treasury, Tax, and related public administration capacities. Together they can pursue a joint strategy for sustainable performance of the core policy support functions that until recently have heavily focused on the MFE. With the shift in locus of policy making to the OPM and with the continuing downsizing of the EMSG Program – including recent or pending withdrawal of

advisors from OPM, CBK, and the Assembly – the need for an integrated approach and strategy across donor-funded projects is evident.

2. Under USAID’s guidance, the EMSG Program should work with the Government to support the implementation of the Brain Fund as originally proposed. Again, under USAID guidance, the EMSG Program should work with other international projects to develop a new, combined strategy to ensure management training that meets international standards for a sustained senior cadre of managers and technical specialists. This strategy also would contribute to the integration of this senior group into a permanent civil service structure funded through annual appropriations for salaries.
3. USAID/BearingPoint advisors should, except when asked by their counterparts, avoid any direct role in advising senior policy officials, directing staff, or producing first drafts of memoranda, instructions, or other government documents and limit their participation to the coaching of principals or, when requested by principals, the coaching or training of staff. USAID can ensure that this occurs by clarifying for senior Government officials the limits of the advisory role.
4. Finally, USAID and USAID/BearingPoint staff should initiate discussions with key Government of Kosovo officials aimed at reaching a common understanding of the reduced magnitude and more limited scope of any follow-on activity aimed at the continued strengthening of key economic institutions. Such discussions should seek to identify the highest Government priorities for continued assistance.

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Acronyms

BDMS	Budget Data's Management System
CAMEL	Bank Rating (Capital adequacy, Asset quality, Management, Earnings, Liquidity)
CBK	Central Bank of Kosovo
CAFAO	Customs and Fiscal Assistance Office of the EU
CIT	Corporate Income Tax
EMSG	Economic Management for Stability and Growth
EU	European Union
FMIS	Freebalance Management Information System
GDP	Gross Domestic Product
ICO	International Civilian Office of the EU in Kosovo
KEK	Kosovo Energy Corporation
KCA	Kosovo Chamber of Advocates
KJI	Kosovo Judicial Institute
LTU	Large Taxpayers Unit
MFE	Ministry of Finance and Economy
MTEF	Medium-term Expenditure Framework
PIP	Public Investment Program
PIT	Personal Income Tax
POE	Publicly Owned Enterprise
PPP	Public/Private Partnerships
PTK	Post and Telekom of Kosovo
SIDA	Swedish International Development Cooperation Agency
SIGTAS	Standard Integrated Government Tax Administration System
TAK	Tax Administration of Kosovo
USAID	United States Agency for International Development
USG	United States Government
VAT	Value Added Tax

Annex 1. Numbers of BearingPoint Advisors: 2001 to 2009

Position	Task Order I	Task Order II	Task Order III	Task Order IV	Task Order V	Task Order VI	Comments
Chief of Party	1	1	1	1	1	1	
MoF- Macro Economic		2	1	1	2	1	
MoF-Treasury/ Budget/Intergov	7	8	4	4	4	3	
MoF- Property Tax	1	1	1	1	1	1	Institutionalized, full time assistance withdrawn 2008
MoF- PPP/Concessions						1	New initiative
MoF- Tax Policy/Admin.	4	5	4	3	3	2	
Central Bank	6	6	5	3	3	1	Institutionalized, full time assistance withdrawn 2009
Commercial Law	3	4	5	4	4	2	Down to 1 full time, January 09
Energy		2	2	1	1	3	Down to 2 full time, February 09
Privatization	1	5	3	5	5	1	90% by value completed; full time assistance withdrawn 2008
Pension			3	2	1		Institutionalized, full time assistance withdrawn 2006
Trade							
Procurement	1		1				
Telecom			1	1	1		
Training					1	1	
Public Utilities		1	2	2			
Public Education	1	1	1	1			
Information Tech		2	1			1	
Total	25	38	36	29	25	18	

