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Report No: 31658-XK

PROJECT APPRAISAL DOCUMENT

ON A

PROPOSED GRANT

IN THE AMOUNT OF SDR 3.7 MILLION
(USD 5.5 MILLION EQUIVALENT)

TO THE

UNITED NATIONS INTERIM ADMINISTRATION MISSION IN KOSOVO
FOR THE BENEFIT OF KOSOVO

FOR A

PUBLIC EXPENDITURE MANAGEMENT TECHNICAL ASSISTANCE PROJECT

June 14, 2005

CURRENCY EQUIVALENTS

(Exchange Rate Effective January 11, 2005)

Currency Unit	=	Euro
€0.74	=	US$1
1.52 US$	=	SDR 1

FISCAL YEAR

January 1 – December 31

ABBREVIATIONS AND ACRONYMS

BPK	Banking and Payments Authority of Kosovo
CFA	Central Fiscal Authority
EAR	European Agency for Reconstruction
DFID	Department for International Development (UK)
FMR	Financial Monitoring Report
IDA	International Development Association
KEK	Korporata Energjetike e Kosovës (Power Corporation of Kosovo)
KCB	Kosovo Consolidated Budget
KTA	Kosovo Trust Agency
LPP	Law on Public Procurement
MFE	Ministry of Finance and Economy
MOH	Ministry of Health
MPS	Ministry of Public Services
MTC	Ministry of Transport and Communications
OED	Operations Evaluation Department
PIP	Public Investment Program
PISG	Provisional Institutions of Self Government
PEMTAG	Public Sector Expenditure Management Technical Assistance Grant
PEIR	Public Expenditure and Institutional Review
PHC	Primary Health Care
POE	Publicly Owned Enterprise
PPA	Public Procurement Agency
RID	Road Information Database
SRSG	Special Representative of the Secretary General
TSS	Transitional Support Strategy
UNMIK	United Nations Interim Administration Mission in Kosovo
USAID	United States Agency for International Development

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KOSOVO
Public Expenditure Management

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KOSOVO

PUBLIC EXPENDITURE MANAGEMENT TECHNICAL ASSISTANCE PROJECT

PROJECT APPRAISAL DOCUMENT

EUROPE AND CENTRAL ASIA

ECSPE

Date: May 13, 2005 Country Director: Orsalia Kalantzopoulos Sector Manager/Director: Deborah Wetzel	Team Leader: William R. Dillinger Sectors: Central government administration (50%); Health (25%) Transport (25%) Themes: Administrative and civil service reform (P)
Project ID: P078674	Environmental screening category: Not Required
Lending Instrument: Specific Investment Loan	Safeguard screening category:

Project Financing Data

[ ] Loan [ ] Credit [X] Grant [ ] Guarantee [ ] Other:

For Loans/Credits/Others:
Total Bank financing (US$m.): 5.50
Proposed terms:

Financing Plan (US$m)

Source	Local	Foreign	Total
BORROWER/RECIPIENT	0.65	0.00	0.00
IDA GRANT FOR POST-CONFLICT	5.50	0.00	5.50
Total:	6.15	0.00	6.15

Borrower (Recipient): United Nations Interim Administration Mission in Kosovo

Responsible Agency: Ministry of Economy and Finance, Ministry of Health, Ministry of Transport and Communications

Estimated disbursements (Bank FY/US$m)									
FY	06	07	08	09	0	0	0	0	0
Annual	1.6	2.9	0.9	0.1	0.00	0.00	0.00	0.00	0.00
Cumulative	1.6	4.5	5.4	5.5	0.00	0.00	0.00	0.00	0.00

Does the project depart from the CAS in content or other significant respects?	[ ]Yes [X] No
Does the project require any exceptions from Bank policies?	[ ]Yes [X] No
Have these been approved by Bank management?	[ ]Yes [X NA
Is approval for any policy exception sought from the Board?	[ ]Yes [X] No
Does the project include any critical risks rated "substantial" or "high"?	[ ]Yes [X] No
Does the project meet the Regional criteria for readiness for implementation?	[ ]Yes [X] No

Project development objective Strengthen Kosovo's ability to use public resources more effectively, efficiently, and transparently

Project description:
Support to Ministry of Economy and Finance and key sectoral ministries for budget formulation, budget execution, and procurement
Support to Ministry of Transport and Communications and Pristina Municipality for expenditure prioritization and traffic safety improvements
Support to Ministry of Health for introduction of family medicine model and performance based payment system in pilot municipalities.

Which safeguard policies are triggered, if any? None.

Significant, non-standard conditions. None.

Board presentation: June 14, 2005

Loan/credit effectiveness: Sept 1, 2005

Covenants applicable to project implementation: None.

A. STRATEGIC CONTEXT AND RATIONALE

1. Country and sector issues

Political and Economic Developments

1. Kosovo[1] is emerging from a post-conflict environment. At the end of the conflict, in 1999, United Nations Security Council (UNSC) Resolution 1244 authorized the establishment of the United Nations Interim Administration Mission in Kosovo (UNMIK) as the interim administration of Kosovo, to be replaced over time with local institutions. The presence of a large NATO-led international force (KFOR) has provided security. GDP, after falling an estimated 20 percent as a result of the 1998-99 conflict, has begun to grow at an average of 3 percent per annum.[2] But the situation remains precarious. The issue of Kosovo's final status remains unresolved. Government institutions are weak. And recent economic growth has been driven by donor support, which is not sustainable and already beginning to fall.

2. The governance structure in Kosovo is complex. In 2001, a Constitutional Framework established the legal framework for the transfer of responsibilities to the Provisional Institutions of Self Government (PISG) comprised of a President, a 120-member Assembly, and an executive branch headed by a Prime Minister. The handover has gradually taken place since 2001. Currently PISG's responsibilities include the provision of education, health, social welfare, energy, telecommunications, and some forms of transport services. Until Kosovo's final status is determined, however, UNMIK retains control over the Banking Payments Authority of Kosovo (BPK), publicly-owned and socially-owned enterprises, customs, and ultimate responsibility for economic and fiscal matters with the power to veto decisions made by the PISG that it finds inconsistent with UNSC Resolution 1244.

3. Under a policy of 'standards before status' UNMIK and the PISG are working on a specific series of reforms aimed at strengthening democratic institutions, protecting minority rights, and establishing the basis for a market economy.[3] In mid-2005, the UN will review progress toward these standards. On that basis, the UN will decide an appropriate critical path/timing for initiating discussions on Kosovo' final status. Progress in the development of capable public sector institutions will be a critical factor in that decision.

Macroeconomic Issues

4. Since the end of the 1999 conflict, there has been a shift away from the policies of the former Socialist Federal Republic of Yugoslavia toward a liberal market policy. The former trade regime was replaced by a simple regime with no quantitative barriers and initially a single 10 percent tariff rate, followed by a subsequent two-tier tariff rate with a lower 0 percent rate on

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[1] Kosovo is currently under United Nations' interim administration pursuant to United Nations Security Council Resolution 1244 (1999) of June 10, 1999 (hereafter referred to as Kosovo).

[2] All GDP data are estimates only. Considerable progress has been made on the compilation of economic statistics but there are still large errors and omissions, difficulty in capturing informal activity, and a lack of fundamental data such as a recent census and production-based estimates of National Income Accounts.

[3] See UNMIK, "*Kosovo Standards Implementation Plan*' (March 31, 2004).

capital and intermediate goods. The use of foreign exchange was legalized for all domestic transactions, initially establishing the Deutsche Mark and later the Euro as the local currency. The Banking and Payments Authority of Kosovo was established to handle domestic payments, and, *inter alia*, licensing and supervision of the banking sector. A Ministry of Economy and Finance (MFE), with responsibility for the Kosovo Consolidated Budget (KCB), and a new tax system and administrative structure have also been established.

5. National Income Account data in Kosovo are weak and largely based on estimates of household consumption from the Household Budget Surveys and government spending from the Treasury accounts. The resulting estimates of Gross Domestic Product (GDP) are weak and are prone to considerable revisions as new data becomes available. The latest GDP data indicate that there has been a recovery of economic activity and positive growth since 2000.[4] According to IMF estimates real GDP growth, reflecting high levels of public and private investment, reached approximately 30 percent in 2001 and has since averaged around 3 percent per year. GDP per capita, at approximately US$400 in 1995, increased to around an estimated US$780 by 2001 and over US$1000 in 2003. Price stability has been achieved, with inflation rates coming down from double digits at the beginning of the decade to zero inflation in 2003. Despite the slow-down in the post-conflict reconstruction boom, private sector activity continues to show signs of recovery, with construction activity exhibiting considerable strength and banking credit more than doubling in each of the last three years.

6. The external financial position has also improved markedly since 2000. The current account deficit (before foreign assistance) has fallen dramatically in the last three years from almost 80 percent of GDP to 50 percent of GDP in 2004, primarily due to an improvement in the merchandise trade balance and as a result of a contraction in imports.[5] The external situation is still far from sustainable: the trade deficit in 2004 was about 50 percent of GDP[6]. Regular exports have been growing rapidly in the last four years, but from a very low base: merchandise exports are currently only about 5 to 8 percent of imports.

7. Prospects for economic growth depend upon the success of two inter-dependent overarching factors: (i) implementation of a policy program that promotes private sector-led growth, including completion of the reconstruction effort and export promotion, within a sustainable macroeconomic framework which will require fiscal prudence; and (ii) a resolution of Kosovo's political status and the maintenance of peace and security in the region.

8. The key public expenditure management problem facing the PISG is to maintain fiscal balance in the face of declining donor receipts while improving the quantity and quality of essential public services. To accomplish this, weak systems of budget formulation, budget execution, auditing, and procurement need to be strengthened. Institutional arrangements for

[4] Estimates of macroeconomic data are based on the IMF and Kosovar authorities estimates concluded in November 2004. The next revision is due following the IMF mission planned for April 2005. In the past, these revisions have resulted not only in new current estimates and future projections, but also to changes to historic estimates.

[5] It should be noted that there is also considerable uncertainty regarding the accuracy of balance of payments estimates. Error and omissions have been growing in size and accounted for 49 percent of the current account deficit in 2003. Given stepped up efforts to stem smuggling, however, it is unlikely that unrecorded trade flows fully explain accounting discrepancies. The export amounts, in fact, include an allowance for smuggling.

[6] The official trade balance includes sales to expatriates as exports.

fiscal responsibility that are currently 'shared' between UNMIK and the PISG must be improved. To attract and retain high caliber staff, the public sector needs to reform the terms of public sector employment. Specific sectoral reforms are also urgent. In the health sector, spending must shift toward primary care. Mechanisms for allocating resources to health care providers must be improved. In the road sector, road user charge policies must be revised and mechanisms for prioritizing and allocating expenditures on road construction and maintenance, strengthened.

2. Rationale for Bank involvement

9. A number of donors are already providing technical assistance to the PISG in Kosovo. USAID is providing extensive support to the Ministry of Economy and Finance (MFE) particularly for macroeconomic forecasting, budget formulation, and treasury operations. The EU, through the European Agency for Reconstruction (EAR), is financing major programs of technical assistance in public investment planning, internal audit, and procurement. But efforts to improve public expenditure management have largely been confined to the MFE. They have yet to extend to the sectoral ministries. Moreover, little attention has been directed to policy and procedural reforms in key sectoral ministries, which are essential to overall improvement in public sector management. These are areas where the Bank has a clear comparative advantage. They would be the focus on the Public Expenditure Management Technical Assistance Grant (PEMTAG).

3. Higher level objectives to which the project contributes

10. The proposed operation contributes to a key objective identified in the recent Transitional Support Strategy (TSS) for Kosovo (April, 2004): building capacity to strengthen economic and public expenditure management. The project's budget analysis and treasury subcomponents will improve expenditure management in the MFE. Its budget formulation and procurement subcomponents will improve expenditure management in key sectoral ministries. The project's health component will demonstrate a more cost-effective means of providing primary health care coupled with testing a new performance-based provider payment mechanism. Its transport subcomponent will increase the effectiveness of spending in the roads sector.

B. PROJECT DESCRIPTION

1. Lending instrument

11. The proposed project would be structured as an International Development Association (IDA) Grant. IDA grants to international organizations are permitted under the Association's Article of Agreement. Kosovo is not a member of the Bank Group, and is therefore not eligible to borrow from the Association. In accordance with the recently approved TSS, the project is proposed to be funded through an IDA Grant which will be provided to UNMIK (the Recipient) for the benefit of Kosovo.

Project development objectives and key indicators

12. The project's development objective is to improve the PISG's ability to use public resources more effectively, efficiently and transparently through strengthened public expenditure

management. The project's impact on budget formulation in key sectoral ministries will be measured by comparing the budget priorities of UNMIK and the PISG, as indicated in the MFE's initial budget circular, to the subsequent budget submissions of the sectoral ministries. Its impact on procurement will be measured by counting the number of external audit findings of material violations of procurement rules. The project's impact on healthcare will be measured by the number of patients registered with family medicine practitioners and the proportion of medical workers' income derived from incentive payments in the demonstration municipalities. Its impact on road management will be measured by counting the number of staff trained in the use of expenditure prioritization software and the number of traffic counters installed. (The latter provide the detailed data necessary to prioritize spending on roads.)

2. Project components

13. The project has three major components. The first addresses cross-cutting problems in public expenditure management: budget formulation, budget execution, and procurement, focusing particularly on high-spending ministries. The remaining components support policy and procedural reforms in two key sectors. One of these is healthcare where the combined effects of neglect, ethnic conflicts, and chaos after the break up of the former Yugoslavia have left Kosovo with some of the worst health conditions in Europe.[7] The other is transport, which has emerged as a key to Kosovo's economic integration with the rest of Europe.

Table 1 Summary of Project Costs by Component

Component	US$ million	Percent
Cross-cutting public sector management	2.435	40%
Health	1.261	21%
Transport*	2.165	35%
Subtotal	5.861	95%
Project Management	.150	2%
Contingencies	.139	2%
Total	6.150	100%

*Including $650,000 in counterpart financing

14. As shown in Table 1, cross cutting public expenditure management reforms account for 40 percent of total project costs. Technical assistance to the health and transport sectors account for a further 21 percent and 35 percent of grant resources respectively.

Public Expenditure Management

15. The public expenditure management component of the project consists of three subcomponents: budget formulation, budget execution, and public procurement. Each subcomponent has been designed to complement large-scale ongoing programs supported by other donors, particularly EAR and USAID. As a result, few of the sub-components are free-standing. While other donors have welcomed Bank engagement in these areas, close coordination will be crucial. Table 2 demonstrates how World Bank assistance will complement the work of other donors.

7 Infant Mortality Rates (IMR) are variably estimated at 18-25-35 per 1000, well above average for lower middle-income countries and Kosovo also exhibits one of the lowest percentages of ante-natal care in pregnant women, and in births attended by a professional.

Table 2: Public Expenditure Management: World Bank and Other Donor Activities:		
	Focus of Intervention	
Component	World Bank (PEMTAG)	Other Donors
Budget Formulation	Sectoral budget analysis in MFE, budget formulation in line ministries (Health, Transport and Communications and Labor and Social Welfare)	USAID: Macroeconomic forecasting, aggregate budget formulation in MFE; budget formulation in selected municipalities EAR: preparation of public investment program
Budget Execution	Cash management; bookkeeping, accounting and financial reporting procedures	USAID, SIDA, CIDA: rollout of electronic commitment and payment components to sectoral ministries
Public Procurement	One-on-one procurement training in line ministries	EAR: redrafting of law on public procurement, drafting of implementing regulations, website publication of procurement operations
Internal Audit		EAR: development of audit policy paper, and guidelines, auditor training
Public employment		EAR: Job classification and wage decompression

17. *Budget Formulation.* While substantial support is being provided by international advisers to the central institutions involved in the budget process (including particularly the MFE) the quality of budget submissions prepared by line agencies is poor. Submissions are well outside initial ceilings provided by the MFE and are unrelated to agreed policies and priorities. Within the MFE, the budget department lacks the capacity to analyze and challenge budget users' proposals in any depth. This component of the project would focus on two major areas of budget formulation. The first would be a consultancy and training program to build capacity in budget preparation in the Ministry of Health, Ministry of Transport and Communications and Ministry of Labor and Social Welfare. The second would focus on building capacity among the budget analysts in the Ministry of Finance, including the counterparts of the same major line ministries. Both tasks would be carried out by long-term and local consultants with specific knowledge in these fields as well as in budget preparation and analysis.

18. *Budget Execution.* With the recent decline in Kosovo's cash reserves and its shift to cash-based appropriations, cash management skills have become increasingly necessary. This component would finance technical support to the PISG's fledgling cash management unit. Assistance is also required to improve the quality of financial information produced by the line ministries. The project would therefore finance the drafting of a set of comprehensive written procedures for bookkeeping, accounting and financial reporting.

19. *Procurement.* With EAR support, and on the basis of World Bank and other recommendations, the PISG will amend the recently-enacted Law on Public Procurement (LPP).

EAR is also financing the drafting of the law's implementing secondary legislation and plans to finance a series of training courses to support their implementation. But one-on-one mentoring by experienced procurement specialists will be required to ensure that the new procurement system is implemented as intended. In cooperation with the EAR, the project will therefore finance international consultants to work with local counterparts.

Health Sector Reforms

20. The transport and health ministries, as major spending entities, will be targets of assistance in budget formulation and procurement. As noted in the Kosovo Transitional Support Strategy (TSS), additional support is warranted.

21. Reforms in the health sector would focus on the introduction of the family medicine model. A major source of inefficiency in Kosovo's health care system is its reliance on queuing to ration access and its excessive use of secondary and tertiary facilities. In primary health care, no system of scheduled appointments exists. And because primary care physicians are trained in a narrow range of fields, referrals to more expensive secondary and tertiary facilities are common, imposing costs on both the health care system and on patients.

22. The PISG intends to address this problem by introducing the family medicine model of primary care. Under this approach, patients would register with an individual doctor of their choice who would become the primary point of contact in the heath care system. These doctors, in turn, receive training in a broad range of primary health care fields, limiting the need for referrals. Although the EAR and the Finnish Government have financed an extensive training program in family medicine, trainees return to their former organizational environment. As a result, the model has yet to take hold. Family doctors and nurses have the mandate but not the incentive to adopt the family medicine approach.

23. The Health Component would have three sub-components: The first sub-component would finance implementation of the family medicine model in four municipalities. It would include support to: (i) an initial review of legislation to remove any legal obstacles to the implementation of the family medicine model; (ii) technical assistance to assist municipal health departments in organizing doctors and nurses into teams and setting up systems for making appointments (micro organizational changes); (iii) the development of guidelines, protocols and standards for family medicine teams and for disease management and disease prevention for practical use in primary health care, (iv) a media campaign to inform the public about the family medicine reform and encourage patients to register with a doctor of their choice; and (v) a study tour to a country in ECA where family medicine has been implemented successfully.

24. A second sub-component would test a new system for paying providers. Although doctors and nurses would continue to be municipal employees and be paid a basic salary, a performance-based payment mechanism would be established for specific treatments in accordance with an agreed program of work for family medicine teams, providing a financial incentive to improve patient care at the primary level and reduce unnecessary referrals. This sub-component would also review relevant legislation to identify any legal obstacles to the implementation of performance-based payments. Training will be provided in the essentials of the new payment system for the Health Care Commissioning Agency, other staff, and

participating providers. In collaboration with the U.K.'s Department for International Development (DFID), the health component would also include a third sub-component to provide limited training for the Ministry of Health on management, policy development and planning, and communication skills.

Transport Sector Reforms

25. Long-standing neglect of maintenance and the conflict in 1999 have had a deleterious impact on Kosovo's road network. Road maintenance has been persistently under-funded, while funds are exhausted on new works, some of which are not economically justified. The poor road network is hampering the internal integration of Kosovo and could, potentially, isolate Kosovo from regional trade flows. Traffic congestion in the main cities and at the border crossing with FYR Macedonia is also a problem.

26. The PISG's immediate strategy for the roads sector is to rehabilitate most of the damaged parts of the road network and reduce the road maintenance backlog as soon as possible. The long-term strategy is to build institutions which will be capable of administering and managing the road network in an efficient and effective manner. To support the PISG's objectives, this component of the proposed project will contribute to improving both the management and use of public expenditure in the transport sector. It will have four sub-components.

27. *Expenditure allocation.* The first would facilitate the prioritization of recurrent and capital expenditures within the road sector and involves the provision of technical assistance to review and strengthen the current Road Information Database (RID), including the incorporation of new traffic data and road condition data, the latter collected by a bump integrator to be rented by the MTC from their own resources. This would include a review of the current responsibilities and organizational structures for the operation and management of the RID, together with training in the use of network expenditure optimization software (HDM4). To provide basic data on current traffic levels, the project would also finance the purchase of automatic traffic counters to measure traffic on the network. (Under the public sector management component of this operation, technical assistance would also be provided to strengthen the budget application process within the MTC.) This component would also produce an assessment of the current expenditure priorities on the primary and secondary road network, at a network level.

28. *Financial sustainability.* Second, the project would finance the development of a detailed action plan to implement some of the key recommendations of the recent road user charges study: first, the introduction of a general increase in fuel duty of 6 and 8 Euro cents per liter on leaded and unleaded gasoline and diesel, respectively; second, to design and implement an appropriate transit fee regime, consistent with EU requirements as manifest in, inter alia, EU Directives 1999/62/EC and COM 2003/448, to ensure that international transit traffic pay a charge that reflects the cost of their actions; and finally, to review, and recommend changes in the current scale and structure of road user charges, more generally, to ensure that the fees all vehicle classes pay covers the damage to the road infrastructure that resulted from their actions.

29. *Road safety.* Third, the project would finance: (a) technical assistance to assist in the identification of 'black spots' and appropriate remedial actions based on international best

practice; (b) a review of the recently-produced manual on road design to ensure that it is consistent with best practice on safe road design principles; (c) technical assistance for the establishment of an Inter-Ministerial Road Safety Council; (d) technical assistance to develop capacity in the area of road accident reconstruction, a skill entirely missing at present. The project would also finance the purchase of suitable software for an Accident Information System, together with establishment and training.

30. *Traffic management by Pristina Municipality.* This sub-component of the project would finance technical assistance to improve traffic management capacities and practices in the Municipality of Pristina, including junction design, traffic signals, road markings, pedestrian policy and practices, and improvements in parking policy, capacities and revenue. In addition, this component would finance a few defined high priority traffic management measures (signage and traffic signals), the purchase of appropriate software, and the collection of necessary data, to establish a tactical traffic assignment model, and a review of both current road investment plans in the area, and an assessment of the need and scope of an 'urban outreach unit' in the MTC, to disseminate best urban transport policy and practice.

3. Lessons learned and reflected in the project design

31. Recent sectoral and country reviews of World Bank assistance by the Operations Evaluation Department (OED) have concluded that support for institutional development (ID) efforts has been largely ineffective. (See OED, *Evaluating Public Sector Reform*, 2001.) It argues that such efforts to improve public management systems were compromised, *inter alia*, by a pattern of underinvesting in governance sector work (or ignoring it during project preparation), a bias toward supplying capacity inputs (such as training and equipment) before reforming governance structures, and weak coordination among donors which led to duplication and an improper sequencing of reforms.

32. These lessons are largely reflected in the project design. The public sector management components of the project were identified on the basis of extensive recent sector work, including the *Kosovo Economic Memorandum* (2004), *Operational Procurement Review* (2004), *Operational Financial Accountability Review* (2004) and the IMF's *Preliminary Findings on Budget Processes* (2004). Preparation of the PEMTAG also coincides with an ongoing Bank Public Expenditure and Institutional Review (PEIR). While the Bank has not undertaken sector work in the health or transport sectors, both components reflect extensive prior sector dialogue and close collaboration with other donors to ensure complementarities of activities. The health sector component was identified on the basis of policy dialogue in connection with the Bank-financed Education and Health Project (2000). The transport component, similarly, reflects earlier discussion in connection with the preparation and implementation of the Urgent Road Project (2000).