Annex 2. Interviews Conducted in Kosovo

March 2009

General

Ahmet Shala, Minister of Finance and Economy
Matthew Smith, USAID/BearingPoint COP for EMSG Program
Edgardo Ruggiero, IMF Resident Representative
Shpend Ahmeti, Executive Director, GAP Institute for Advanced Studies
Hajdar Korbi, Advisor to Minister of MFE
Doug Todd, USAID/BearingPoint Senior Economic Advisor
Vito Intini, World Bank
Mark Poston, Head of Office, DFID Kosovo
Chris Hall, President, American University in Kosovo
Freek Janmaat, EC Economic Advisor
Valerie Bilgri-Holm, Economic Officer, US Embassy, Kosovo
Robert Newsome, Political Officer, US Embassy, Kosovo

MFE Budget and Treasury

Bedri Hamza, Deputy Minister of Finance and Economy
Agim Krasniqi, Central Budget Director, MFE
Mehmet Simnica, Senior Budget Analyst, Central Budget Department, MFE
Lulzim Ismajli, Treasury Director, MFE
Liridon Mavriqi, Policy Advisor to Minister Shala
Kris Kauffman, USAID/BearingPoint Central Budget Advisor
Magda Tomczynska, USAID/BearingPoint Municipal Budget Advisor
Anne Schwartz, US Treasury
Bernard Nikaj, PIP staff (EU)
Steve Leeds, World Bank PEFA
Azem Reqica, Budget Department, MFE
Petrit Popova, Municipal Budget Director, MFE
Semra Tyrbedari, Economic Policy Department, MFE
Selim Thaqi, Economic Policy Department, MFE
Valmira Rexhebeqaj, Economic Policy Department, MFE
Sally Houstoun, PIP (EU) Team Leader
Flora Fazliu, Budget Department Coordinator with PIP
Ardiana Meholli, Economic Officer, International Civilian Office, EU Special Representative

MFE Tax Administration (including Property Tax)

Stan Beesley, USAID/BearingPoint Tax Advisor
Etienne Cosyns, USAID/BearingPoint Tax Advisor
Josh Aslett, USAID/BearingPoint Tax IT Advisor
Naim Fetahu, Director of Tax Administration of Kosovo
Chad Corson, USAID/BearingPoint Property Tax Advisor
Darlene Berthod, US Treasury
Fortuna Haxhikadija, Director of Property Tax Department, MFE
Isen Lipovica, Manager of Large Taxpayers Unit of Tax Administration of Kosovo

Central Bank of Kosovo

Noble Fenson, USAID/BearingPoint Central Bank Advisor
Hashim Rexhepi, Governor, Kosovo Central Bank

Peter Nichols, US Treasury Advisor (by phone)
Skendije Himaj Zekaj, Chief Financial Supervision Officer, Kosovo Central Bank
Edgardo Ruggiero, IMF Resident Representative
Philip Sigwart, Pro-Credit Bank, President of the Kosovo Bankers' Association

Commercial Law Development

Bill Klawonn, USAID/BearingPoint Legal Advisor
Kent McNeil, USAID/BearingPoint Training Advisor
Besim Beqaj, President, Kosova Chamber of Commerce

MFE P/P/P (including airport concession)

Jill Jamieson, USAID/BearingPoint PPP Advisor
Fatmir Limaj, Minister of Transport and Communication
Agron Mustafa, Managing Director, Pristina International Airport
Dritan Gjonbalaj, Director General, Civil Aviation Authority
Lorik Fejzhullahu, Acting Director, PPP Unit, Ministry of Finance and Economy
Kirk Adams, USAID/BearingPoint Mining Advisor
Hans Mohrmann, Pristina Airport Transaction advisor (by email)

USAID

William Lawrence
Besa Ilazi, Economic Growth Officer
Luan Gashi, Program Economist
Susan Fritz, Deputy Mission Director