33. The project's technical assistance, training, and equipment financing follow from broader reforms in legislation and governance. Technical assistance for budget formulation follows the enactment of the Law on Public Financial Management and Accountability in May 2003. Training in procurement will occur only after the revisions to the 2004 procurement law and its implementing regulations are in place. The health component is aimed at improving the governance structure itself; training having already been provided by other donors. There are,

however, underlying structural issues that lie beyond the reach of this project. These include the complex budget formulation process and respective roles of UNMIK and the PISG.

34. The problem of donor coordination has been addressed by deliberately designing the project to focus on gaps in other donor assistance. Thus USAID's support for budget formulation in the Ministry of Finance will be complemented by the project's support for budget formulation in key line ministries. EAR's support for revisions in procurement legislation will be complemented by the project's mentoring program. EAR's support for family medicine training will be complemented by the project's support for the actual implementation of the family medicine PHC strategy and health financing reforms.

4. Alternatives considered and reasons for rejection

35. Previous Bank support for public sector management reforms in Kosovo has taken the form of adjustment grants. There have been three of them; each based on up-front conditionality. (A fourth, in 2002, was solely aimed at private sector development.) The Implementation and Completion Reports (ICRs) on these operations are positive. Up-front core conditions were consistently met. Most supporting legal and policy actions have also been carried out. But experience suggests that conditionality alone is not a sufficient means of addressing the fundamental capacity constraints on public sector management in Kosovo. On-the-job mentoring will be required to inculcate improvements in budget formulation and procurement in the line ministries, as well as the system for expenditure evaluation in the transport ministry. Hands-on technical assistance will be required to implement the family medicine concept in the health sector. For this reason, the project is designed as a technical assistance grant, rather than an adjustment operation.

C. IMPLEMENTATION

1. Institutional and implementation arrangements

36. Overall responsibility for each of the three components will be assigned to its respective implementing ministry: Economy and Finance, Health, and Transport and Communications. Each implementing ministry will designate a high-level representative to serve on a Project Steering Committee which will be responsible for monitoring progress on the project as a whole and for resolving inter-ministerial disputes. The Ministry of Public Services and the Ministry of Labor and Social Policy, as participants in the public sector management component of the project, will also appoint high level representatives to the steering committee. UNMIK Pillar IV will also be represented. The Committee will meet on a quarterly basis or more frequently if the need arises. The assistant to the permanent secretary of the MFE will act as the steering committee's secretariat.

37. Each of the three implementing ministries will also appoint a Project Supervisor who will be responsible for monitoring overall progress on its respective component of the project. (The ministries' representatives on the Steering Committee may serve in this capacity.) The project supervisor will be assisted by a project administrator who will be responsible for drafting terms of reference, technical specifications for goods; drawing up shortlists, participating in evaluation

committees and contract negotiations, facilitating the work of consultants, and approving payments after checking the quality and quantity of work undertaken.

38. *Procurement* will be carried out by each of the three implementing ministries, under the supervision and with the advice of the Public Procurement Agency (PPA). The PPA has agreed to provide such assistance to the line ministries. A start-up procurement consultant will be hired using project funds to assist the PPA in this regard.

39. With respect to large value consulting contracts (those requiring prior review of the Bank as specified in Annex 8) and the procurement of goods under ICB (including large value shopping), PPA will act as an internal procurement agent of the implementing ministries. Implementing ministries will be responsible for preparing draft TORs, Expression of Interest Notices, and technical specifications (in the case of goods) with the advice and supervision of PPA. Both the PPA and the implementing ministry will participate in the committee that will evaluate technical and financial proposals (and bids in case of goods). Both will also participate in contract negotiations. The PPA will draft the RFP contracts for each package. The respective implementing ministry will sign the contract and will be responsible for ensuring that the contract is implemented effectively.

40. With respect to small value consultancy contracts, the respective implementing ministry will be responsible for drafting TORs and preparing short-lists of consultants and firms and with limited assistance from the PPA to carry out the subsequent procurement activities. Ministries will also handle small value shopping contracts for goods with the advice of the PPA. Both the PPA and the ministry will participate in evaluation committees and contract negotiations. The implementing ministry will sign the contract based on standard draft to be given by the PPA and will be responsible for ensuring that the contract is implemented.

41. *Financial management* activities will be performed by the Grants Unit in the MFE, with the participation of the relevant implementing ministry. The implementing ministries will be responsible for checking the quality and quantity of work carried out against contracts, issuing payment orders, and producing disbursement documentation. The MFE/Grants Unit will approve SOEs and other disbursement documentation and submit them, through UNMIK, to the Bank.

42. The MFE will maintain a financial management system acceptable to the Bank. The project's financial statements will be audited by independent auditors acceptable to the Bank and on terms of reference acceptable to the Bank commencing with the accounts for the year ending December 31, 2006. The annual audited statements and audit report will be provided to the Bank within six months of the end of each fiscal year. The audits will need to be conducted in accordance with International Standards on Auditing (ISA) as issued by the IFAC and on terms of reference acceptable to the Bank. MFE will maintain acceptable financial management on a cash basis of accounting including additional commitment information as explained in the section above on accounting policies and procedures.

2. Monitoring and evaluation of outcomes/results

43. The project's impact on budget formulation in the sectoral ministries will be measured by comparing the budget priorities indicated in the MFE's initial budget circular, to the subsequent budget submissions of the sectoral ministries. (In the past, sectoral submissions have greatly exceeded guidelines provided in the circular.) This is clearly a crude indicator of improvements in the quality of budget formulation in the sectoral ministries and in the quality of budget analysis in the MFE. Nevertheless, an increasing match between the two sets of figures will indicate that budget users are taking the budget process seriously. The project's impact on procurement will be measured as the number of external audit findings of material violations of procurement rules. The project's impact on healthcare will be measured by counting the number of patients registered with family medicine practitioners and the proportion of medical workers' income derived from incentive payments in the pilot municipalities. Its impact on road management will be measured by counting the number of staff trained in the use of expenditure prioritization software and the number of traffic counters installed. (The latter provide the detailed data necessary to prioritize spending on roads.)

3. Sustainability

44. There is substantial evidence of broad-based political support for the sort of reforms the project would finance. As detailed in Annex 2, UNMIK and the PISG have successfully complied with public sector management reform measures supported by the Bank's Economic Assistance Grants I, II, and IV. The legislative record is also reassuring, as witnessed by the enactment of the Law on Public Financial Management and Accountability (May 2003) and the new procurement law. The PISG continues to employ a large number of external advisors in senior positions and observes their advice.

45. This support is motivated in part by strategic considerations: the widespread perception that the successful resolution of Kosovo's status will require the establishment of viable public sector institutions—an item implicit in the Contact Group's 'standards before status' policy. The PISG's recent decision to embark upon a stabilization-association agreement with the EU provides a similar impetus for reform, as does the prospect of EU accession itself.

4. Critical risks and possible controversial aspect

46. The project confronts three overarching risks. First, domestic political events and/or heightened tension over Kosovo's political status may distract the PISG, or weaken its resolve to undertake reforms. This risk is mitigated to some degree by the incentive the PISG has to continue to make progress against the Standards, so as not to jeopardize the successful resolution of Kosovo's status and its eventual accession to the EU

47. A second risk is that the impact of the project's training components will be offset by the departure of trainees. As noted earlier, the PISG does not offer competitive salaries for high level staff. This risk will be mitigated by the planned decompression of salaries and by the project-supported efforts to improve the recruitment process. Ironically, the expected withdrawal of donors from Kosovo is likely to improve staff retention, as job opportunities outside the public sector will diminish.

48. The third risk is that the advisors hired under the project will fail to provide sound policy advice or impart their knowledge successfully to permanent Kosovar staff. This has clearly been a concern in other donor-financed technical assistance in Kosovo, and elsewhere in the region. The project will reduce this risk in part by explicitly including handover provisions in terms of reference and requiring the use of local personnel. But, it must mainly be addressed by devoting sufficient Bank attention, during supervision, to the consultant recruitment process (including terms of reference, evaluation of individual candidates, and periodic evaluations of performance).

Risks	Risk Mitigation Measures	Risk Rating with Mitigation
To project development objective: to strengthen Kosovo's ability to use public resources more effectively, efficiently and transparently		
Renewal of civil unrest diverts PISG and UNMIK attention from reforms	Mitigation measures lie outside scope of project	M
To project objective: improve budget formulation, budget execution, audit, and procurement in the MFE and key sectoral ministries; improve road management; pilot reforms in health care provision		
Trained staff leave government to take jobs with donors, private sector	Encourage wage decompression; monitor recruitment and promotion to ensure that training improves career prospects	M
Consultants fail to transfer knowledge to permanent staff	Explicitly include handover provisions in terms of reference; closely monitor consultant recruitment process and ongoing work during supervision	M
To component results		
Public sector management		
Procurement law is no better than its predecessor, and/or implementing regulations are poor	Closely monitor redrafting of law during project preparation and drafting of implementing regulations during first year of implementation	M
Health care		
Staff resistance to institutional reforms	Phased implementation approach under the project on the basis of local authorities commitment to the reform.	M
Transport component		
Trained staff reassigned to other positions	MTC assurances that counterparts will remain in place throughout project implementation	L

5. Loan/credit conditions and covenants

There are no non-standard conditions for Board presentation or effectiveness.

D. APPRAISAL SUMMARY

1. Economic and financial analyses

49. The project is financed as a grant, which the recipient (UNMIK) will pass on to the Kosovo Consolidated Fund (KCF) for the purposes specified in the project documentation. To the extent that the grant replaces own-source revenues that would otherwise have been used for these purposes, it will increase the general budgetary resources of the KCF. The public sector management component may imply eventual increases in certain staff salaries, however, to prevent the departure of staff once they are trained. As the number of such positions is small, this would not have any significant fiscal implications for the KCF as a whole.

50. The fiscal situation of the KCB itself has fluctuated in recent years. Considerable progress was made in raising domestic revenues and controlling expenditures in the immediate post-conflict years. Buoyed by the introduction of new taxes and a post-conflict boom, tax revenues exceeded projections. At the same time, public spending was discouraged by certain budgetary practices.[8] As a result, budget surpluses were achieved in every year until 2004 and a cash surplus of approximately €300 million had accumulated by the beginning of 2003.

Table 2 Trends in Kosovo General Budget Finances
(% of GDP)

	2001	2002	2003	2004 Est	2005 proj
General Government revenues	21.4	30.1	32.8	32.6	30.2
General Government expenditures	15.0	23.1	30.3	39.5	35.5
Surplus/Déficit (after grants)	6.4	7.0	2.5	-6.8	-5.4

Source: IMF estimates

51. Growth in tax revenues leveled off in 2003 and 2004, while the constraints to expenditure management have largely been removed. As a result, the budget recorded a cash deficit of €130 million (6.8 percent of GDP) in 2004. The prospects for further growth in the tax base are not encouraging. Between 1999 and 2003 the international donor community spent an estimated €1.96 billion in Kosovo, while remittances from the Kosovo diaspora added another €550m per annum over this period. Since 2000, donor grants have fallen by 70 percent, and are forecast to continue to decline. As a result, over the next four years, Kosovo's medium term fiscal framework will require an absolute reduction in general government expenditures from the levels inn 2004. Beginning in 2006, the Government will have to maintain a balanced budget, using the remaining cash surplus as a liquidity buffer. The PEIR, currently under preparation (and due out in gray cover in June of this year) will assist the authorities in ensuring that fiscal policy is prudent and that the surpluses accrued to date are spent in a sustainable way, in line with short and long term priorities. The PEIR will also identify numerous contingent liabilities, as yet not explicitly included in the medium term fiscal framework.

[8] Budget managers, for example, had no incentive to meet expenditure targets as unused appropriations were routinely rolled over into the following year appropriation.

2. Technical

52. The project has been designed on the basis of extensive prior sector work, including the *Kosovo Economic Memorandum* (2004), *Operational Procurement Review* (2004), *Operational Financial Accountability Review* (2004) and the IMF's *Preliminary Findings on Budget* Processes (2004). Preparation of the project also coincides with the PEIR. The health sector component was identified on the basis of policy dialogue in connection with the Bank-financed Education and Health Project (2000). The transport component, similarly, reflects discussion in connection with the Urgent Roads Project (2000). Project design also reflects extensive consultations with PISG counterparts, donors, and consultants who have been working in Kosovo for several years. The scope of the operation has been restricted so as not to overstretch the implementation capacity of the benefiting organizations. An attempt has also been made to adjust the degree of sophistication of the reforms to current conditions and absorptive capacity.

53. The Bank's Operational Procurement Review (June 2004) identified several corrective measures to be taken by the government including the need for simplifying the Law on Public Procurement(UNMIK Regulation 2004/3 of February 9, 2004) that became effective on June 09, 2004. OPR also recommended: (a) creation of new oversight bodies Public Procurement Regulatory Commission (PPRC) and Public Procurement Agency (PPA); and (b) preparation and use of implementing regulations and Standard Bidding Document; EAR is assisting PPRC in these areas as also the training. Discussions were held during appraisal both with PPA and PPRC which have just started functioning. Substantial work remains to be done to build capacity in the PPA, the PPRC and major spending institutions to implement public procurement efficiently and cost-effectively.

3. Fiduciary

54. The financial management arrangements of the project are acceptable to the Bank. As of the date of this report, the Recipient is in compliance with its audit covenants of the existing Bank-financed project. Current project financial statements and auditing arrangements for the previous grants managed by MFE are acceptable and it has been agreed that these arrangements will be replicated for the proposed project. The annual audited project financial statements will be provided to the Bank within six months of the end of each fiscal year.

55. An Operational Financial Accountability Report was finalized in November 2004. Despite significant progress since 2001, public financial management in Kosovo suffers from fundamental weaknesses, and basic structures for financial accountability are still in their infancy. The overall legal framework for budgeting and budget management is largely compatible with internationally recognized standards, but for some aspects it appears to be too advanced for the current administration's capacity. Carry-over practices and weaknesses in capacity, organization and coordination hamper budget preparation and undermine the credibility of the budget as a policy management instrument. While treasury and cash management are well-regulated areas of public financial management, they suffer from inefficiencies. The system through which Commitment and Payment Orders flow to ensure authorization of payments is well regulated. The Treasury authorizes commitments and payments based on proposals and supporting documentation by budget organizations and municipalities. The Treasury pays from a single account in the central Banking and Payment Authority of Kosovo (BPK).

56. As with most public financial management functions, accounting is constrained by limited capacity, and financial reporting needs more realistic requirements and statutory deadlines, improved procedures, and trained personnel. Internal control and internal audit at all levels of government are in their infancy. Considerable time and effort will be required to make them fully operational. External audit is undeveloped and, as with internal audit, it will need sustained external support for its development. Specific procedures have been developed by MFE to secure proper financial accountability of this project.

4. Social

57. The project takes place in the context of Kosovo's uncertain political status and ethnic tensions. Improvements in public sector management are perceived to be helpful to a successful conclusion to the status negotiations. However, prolonged uncertainty carries the risk that ethnic tensions could spill over, distracting the PISG from the reform agenda.

58. The political economy of the proposed reforms is typical of governance reforms in general: the benefits will be diffused among the general population while the costs will be concentrated on the relatively few who exploit the weaknesses in the existing system. The procurement reforms, in particular, should lower the costs and improve the quality of public services, by increasing competition and reducing fraud. But those who benefit from corruption will suffer. Although winners will clearly outnumber losers under the reforms, the latter are more likely to mobilize politically.

59. Reforms in the health sector may also encounter resistance from older, less entrepreneurial medical staff, who may resist retraining in family medicine and the increased use of output based measures as a means of determining compensation.

5. Environment

60. The project focuses on management reforms in public administration, along with procedural reforms in the Ministries of Health and Transport and Communications. It has no direct environmental impact. The project does not include any major physical rehabilitation or civil works. The project is therefore rated as 'C'.

6. Safeguard policies

61. The project triggers no safeguard policies.

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment (OP/BP/GP 4.01)	[ ]	[X]
Natural Habitats (OP/BP 4.04)	[ ]	[X]
Pest Management (OP 4.09)	[ ]	[X]
Cultural Property (OPN 11.03, being revised as OP 4.11)	[ ]	[X]
Involuntary Resettlement (OP/BP 4.12)	[ ]	[X]
Indigenous Peoples (OD 4.20, being revised as OP 4.10)	[ ]	[X]
Forests (OP/BP 4.36)	[ ]	[X]
Safety of Dams (OP/BP 4.37)	[ ]	[X]
Projects in Disputed Areas (OP/BP/GP 7.60)*	[ ]	[X]
Projects on International Waterways (OP/BP/GP 7.50)	[ ]	[X]

7. Policy Exceptions and Readiness

62. This project complies with all applicable Bank policies and no exceptions are requested. TORs for the majority of consulting assignments have been prepared (see annexes). Project supervisors and administrators have been appointed. Financial management and procurement arrangements have been agreed upon and are specified in the Project Implementation Manual.

* *By supporting the proposed project, the Bank does not intend to prejudice the final determination of the parties' claims on the disputed areas.*

Annex 1: Country and Sector or Program Background

1. Kosovo is now emerging from a post-conflict environment. In 1999, UN Resolution 1244 authorized the establishment of the United Nations Interim Administration Mission in Kosovo (UNMIK) to provide an interim administration. The presence of a large NATO-led international force (KFOR) has provided security. GDP, after falling 20 percent as a result of the 1998-99 conflict, has begun to grow. But the situation is precarious. There is no resolution of Kosovo's final status. Government institutions are weak. And recent economic growth has been driven by donor support and remittances. Both exogenous factors, these external finance flows have financed domestic consumption and supported the economy since the end of the conflict. The large current account deficit implies real sector adjustments should there be a sudden or drastic fall in either private inflows or foreign assistance.

Table 3 Kosovo: Selected Indicators, 2001-05

	2001	2002	2003	2004 est	2005 proj
GDP (€ m)	1625	1735	1797	1895	1999
GDP per capita (€ m)	870	913	930	964	1000
GNDI per capita (€ m)	1086	1119	1118	1143	1171
Real GDP growth rate (%)		1.2	3.1	3.2	1.7
Consumer price index (%)	11.7	3.6	1.0	1.5	2.0
In percent of GDP					
General Government revenues	21.4	30.1	32.8	32.6	30.2
General Government expenditures	15.0	23.1	30.3	39.5	35.5
Surplus/Deficit (including grants)	6.4	7.0	2.5	-6.8	-5.4
Current account balance before foreign assistance	-79.1	-63.6	-56.5	-50.0	-42.1
Current account balance	-8.6	-11.6	-15.8	-17.1	-23.6

Source: IMF estimates

2. The governance structure in Kosovo is complex. In 2001, a Constitutional Framework established the legal framework for the transfer of responsibilities to the Provisional Institutions of Self Government (PISG) comprised of a President, a 120-member Assembly, and an executive branch headed by a Prime Minister. The handover has gradually taken place since 2001. Currently PISG's responsibilities include the provision of education, health, social welfare, energy, telecommunications, and some forms of transport services. Currently, under UNSC Resolution 1244 and the Constitutional Framework, UNMIK is responsible for, *inter alia*, the Banking Payments Authority of Kosovo (BPK), the administration and oversight of publicly-owned and socially-owned enterprises, customs, and bears ultimate responsibility for economic and fiscal matters.

3. Under a policy of 'standards before status' UNMIK and the PISG are working on a specific series of reforms aimed at strengthening democratic institutions, protecting minority rights, and establishing the basis for a market economy.[9] In mid- 2005, the UN will review

[9] See "*Kosovo Standards Implementation Plan*' (March 31, 2004).

progress toward these standards. On that basis, the UN will decide when and if discussions will start on Kosovo' final status. Progress in the development of the legal and regulatory framework and capable public sector institutions will be a critical factor in that decision.

4. The key public expenditure management problem facing the PISG is to maintain fiscal balance in the face of declining donor receipts while improving the quantity and quality of essential public services. To accomplish this, weak systems of budget formulation, budget execution, auditing, and procurement need to be strengthened. Institutional arrangements for fiscal responsibility that are currently 'shared' between UNMIK and the PISG must be improved. To attract and retain high caliber staff, the public sector needs to reform the terms of public sector employment. Specific sectoral reforms are also urgent. In the health sector, spending must shift toward primary care. Mechanisms for health financing and allocating resources to health care providers must be reformed. In the road sector, the mechanisms for prioritizing and allocating expenditures, and capacity to manage the sector more generally, need considerable strengthening.

5. *Budget formulation.* The overall legal framework for budgeting and budget management is largely compatible with internationally recognized standards. Substantial progress has been made in institutionalizing the budget process specified in the recent Law on Public Financial Management and Accountability, although in some respects it appears to be too complex for the current administration's capacity. One of the principal problems has been the practice of budgeting on a commitment basis so that funds for multi-year activities were fully appropriated in advance. The result has been the accumulation of a pool of unused, although largely committed, funds amounting to about €171 million. One of the main advances during 2004 and for the 2005 budget process has been to move to an annual cash budget, which will provide a more accurate view of Kosovo's fiscal situation.

6. While substantial support is being provided by international advisers to the central institutions involved in the budget process (including particularly the MFE), the quality of budget submissions prepared by line agencies is poor. Submissions are well outside initial ceilings provided by the MFE. (Initial submissions for 2005 exceeded €1 billion, despite an overall resource ceiling of €600 million.) Submissions of line ministries are largely based on previous years' submissions and are not linked to sectoral priorities and policies. The problem is compounded by the previous practice of multi-year appropriations which has generated a sense of entitlement to resources which will no longer be available.

7. Within the MFE, the budget department lacks the capacity to analyze and challenge budget users' proposals in any depth. Until 2003, the number of budget analysts was extremely small. The department administration was heavily reliant on external assistance funded by a USAID technical assistance project. Although 15 new staff were recruited in 2003, they have had to be trained from scratch. This weakness is particularly acute in the case of the MFE's capacity to analyze the Kosovo Trust Agency's requests for transfers to publicly-owned enterprises (POE) of which the most important is the energy utility (KEK). In 2003 and 2004, subsidies to the POEs under the KTA amounted to €97 million and €93 million respectively, out of total General Government expenditure of €544 million in 2003 and €748 million in 2004. While there is a clear need to improve the analytic capability of the Budget Department in all sectors, the need is

particularly great in the case the largest spending ministries, particularly health, transport and labor and social protection.

8. Fundamental structural problems in the budget formulation process also exist. The distinct roles of the PISG and the UNMIK complicate the budget process. Although the PISG is responsible for budget formulation, the SRSG (Special Representative of the Secretary General) has the ultimate authority to approve the budget and as such constitutes a 'court of appeal' over the government for budget organizations that are unhappy with their appropriations. This is most notable in the case of the publicly owned enterprises under the KTA. Donor financed capital works are also excluded from the budget, particularly at the preparation stage. The result is that decisions on Public Investment Program (PIP) and non-PIP capital spending are taken separately, and are thus less likely to be consistent with sectoral and overall government priorities. While the PEMTAG cannot address these issue directly, solutions to this problem will be proposed under the ongoing Public Expenditure and Institutional Review.

9. *Budget execution.* Budget execution, performed by the Treasury Department, is relatively efficient and transparent. Once the budget has been appropriated and signed by the SRSG, line item appropriations are entered into the system. Treasury then allocates quarterly spending limits for all appropriations. Budget organizations can commit and spend funds up to the amount of the allocation. The Treasury pays from a single account in the central Banking and Payment Authority of Kosovo (BPK). Procedures for bookkeeping, accounting and financial reporting are not codified, however. Even the central Treasury lacks a manual of procedures specifying many of the processes and controls that are currently in place.

10. The Treasury uses a software system (Freebalance) to record commitments and payment orders. While municipalities are able to enter data on the system, line ministries are not. Instead, they are required to submit paper copies of commitments and payment orders, which are then entered into the system at Treasury. This delays budget execution. Until recently, budget execution was also slowed by the absence of an electronic link between the Treasury system and the Banking and Payments Authority of Kosovo (BPK). Improvements are in train. In late 2004, payment orders began to be transferred from the Treasury to BPK on CDs. (A direct electronic link is in the works.) The Treasury is now in the process of extending the electronic payment and commitment components of the software system to the line ministries. A time bound plan to this effect was prepared and presented to the PISG in December, 2004. Technical assistance in the use of the software will be provided by the Canadian and Swedish governments, which have been working with the Treasury Department in parallel with the USAID contractor.

11. Until now the existence of a considerable surplus of funds and the pattern of under spending by sectoral ministries has meant that the cash management function was not critical. (Although, as noted earlier, this surplus was partly illusory, as it included cash committed to multi-year projects.) With the shift to cash based annual appropriations and a fiscally constrained environment, cash management skills will become essential.

12. *Procurement.* A new Law on Public Procurement (LPP) was promulgated as UNMIK Regulation 2004/3 of February 9, 2004. It addressed many of the flaws in the prior legislation (Finance Administration Instruction 2/99). In particular, it established open tendering as the main procedure for awarding public contracts and imposes controls over the use of other, less

competitive procedures. The new LPP also provided for a number of valuable safeguards, which were designed to make abuses of the procurement procedures more difficult, to improve transparency in decision-making related to procurement and to ensure that more than one pair of eyes review transactions in which competition may be restricted to a limited number of bidders. The Bank, however, has expressed its concern over the complexity of the law and, in particular, its call for three separate enforcement agencies: a public procurement regulatory board, a regulatory authority, and a rules committee. In light of the Bank's and other comments, the Government is expected to amend the law. An EAR-financed consultant is now in the final stages of drafting the amendments. EAR is also financing the drafting of the law's implementing secondary legislation and intends to finance a training program to support their implementation. The latter would consist of a series of periodic training courses for staff of the major line ministries, along with the development of a procurement training module in the Kosovo Institute of Public Administration.

13. To improve transparency and accountability in procurement, Kosovo needs a management information system to collect and publish information on public procurement. This could include automated systems for communicating procurement information between the contracting authorities and key executive and oversight bodies, a public procurement website for publication of legislation, regulations, standard forms, invitations to bids, contract award notices, as well as comprehensive information on public procurement operations and performance measurement statistics. At present, the public procurement agency has a website (www.ks-gov.net/prokurimi) which contains the procurement law and a very small number of invitations to bid and notices of contract awards. It falls far short of the public procurement website envisaged in the Bank's recent Operational Procurement Review. EAR has agreed to fund the technical assistance required to upgrade the system.

14. *Audit.* Internal control, including internal audit is underdeveloped in Kosovo's public sector. There is a lack of comprehensive written procedures for financial management and control processes. Basic control activities, such as reconciliation of accounting and transaction data from different sources, are not performed. The central internal audit function was transferred from the Central Fiscal Authority of UNMIK to the MFE in 2002. Most of the staff (totaling some 25 staff) in the department have only received very basic training in internal audit. Another 75 staff are employed as internal auditors in other ministries and in the municipalities. A few of these auditors have produced reports on their individual institutions. The audits performed are focused on compliance aspects and the checking of certain types of transactions. Both the EU and the IMF have recommended that the Government give high priority to the development of internal financial control in all budgetary institutions, along with appropriate capacity building.

15. The EAR is currently financing a €1.9 million project aimed at strengthening public internal financial control and internal auditing throughout the MFE and other PISG institutions including ministries. The project, which is still at its inception stage, will run over a period of 24 months and consists of two components. The first, focused on internal control, will provide for training and the development of a strategy and regulatory framework for internal control. The second, focused on internal audit, will provide training for internal auditors and managers.

16. External audit of the Kosovo consolidated budget is currently outsourced to the Netherlands's Court of Audit, which undertook the audits for 2002 and 2003. An Auditor

General's Office was established by UNMIK Regulation 2002/18 "On the Establishment of the Office of the Auditor General of Kosovo and the Audit Office of Kosovo" of October 4, 2002, and an Auditor General has recently been appointed, along with a deputy and twenty local trainees. The plan is to recruit another 40 trainees in 2004 and 2005. Funding for the development of the OAG's audit capacity will be provided from a € 2.8 million EAR-financed grant over a period of 44 months.

17. *Public Employment* The PISG's ability to improve performance in public expenditure management--and to prepare for the phase out of external assistance--is constrained by the difficulty of recruiting and retaining highly skilled local staff. This is in part due to compressed pay scales within the public sector. It is also due to competition for skilled employees from the numerous international organizations present in Kosovo. Slapdash enforcement of the recruiting procedures specified in the civil service law has resulted in some positions being filled by under-qualified staff. A significant part of the wage bill is said to be wasted on overstaffing, particularly in the municipalities and in support positions in the health ministry. While the PISG's ability to add staff and increase salaries is subject to severe resource constraints, it is evident that it could do better.

18. One avenue for improvement is wage decompression. At present, salaries in senior technical positions are only about one-fifth of those in equivalent donor-financed positions. A recent EAR-funded review of the pay and grading system recommended a substantial increase in the spread between wages in senior positions and those at lower levels. This would allow the PISG to increase top-level wages at a relatively modest cost. (It is estimated that the recommended strategy would raise the wage bill by about 6-7 percent.) Implementation of the new system requires the matching of all staff from their existing positions to the appropriate new grade and pay range. An initial round of matching was undertaken in late 2004, but resulted in a large number of irregularities. (Each ministry was permitted to grade its own staff, resulting in some cases, in a high degree of grade inflation.) The PISG initially expected to introduce the new pay and grading system on January 1, 2005. Unexpectedly poor fiscal results from 2004 and a recognition that the review process was not carried out effectively have since prompted the Government to postpone the date. It is now scheduled to be introduced on July 1, 2005.

19. At the same time, the PISG could improve its staffing and recruitment procedures. Although the civil service law lays out a procedure for creating new positions and for recruiting staff, it appears that it is observed in the breach, particularly in municipalities. To add positions, line ministries simply include funding for new positions in their annual budget requests. If sufficient funding is available, they can proceed. Municipalities require no prior authorization, as long as the positions are funded in their budgets. (At its outset, UNMIK did set a cap on employment for each budgetary organization, but is not a binding constraint—reportedly because the cap is high. A temporary freeze on new hiring was imposed in 2003, but only to free up resources to finance a 20 percent wage increase. The freeze is no longer in effect.) For 2005, stricter procedures including clear authorizations for recruitment by the Ministry of Public Services and the Ministry of Economy and Finance, have been approved.

20. Ultimately, Kosovo cannot afford to offer competitive salaries unless it reduces overstaffing. This is a considerably more ambitious task, requiring a ministry-by-ministry functional review and analysis of staffing needs. EAR estimates that this would cost €3.5

million. It would also require a program of layoffs and early retirements. This would be politically difficult, particularly in an environment in which unemployment is already high. While the MFE is nominally committed to a rationalization of staffing levels, the broader political consensus required to successfully carry one out does not exist. The PEMTAG therefore includes no funding for such an activity.

21. *Health Sector.* Kosovo inherited a system of publicly financed universal health care from the former Yugoslav regime. This has now crumbled under the combined effects of neglect, ethnic disagreements, and chaos after the break up of the former Yugoslavia. A major source of inefficiency in Kosovo's health care system is its reliance on queuing to ration access and its excessive use of secondary and tertiary facilities. No system of scheduled appointments exists. Because primary care physicians are trained in a narrow range of fields, referrals to more expensive secondary and tertiary facilities are common, imposing costs on both the health care system and on patients.

22. The current health financing system, by the same token, provides no incentives for improved performance. The current flow of public health funds includes two types of disbursements. Funding for secondary and tertiary care is provided directly by the MOH to individual facilities on the basis of inputs (salaries, equipment and supplies, etc.) Funding for primary health care (PHC) is disbursed to the municipalities, where the Director of Health Care, in collaboration with PHC providers, is responsible for health care provision. In principle, a health allocation commission[10] defines the annual PHC allocation to municipalities based on population size, a "fair share financing" rule to ensure adequate financing of minority communities, territorial characteristics, and the number of health facilities in the form of a specific health financing grant. In reality, the final amounts are negotiated between the municipalities and the MFE on the basis of existing facilities and staff and historical input costs. As a result, neither primary or secondary care providers have an incentive to increase efficiency or expand provision.

23. The Government intends to address these problems by introducing the family medicine model of primary care. Under this approach, patients are encouraged to register with an individual doctor of their choice who becomes the primary point of contact in the heath care system. These doctors, in turn, receive training in a broad range of primary health care fields, limiting the need for referrals. With support from the EAR and the Finnish Government, over 400 doctors have already completed the 2-3 year training program in family medicine. Eight hundred nurses have also been trained. But because trainees return to their former organizational environment, the model has yet to take hold. Family doctors have neither the mandate nor the incentive to adopt the family medicine approach.

24. To provide the necessary mandates and incentives, the PISG intends to fundamentally restructure the provision and financing of primary health care, starting in two or three demonstration municipalities. The reform would have two principal sub-components. The first would support primary health care restructuring to address sectoral inefficiencies. The sub-component will support the restructuring in demonstration sites of the traditional narrow

[10] Members of the commission include representatives of the central level and mayors with the latter holding the majority.

specialist based PHC system into family medicine units that will ultimately have the capacity to address 80 percent of the municipality health needs, thus significantly reducing the unnecessary high rate of cases now treated at hospitals. The second would support be the development and test of a new system for paying providers through *a performance-based payment mechanism* to be established for specific treatments in accordance with an agreed program of work for family medicine teams, providing a financial incentive to improve patient care at the primary level and reduce unnecessary referrals. (Further details are included in Annex 4.)

25. *Transport.* Long-standing neglect of maintenance and the recent conflict have had a significant impact on Kosovo's road network. In addition to bombed bridges and landslides, a significant part of the network is still in very poor condition. Road maintenance, now carried out through contractors, has been persistently under-funded, while funds are exhausted on new works, some of which are not economically justified. This has resulted in a continuous deterioration of the road network partially mitigated by the rehabilitation of the sections financed by the donor community in the past four years. The poor road network is hampering the regional integration of Kosovo and will keep the country outside of the regional trade flows.

26. Traffic congestion in the main cities and at the border crossing with FYR Macedonia is also a problem. Pristina has experienced explosive growth due to the effects of the Kosovo conflict. The population of the city has more than doubled over the past decade to over 500,000 persons and now constitutes about a quarter of the total population of Kosovo. As the city is the dominant commercial and administrative center of the region, a functioning urban road system is crucial to the economy of Kosovo. Traffic safety is also an issue with 900 accidents involving 1,470 injured and 160 fatalities in 2001, according to UNMIK records.

27. The Government's immediate strategy for the roads sector is to rehabilitate most of the damaged parts of the road network and reduce the road maintenance backlog as soon as possible. The long-term strategy is to build institutions, which will be capable of administering and managing the road network, involving primarily the Ministry of Transport and the Department of Roads. Some initial steps have been taken, including the establishment of a regulatory framework in line with EU requirements. The Government has also commissioned a study on road financing (by Roughton Intl.) and a separate study on road safety. Recommendations of these reports would be supported by the proposed project.

Annex 2: Major Related Projects Financed by the Bank and/or other Agencies
KOSOVO: Public Expenditure Management

1. The Bank has financed three adjustment-type grants aimed at improving public sector management.

- **Economic Assistance Grant I** (US$5.0 million; approved in CY00; closed) supported the creation of a fully functioning budget management system and a bank licensing and supervision capability. Under its aegis, the newly-created Central Fiscal Authority (CFA) made good progress in designing and implementing the Kosovo budget. The Banking and Payments Authority of Kosovo (BPK) was established at the end of 1999, and legislation for bank licensing, regulation and supervision then followed.

- **Economic Assistance Grant II** (US$5.0 million; approved in CY0l; closed) supported the formulation of a sustainable 2001 budget as well as tax and tariff reforms. A basic system of border-based taxation was established, resulting in a dramatic drop in the share of revenues contributed by donor funding (from 48 percent in 2000 to 21 percent in 2001). A liberal trade and customs regime was maintained. However, the full elimination of tariffs at the time of the introduction of the VAT did not take place because of revenue considerations.[11]

- **Economic Assistance Grant IV** (US$5.0 million; approved in CY03; closed) aimed at enhancing medium-term macrofiscal sustainability and improving financial management. The Kosovo Consolidated Budget for calendar year 2003 was approved by the SRSG. The 2004-2006 macro and revenue framework were agreed by the SRSG and used in the development of the 2004 budget. Regulations establishing the Office of the Auditor General and the Audit Office were promulgated and the Audit Office was established.

2. In the health sector, the Bank has supported an **Education and Health Project** (US$4.4 million. approved in CY00), which funded the development of an interim health care financing strategy, including the identification of priorities for publicly financed health care, the design and implementation of a co-payment system, and the development of options for private financing and private provision of health care. In the roads sector, the Bank supported the **Urgent Road Project** (US$5.0 million, plus US$43 million in co-financing; approved in CY00); closed) which supported the re-establishment of a road management capacity in the MTC, along with priority rehabilitation projects.

3. Other donors have been active in supporting public sector management reform. The European Agency for Reconstruction supported the development of a uniform salary and grading system for civil servants and the establishment of the Institute for Public Administration. As noted in the main text, the EAR is currently funding revisions to the procurement law and the drafting of the law's implementing regulations. It plans to finance a series of training courses to support their implementation later in 2005. EAR is also financing a €1.9 million, two-year project aimed at strengthening public internal financial control and internal auditing throughout the PISG.

[11] The Bank also financed the Economic Assistance Grant III. It focused on private sector development.

4. The United States has also been strongly involved in governance activities, including the provision of technical support for the Ministry of Economy and Finance (in the form of close to twenty long-term advisors and numerous short-term advisors.) With USAID support, the MFE is implementing new budget control procedures at the central and regional levels, including a computerized treasury ledger system, to ensure transparency and accountability in public expenditure practices. USAID has also supported the design of a new system of intergovernmental finance. The system resulted in the formulation of systematic grant policies and procedures based on expenditure needs for the 2004 budget cycle.

Annex 3: Results Framework and Monitoring
KOSOVO: Public Expenditure Management

Results Framework

PDO	Outcome Indicators	Use of Outcome Information
Kosovo uses public resources more effectively, efficiently and transparently	Strategic allocation of public resources through an improved budget preparation process within an overall medium term macro and fiscal framework.	Demonstrate effectiveness of systemic reforms and inform future improvements.
Intermediate Results One per Component	**Results Indicators for Each Component**	**Use of Results Monitoring**
Component One: PSM (i) Sectoral budgets reflect UNMIK/PISG priorities (ii) Public procurement is increasingly transparent, competitive	**Component One:** (i) Difference between ceilings established in budget circular and budget user's initial proposed budgets (ii) Number of external audit findings of material violations of procurement rules	**Component One:** (i) Widening discrepancies will indicate inadequacy of budget formulation TA; need to further strengthen central controls (ii) Increase in number of violations will flag need to strengthen penalties, tighten enforcement
Component Two: Health Scope of medical care is expanded under the family medicine model in demonstration municipalities	**Component Two :** (i) Number of patients registered with family medicine practitioners (ii) Proportion of health care worker remuneration paid in form of incentive payments.	**Component Two:** Provide performance feedback to set targets and agree on strategies for performance improvement • Evaluate the effectiveness of sector interventions and identify priorities for future policy interventions • Provide feedback for allocation of resources to improve access to health care • Ensure that primary care level is providing quality services, including range of preventive services • Ensure smooth transformation of health centers to family medicine model
Component Three: Transport PISG spending on roads becomes increasingly cost effective as road data is improved and staff become adept at prioritization software	**Component Three:** Number of traffic counters installed; Number of staff trained in prioritization software	**Component Three:** i) Demonstrate the capacity of MTC to introduce an essential component of the pavement management system (ii) Demonstrate the capacity of MTC to conduct economic appraisal of all road investments

Arrangements for results monitoring

		Target Values					Data Collection and Reporting		
Outcome Indicators	**Baseline**	**YR1**	**YR2**	**YR3**	**YR4**	**YR5**	**Frequency and Reports**	**Data Collection Instruments**	**Responsibility for Data Collection**
NA									
Results Indicators for Each Component									
Component One : (i) Difference between ceilings established in budget circular and budget user's initial proposed budgets (ii) Number of external audit findings of material violations of procurement rules							Annual, MFE Annual, Auditor General's Office	MFE annual budget circular, line ministry budget submissions AGO's annual report	MFE AGO
Component Two : (i) Number of patients registered with family medicine practitioners (ii) proportion of health care worker remuneration paid in form of incentive payments.							Annual, main family medicine centers and family medicine centers in demonstration municipalities	Main family medicine centers and family medicine centers in demonstration municipalities through patient registries HIS and service contracts with PHC providers	Center for Family Medicine Development is responsible for development and monitoring implementation of PHC strategy HCCA
Component Three: (i) Number of traffic counters installed (ii) Number of staff trained in HDM4							Annual project progress reports	MTC internal documents	MTC staff

Annex 4: Detailed Project Description
KOSOVO: Public Expenditure Management

1. *Budget Formulation.* This component of the proposed public sector management technical assistance grant (PEMTAG) would focus on two major areas of budget formulation. The first would be a consultancy and training program to build capacity in budget preparation in three major line ministries (Labor and Social Welfare, Health and Transport). It would pay for long-term consultants with specific knowledge of policy and technical issues in the area of each ministry, in addition to experience in budget preparation. To ensure the transmission of knowledge to local staff, terms of reference would include specific handover provisions. The second part would focus on building capacity among the budget analysts in the Ministry of Finance. This would include the counterparts of the three major line ministries and the municipalities, as well as the counterpart of the UNMIK-entity responsible for publicly-owned and socially-owned enterprises, the Kosovo Trust Agency (KTA). Again, this work would be carried out by long-term consultants with specific knowledge in these fields as well as in budget preparation and analysis, supported by local consultants.

2. The project will *not* attempt to address the budget formulation problems of all the major spending agencies. Municipalities, for example, account for close to thirty percent of general government spending (including spending on education and health) and represent a logical target for assistance. Such assistance, however, would be difficult, given the number of such jurisdictions (30). USAID is now implementing a Local Government Initiative (LGI) project which involves placing long-term advisers for three years, in five municipalities (Gjakovë, Gjilan, Podujevë, Shterpce and Suharekë). The LGI will assign a resident municipal consultant who will work side-by-side with municipal authorities to develop capacities, establish systems, and provide on-the-job training while addressing real community challenges. The LGI will also assist in improving the legislative framework for local governance and refining and clarifying the roles and responsibilities of municipal governments. Given the extent of USAID's efforts and the limited resources available under the PEMTAG, municipalities are excluded from the proposed operation

3. The project will also give short shrift to the major publicly owned enterprises (POEs), except for the loss making power-company KEK. KEK, along with other publicly- and socially-owned enterprises, is administered by the KTA, an UNMIK established entity. This arrangement has not worked harmoniously in the past, particularly when KCB budgetary resources have been required to assist the financially ailing company. In August 2004 a foreign private utility company was contracted to operate KEK. It is required, inter alia, to prepare a medium term business plan for the utility and to achieve certain performance benchmarks. This is expected to reduce KEK's claims on the KCB budget. Funding is nevertheless included in the PEMTAG to assist in the analysis of KEK's annual budget submissions.

4. A second component of the proposed project would aim at strengthening the capacity of the Ministry of Economy and Finance to analyze the submissions of major budget users. This would focus on the counterparts of the main spending ministries, the municipalities and the Kosovo Trust Agency (KTA).

5. The costs of the two components is estimated at € 935,000. This would finance:

- eight consultant-months of international consulting services[12] and 24 consultant-months of local consulting services to each of the three major spending ministries to assist in developing budget submissions linked to policy priorities and strategies;

- 24 consultant-months of international consulting services and 72 consultant- months of local consulting services to assist the Ministry of Economy and Finance in analyzing the budgets of the three target ministries, the municipalities, and KTA; and

- seven consultant-months of international consultants and 21 consultant-months of local consultants for training related to these two activities.

6. Assistance for budget preparation in the line ministries would be coordinated with related projects supported by other donors. These include the EAR's planned support for investment project identification and preparation in the line ministries (which will begin in January, 2005) and USAID's ongoing support to the Ministry of Economy and Finance and the municipalities. Assistance in the area of budget preparation and analysis under the PEMTAG project will also be coordinated with other components of the PEMTAG, including procurement reforms and sectoral reforms in the Ministries of Health and Transport.

7. *Budget Execution.* With the recent decline in Kosovo's cash reserves and its shift to cash based accounting, cash management skills have become increasingly important. This component would finance technical support to the PISG's fledgling cash management unit. Assistance is also required to improve the quality of financial information produced by the line ministries. Procedures for bookkeeping, accounting and financial reporting are not codified. Even the central Treasury lacks a manual of procedures specifying many of the processes and controls that are currently in place. The PEMTAG would therefore finance the drafting of a set of comprehensive written procedures for bookkeeping, accounting and financial reporting. The Treasury currently has available €100,000 for training in this area, from funds derived from the proceeds of a World Bank credit line for Small and Medium Enterprises. An additional €230,000 would be needed to finance the marginal cost of 24 consultant-months of technical assistance. The proposed manual would complement the planned extension of the Treasury's software system to the line ministries.

8. *Procurement* One-on-one mentoring by experienced procurement specialists will be required to ensure that the new procurement system is implemented as intended. In agreement with the EAR, the PEMTAG would finance international consultants to work with local counterparts over a period of up to two years. Specific institutions will be selected, in consultation with the PISG, based on their responsibility for implementing procurement for critical, high-value public investments and their readiness to allocate dedicated resources to achieve high performance in their procurement operations.) These will be the Ministries of Health, Transport, and Public Services. It is estimated that this will cost approximately €500,000.

[12] International Consultants includes consultant service firms from the region.

Health Sector Reforms

9. The Health Component would have three sub-components.

10. The first sub-component would finance implementation of the family medicine model in four municipalities. It would include support to: (a) an initial review of legislation to remove any legal obstacles to the implementation of the family medicine model; (b) technical assistance to assist municipal health departments and Main Family Medicine Centers in organizing doctors and nurses into teams and setting up systems for making appointments (micro organizational changes); (c) the development and implementation of guidelines, protocols and standards for family medicine teams and for disease management and disease prevention for practical use in primary health care, (d) a media campaign to inform the public about the family medicine reform and encourage patients to register with a doctor of their choice; and (e) a study tour to a country in ECA where family medicine has been implemented successfully.

11. A second sub-component would test a new system for paying providers. Although doctors and nurses would continue to be municipal employees and paid a basic salary, a performance-based payment mechanism would be established for specific treatments in accordance with an agreed program of work for family medicine teams, providing a financial incentive to improve patient care at the primary level and reduce unnecessary referrals. This sub-component would also provide training in the essentials of the new payment system for the Health Care Commissioning Agency, other staff, and participating providers.

12. The third sub-component would support skills development for the Ministry of health and would be coordinated closely with DFID. It would target training in three areas – management, policy development and planning, and communications skills. The health component would finance technical assistance, training, software and limited incremental operating costs.

Transport Sector Reforms

13. *Expenditure allocation* The transport component of the PEMTAG would have four subcomponents. To facilitate the prioritization of recurrent and capital expenditures within the road sector, technical assistance would be provided to review and strengthen the current Road Information Database (RID). This would include: (i) a review of the current responsibilities and organizational structures for the operation and management of the RID; (ii) the incorporation within the RID of data from a bump integrator (which is to be rented at MTC expense from FYR of Macedonia) which will measure road conditions across the whole network; (iii) the provision of training in the use of network expenditure optimization software (HDM4); and (iv) the production of an assessment of expenditure priorities on the primary and secondary road network, at a network level. This component will also finance the purchase of 50 fixed and mobile automatic traffic counters to measure traffic on the network, and international training for key staff in the MTC. (Under the public sector management component of this operation, technical assistance would also be provided to strengthen the budget application process within the MTC.)

14. *Financial sustainability.* Second, the project would finance the development of a detailed action plan to implement three of the main recommendations of the recent road user

charges study. Specifically, technical assistance would be provided to: (i) assess the costs and benefits and identify appropriate steps to introduce a general increase in the fuel duty of 6 and 8 Euro cents per liter on leaded and unleaded gasoline and diesel, respectively; (ii) design and implement an appropriate transit fee regime, consistent with EU requirements as manifested in, inter alia, EU Directives 1999/62/EC and COM 2003/448; (iii) review, and recommend changes, in the current scale and structure of road user charges, more generally, to ensure that the fees all vehicle classes pay covers the damage to the road infrastructure that resulted from their actions.

15. *Road safety.* To address road safety issues, the project would finance technical assistance for: (i) the establishment of an Inter-Ministerial Road Safety Council (including assistance with the clarification of its organizational composition, actual role, internal and external communication, campaign plan, and funding and annual report); (ii) the identification of 'black spots' and the implementation of appropriate remedial actions based on international best practice; (iii) training in road accident reconstruction; (iv) a traffic safety audit on a defined route; and (v) a review of the recently produced manual on road design to ensure that it is consistent with best practice on Safe Road Design principles. This subcomponent will also fund the purchase of suitable software for an Accident Information System, together with establishment and training.

16. *Traffic management by Pristina Municipality* This subcomponent of the project would finance technical assistance to improve traffic management capacities and practices in the Municipality of Pristina. This would include assistance in: (i) developing traffic management schemes to improve traffic flow; (ii) planning and managing parking to improve utilization of available parking spaces and to minimize disruptions to motor vehicle traffic and pedestrians; and (iii) public transport planning and regulation to improve public transport services. In addition, this subcomponent would finance a few defined high priority traffic management measures (signage and traffic signals), the purchase of appropriate software, and the collection of necessary data, to establish a tactical traffic assignment model, and a review of both current road investment plans in the area, and an assessment of the need and scope of an 'urban outreach unit' in the MTC, to disseminate best urban transport policy and practice.

Annex 5: Project Costs

TABLE 5.1 SUMMARY OF PROJECT COST			
Project Cost By Component and/or Activity	Local US $million	Foreign US $million	Total US $million
Public sector management	.125	2.310	2.435
Budget formulation	.125	1.137	1.262
Cash management/treasury manuals		.499	.499
Procurement		.674	.674
Health	.140	1.120	1.261
Primary health care restructuring	.090	.370	.460
Performance-based pay mechanism	.034	.520	.554
Skills development	.016	.230	.246
Transport		2.165	2.165
Expenditure allocation		.700	.700
Financial sustainability		.100	.100
Road safety*		.400	.400
Pristina traffic mgmt.**		.965	.965
Project management (PPA, Grants Unit)		.150	.150
Total Baseline Cost	.265	5.745	6.011
Physical Contingencies			0
Price Contingencies		.139	.139
Total Project Costs[1]	.265	5.884	6.150

Table 5.2 SUMMARY OF FINANCING PLAN (US$ MILLIONS)				
	Local	Foreign	Total	% of Total
IDA			5.500	89.4%
KCB			.300	4.9%
Pristina Municipality		-	0.350	5.7%
Total			6.150	100.0%

[1]Identifiable taxes and duties are US$ 13,250 and the total project cost, net of taxes, is US$6.136 million. Therefore, the IDA share of project cost net of taxes is 89.6 percent.

Annex 6: Implementation Arrangements

Overall responsibility for each of the three components will be assigned to its respective implementing ministry: Economy and Finance, Health, and Transport and Communications. Each implementing ministry will designate a senior-level project supervisor who will be responsible for monitoring overall progress on its respective component of the project. High-level representatives appointed by the Minister from each relevant ministry will participate in a steering committee which will be responsible for resolving inter-ministerial disputes. The Ministry of Public Services and the Ministry of Labor and Social Policy, as participants in the public sector management component of the project, will also appoint representatives to the steering committee. UNMIK Pillar IV will also be represented. The Committee will meet on a quarterly basis or more frequently if the need arises. The assistant to the permanent secretary of the MFE will act as the steering committee's secretariat.

Each project supervisor will be assisted by a more junior project administrator, who will be responsible for:

- developing annual work program drafts and activity budgets;
- developing quarterly management draft reports and annual reports on activities to be implemented by each Ministry;
- preparing the mid-term review;
- drafting terms of reference (TORs) and technical specifications for goods; drawing up shortlists; participating in evaluation committees, contract negotiations and award of contract;
- post contract work including facilitating the work of consultants; and
- approving payments after checking the quality and quantity of work undertaken.

Procurement will be carried out by each of the three implementing ministries, with the assistance of the Public Procurement Agency (PPA). While the implementing ministries will be responsible for drafting TOR, specification and signing of contract including its implementation , the PPA will act as their internal procurement agent.

The implementing ministries will be responsible for checking the quality and quantity of work carried out against contracts, issuing payment orders, and producing disbursement documentation. The Grants Unit will approve SOEs and other disbursement documentation and submit them to the Bank through UNMIK.

Based on the documents prepared by the implementing ministries, all relevant documents will be processed by the Grant Unit in the MFE, either to be paid by the Treasury or by direct payments. The MFE will prepare all the relevant documents in support of applications for withdrawal, sign them and forward them to the Bank through UNMIK. Contributions from the Kosovo Consolidated Budget (KCB) and the Municipality of Pristina will be made using normal PISG procedures.

The designated project administrator in each implementing ministry will check and process all CPOs received from the implementing ministries before submission to the MFE. The Grants Unit in MFE will assign a staff member to be responsible for the processing and control of payments, production of withdrawal applications, and for producing quarterly and annual financial statements for the project. The Grants Unit in MFE will work closely with the Procurement Agency and the implementing ministries to ensure that quarterly FMRs, annual financial statements and other progress reports are submitted in a timely manner to the Bank reflecting the implementation status of the project. Disbursements from the Grant will be made based on traditional disbursement methods, reimbursing the KCB based on Statements of Expenditures (SOEs) as well as using direct payments from the Grant. Reimbursement will be made monthly throughout the project period. The Grants Unit will also be responsible for drafting the Implementation Completion Report.

The accounting books and records will be maintained on a cash basis by the MFE based on the documentation provided by the implementing ministries, including additional commitment information for signed contracts. Quarterly and yearly project financial statements will be presented in EUR. MFE will institute a set of appropriate accounting procedures and internal controls including authorization and segregation of duties for this project based on previous similar projects.

The project financial statements and auditing arrangements for the previous projects managed by MFE are acceptable and will be replicated for the proposed project. The auditor will be appointed by the MFE. The audits will be conducted in accordance with International Standards on Auditing. The annual cost of the audits will be covered by the grant.

MFE will produce all financial reports and SOEs for the Bank. The formats of the quarterly Financial Monitoring Reports (FMRs) to be used for project monitoring and supervision and the formats of these will be agreed during negotiations and will be included in the FM manual. MFE will produce a full set of FMRs every three months throughout the life of the project.

The chart of accounts will be based on the Government Financial Management Information System. As the participants under the project fall under the umbrella of the Kosovo Consolidated Budget, all project-related payments will be made via the Single Treasury Account (STA), and the accounts would be maintained as part of the MFE's accounting system. Based on monthly reports from this system (Freebalance) MFE will, through the Grants Unit, manually produce the quarterly and annual financial reports required.

Annex 7: Financial Management and Disbursement Arrangements

Country Issues

An Operational Financial Accountability Report was finalized in November 2004. Despite significant progress since 2001, public financial management in Kosovo suffers from fundamental weaknesses, and basic structures for financial accountability are still in their infancy. The overall legal framework for budgeting and budget management is largely compatible with internationally recognized standards, but for some aspects it appears to be too advanced for the current administration's capacity. Carry-over practices and weaknesses in capacity, organization and coordination hamper budget preparation and undermine the credibility of the budget as a policy management instrument. While treasury and cash management are well-regulated areas of public financial management, they suffer from inefficiencies. The system through which Commitment and Payment Orders flow to ensure authorization of payments is well regulated. The Treasury authorizes commitments and payments based on proposals and supporting documentation by budget organizations and municipalities. The Treasury pays from a single account in the central Banking and Payment Authority of Kosovo (BPK).

As with most public financial management functions, accounting is constrained by limited capacity, and financial reporting needs more realistic requirements and statutory deadlines, improved procedures, and trained personnel. Internal control and internal audit at all levels of government are in their infancy. Considerable time and effort will be required to make them fully operational. External audit is undeveloped and, as with internal audit, it will need sustained external support for its development.

Specific procedures are developed by MFE to secure proper financial accountability of this project.

Strengths and Weaknesses

The significant strengths that provide a basis of reliance on the project financial management system include: (a) the experience of MFE and UNMIK of implementing previous projects and satisfying Bank financial management requirements; and (b) the audit reports and management letters issued by the auditors.

There are no significant weaknesses of the project financial management system.

Implementing Entity

Overall responsibility for each of the three components will be assigned to its respective implementing ministry: Economy and Finance, Health, and Transport and Communications. Each implementing ministry will designate a project administrator who will be responsible for its respective role in procurement and financial management. This would specifically include drafting TORs, shortlists, and technical specifications for goods, participating in evaluation committees and contract negotiations, facilitating the work of consultants, and approving payments after checking the quality and quantity of work done.

Procurement for each implementing ministry will be carried out by the Public Procurement Agency (PPA), with the participation of the relevant ministry. With respect to technical assistance and training, the implementing ministry will be responsible for drafting TORs for consultants' assignments and preparing short-lists of consultants and firms. Both the PPA and the ministry will participate in evaluation committees and contract negotiations. With respect to goods, the ministry will be responsible for preparing technical specifications for goods, with the assistance of the PPA. The PPA would be responsible for carrying out the procurement, i.e., inviting expressions of interest, preparing bidding packages, obtaining clearances, inviting bids, and evaluating proposals.

Financial management activities will be performed by the Grants Unit in the MFE, with the participation of the relevant implementing ministry. The implementing ministries will be responsible for checking the quality and quantity of work carried out against contracts, issuing payment orders, and producing disbursement documentation. The Grants Unit will approve SOEs and other disbursement documentation and submit them to the Bank through UNMIK.

Funds Flow

All payments will be made by the MFE from its own sources of funds and no special account will be needed. Based on the documents prepared by the implementing ministries all relevant documents will be processed by the Grant Unit in the MFE, either to be paid by the Treasury or by direct payments. The MFE will prepare all the relevant documents in support of applications for withdrawal, sign and forward them to the Bank through UNMIK. Contributions from the MTC and the Municipality of Pristina will be made using normal PISG procedures.

Staffing

The project administrator in each implementing ministry will check and process all Commitment and Payment Orders (CPOs) received from the implementing ministries before submission to the MFE. All entities producing the CPOs have duly established finance units with adequate staffing and the processing of the project invoices will follow the normal procedures these units are already using. The designated point person in each implementing ministry will check and process all CPOs received from the implementing ministries before submission to the MFE. The Grants Unit in MFE will assign a staff member to be the focal point for processing and control of payments, production of withdrawal applications, as well as producing quarterly and annual financial statements for the project. The Grants Unit in MFE will work closely with the Procurement Agency and the implementing ministries to ensure that quarterly FMRs, annual financial statements and other progress reports are submitted timely to the Bank reflecting the implementation status of the project.

Accounting Policies and Procedures

The accounting books and records are maintained on a cash basis by MFE based on the documentation provided by the implementing ministries including additional commitment information for signed contracts. Quarterly and yearly project financial statements are presented in EUR. MFE will institute a set of appropriate accounting procedures and internal controls including authorization and segregation of duties for this project based on previous similar projects.

The policies and procedures are further elaborated in the Project Implementation Manual.

Internal Audit

No internal audit is established and no such function is deemed necessary.

External Audit

As of the date of this report, the grant receiver is in compliance with its audit covenants of the existing Bank-financed project. Current project financial statements and auditing arrangements for the previous projects managed by MFE are acceptable and it has been agreed that these arrangements will be replicated for the proposed project. The audit will only cover the project activities. The auditor will be appointed by the MFE. Specific terms of reference will be agreed during negotiations. The audits are conducted in accordance with International Standards on Auditing. The annual cost of the audits will be covered by the grant.

Reporting and Monitoring.

MFE will produce all financial reports and SOEs for the Bank. The formats of the quarterly Financial Monitoring Reports (FMRs) will be agreed during negotiations to be used for project monitoring and supervision and the formats of these will be included in the FM manual. MFE will produce a full set of FMRs every three months throughout the life of the project.

Information Systems.

The chart of accounts is based on the Government's Financial Management Information System. This system was assessed in the Operational Financial Accountability Report and found to be acceptable for the purpose of registering the necessary financial information. As the participants under the project fall under the umbrella of the Kosovo Consolidated Budget, all project related payments would be made via the Single Treasury Account (STA), and the accounts would be maintained as part of the MFE's accounting system. Based on monthly reports from this system (Freebalance), MFE will produce the quarterly and annual financial reports required. The consolidated reports on uses of funds according to organizational code, the uses of funds according to sub-component, and the commitment/obligation analysis report with commitment and actual data (that is report 1 to 3), will all be produced by the Freebalance system on request of the Grants Unit. The contract monitoring information (report 4a, 4b, and 4c) will be produced by the implementing ministries based on the commitment/obligation analysis report and the information on each contract. The narrative report and the consolidation of the other reports will be done by the Grants Unit.

Disbursement Arrangements.

Disbursements from the Grant will be made based on transactional disbursement methods, reimbursing the Recipient based on Statements of Expenditures (SOEs) as well as using direct payments from the Grant, although only in exceptional cases as initiated by the MFE. No special account will be opened.. Reimbursement will be made monthly throughout the project period. There is no plan to move to report-based disbursement.

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Supervision Plan

During project implementation, the Bank will supervise the project's financial management arrangements in two main ways: (i) review the project's quarterly financial management reports as well as the project's annual audited financial statements and auditor's management letter; and (ii) during the Bank's supervision missions, review the project's financial management and disbursement arrangements to confirm that satisfactory financial management arrangements have been maintained. As required, a Bank-accredited Financial Management Specialist will assist in the supervision process.

Annex 8: Procurement Arrangements

A. General

Procurement for the proposed project would be carried out in accordance with the World Bank's "Guidelines: Procurement under IBRD Loans and IDA Credits" dated May 2004; and "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" dated May 2004, and the provisions stipulated in the Grant Agreement. The various items under different expenditure categories are described in general below.

The Procurement under the project relates to the following components: (a) Public Sector Management ; (b)Health; (c) Transport ; and (d) Project Management for Grants Unit

A General Procurement Notice (GPN) will be published in the UN Development Business online and in the Development Gateway's "dgMarket". All individual Specific Procurement Notices (SPN) for goods and Expressions of Interest (EOI) estimated to cost US$200,000 or more for consulting services will be also be advertised in the UNDB online and in dgMarket. and in at least one newspaper of wide circulation in Kosovo

Project Agencies would follow the World Bank anti-corruption measures and would not engage the services of firms and individuals debarred by the Bank. The listing of such debarred firms and individuals is located at: *http://www.worldbank.org/html/opr/procure/debarr.html*

Procurement of Works: No works would be procured under this project.

Procurement of Goods Goods procured under this project would include automatic traffic counters and signals, traffic model software, and signage The procurement will be done using the Bank's Standard Bidding Documents (SBD) for all ICB and Invitation to Quote document (for shopping) agreed with the Bank.

Selection of Consultants. The project will finance an extensive array of consulting services to (inter alia) cover: (a) within the Public Sector Management component: budget formulation, cash management and treasury manuals ,procurement consultant , and in the major spending ministries for one-on-one mentoring (b) within the Health component: primary health care restructuring, performance based pay mechanism and skill development; and (c) within the Transport Sector: financial sustainability, road safety, urban traffic management and HDM4/road data bank and (d) within the Project Management component, start-up procurement and disbursement consultants and audit services.

Operating Costs. The project will finance limited operating costs for the MFE Procurement and Grants Unit and in the health subcomponent.

Project Implementation Manual. The detailed procurement/selection arrangements, procurement methods and organization of procurement are also given in the Project Implementation Manual, which is available as part of the project documentation

Procurement will be carried out by each of the three implementing ministries, under the supervision of the Public Procurement Agency (PPA). With respect to small value consultancy contracts, the implementing ministry will be responsible for drafting TORs and preparing short-lists of consultants and firms, with the assistance of the PPA. Both the PPA and the ministry will participate in evaluation committees and contract negotiations. With respect to large value consulting contracts (those requiring prior review of the Bank) and the procurement of goods, the implementing ministry will be responsible for preparing TORs and technical specifications (in the case of goods) and will also prepare the first draft of the request for proposals and bidding documents, with the procurement assistance and advice of the PPA. Both the PPA and the implementing ministry will participate in the committee that will evaluate the technical and financial proposals. Both will also participate in contract negotiations. The implementing ministry will sign the contract and will be responsible for ensuring that the contract is implemented.

B. Assessment of the agency's capacity to implement procurement

Procurement activities will be carried out by the Public Procurement Agency, with the participation of the relevant implementing ministry. The Ministry of Finance will implement the public sector management component; the health and transport components will be implemented by their respective ministries.

An assessment of the capacity of the implementing agency to implement procurement actions for the project was carried out by Devesh Mishra (World Bank) in December of 2004. This assessment was carried out in association with the task team for the proposed Business Environment Technical Assistance Project. This was followed by another round of discussions with PPA in March/April 2005 particularly on making the PPA aware of the changes in the Bank's Guidelines and to ensure that the procurement management arrangement as recommended in the Project Implementation Manual is workable.

The PPA has a staff of 15, with backgrounds in economics, law or engineering. Although they have little procurement experience (averaging about two years), many have been trained at courses organized by the International Labor Organization. . It was concluded that though these staff have minimum basic experience in Bank-funded procurement, they will need mentoring by one more experienced procurement consultants(start-up consultant) This start-up procurement consultant will be an international consultant with approximately 10 years of experience in Bank-funded procurement or experience in a similar international funding agency. The procurement consultant's services will be financed under the Project Management (Grants Unit) component of the PEMTAG project. Bank staff will have to be closely involved in the initial project period to assist PPA till the start-up procurement consultant is selected.

C. Procurement Plan

The Borrower, has developed a procurement plan for project implementation which provides the basis for the procurement methods. For each contract to be financed by the grant, the different procurement methods or consultant selection methods, the need for pre-qualification, estimated costs, prior review requirements, and time frame will be agreed between the Borrower and the Bank and specified in the Procurement Plan. The Procurement Plan will be updated at least annually or as required to reflect the actual project implementation needs and improvements in institutional capacity. The Procurement Plan will be available at the office of the Public Procurement Agency. It will also be available in the project's database and in the Bank's external website.

D. Frequency of Procurement Supervision

In addition to the prior review supervision to be carried out by Bank staff, periodic supervision missions (at least every 12 months) will visit the field to carry out post review of procurement actions.

E. Details of the Procurement Arrangements Involving International Competition

Goods

1. **Prior Review Threshold**: Procurement Decisions subject to Prior Review by the Bank as stated in Appendix 1 to the Guidelines for Procurement:

	Procurement Method	Prior Review Threshold
1.	ICB (Goods)	All
2	Shopping	First two contracts (contracts not to exceed $100,000)

2. Procurement Packages with Methods and Time Schedule

Contract (Description)	Estimated Cost (US $ Million)	Procurement Method	Review by Bank (Prior / Post)	Expected Bid-Opening Date	Bid Evaluation completion	Contract award	Contract completion
Automatic Traffic Counters	0.500	ICB	Yes	August 2005	October 2005	November2005	May 2006
Accident Information System	0.100	ICB	Yes	August 2005	October 2005	November 2005	May 2006
Traffic signal Installation	0.400	ICB	Yes	August 2005	October 2005	November 2005	May 2006
Vertical and Horizontal Signage	0.100	ICB	Yes	March 2006	May 2006	June 2006	December 2006
Traffic Model, software, computer	0.050	Shopping, Direct Contracting or part of TA	First two shopping and Direct contracting	continuous	continuous	continuous	December 2006
Total -Goods	**1.15**						

Selection of Consultants

1. **Prior Review Threshold.** Selection decisions subject to Prior Review by Bank as stated in Appendix 1 to the Guidelines Selection and Employment of Consultants:

	Selection Method	Prior Review Threshold
1.	Competitive Methods (Firms)	$50,000
2.	Single Source (Firms)/Sole-Source individuals	All
	Contracts with Individuals	$25,000

All TORs shall be subject to prior review

2. **Short list comprising entirely of national consultants**: Short list of consultants for services, estimated to cost less than $100,000 equivalent per contract, may comprise entirely of national consultants in accordance with the provisions of paragraph 2.7 of the Consultant Guidelines .This will however be determined on a case-by-case basis depending on the nature of the consultancy

3. **Consultancy Assignments with Selection Methods and Time Schedule**

Ref. No.	Description of Assignment	Estimated Cost US $ Million	Selection Method	Review by Bank (Prior / Post)	Expected Proposals Submission Date	Tech Evaluation completion	Contract Award	Contract Completion
I	**Public Sector Management**							
(i)	Budget Formulation	1.262	QCBS	Prior	September 2005	November 2005	January 2006	June 2007
(ii)	Cash Management /treasury manual	0.499	QCBS	Prior	September 2005	November 2005	January 2006	December 2007
(iii)	Procurement (one-on-one mentoring in line ministries)	0.674	QCBS	Prior	September 2005	November 2005	January 2006	December 2007
II	**Health**							
(i)	Primary health care restructuring	0.460	QCBS	Prior	September 2005	November 2005	January 2006	December 2007
(ii)	Performance-based pay mechanism	0.554	QCBS	Prior	December 2005	February 2006	April 2006	March 2008
(iii)	Skills Development (Training)	0.246	Individual, CQ, SOE	Prior	continuous	continuous	Continuous	Continuous
III	**Transport**							
(i)	Financial Sustainability	0.100	CQ	Prior	August 2005	October 2005	December 2005	June 2006
(ii)	Road Safety	0.250	QCBS	Prior	August 2005	October 2005	December 2005	December 2006
(iii)	Urban Traffic Management	0.450	QCBS	Prior	August 2005	October 2005	December 2005	June 2007
(iv)	HDM4/Road Data Bank	0.200	QCBS	Prior	August 2005	October 2005	December 2005	December 2006
(v)	Road Accident Reconstruction	0.050	CQ	Prior	August 2005	October 2005	December 2005	December 2006
(vi)	Training	0.015	SOE		continuous	continuous	continuous	continuous
IV	**Project Management Grants Unit**							
(i)	Start-Up Procurement Consultant	0.075	Individual	Prior	May 2005	June 2005	July 2005	July 2007
(ii)	Start-Up Disbursement Consultant	0.050	Individual	Prior	June 2005	July 2005	August 2005	September 2007
(iii)	Audit Services for the PEMTAG	0.025	Least Cost	Prior	November 2005	December 2005	January 2006	March 31, 2009
	Total- Consultancy	**4.91**						

IV. Implementing Agency Capacity Building Activities with Time Schedule

Agreed Capacity Building Measures. This project itself is a capacity building program by one-on-one-mentoring of procurement staff of high spending line ministries. In addition to hiring of start-up procurement consultant to assist PPA. The European Agency for Reconstruction (EAR) is financing a training program to support the implementation of the Procurement Law. Until such time as the start-up consultant is hired, Bank staff will train/provide advice to PPA on Bank procurement procedures. The start –up procurement consultant will work for about 18-24 months. PPA will act as an internal procurement agent for the line ministries and will provide full procurement support to them until capacity is built in the ministries. PPA also identified contact procurement persons in each line ministry. The training activities of EAR and of one-on-one mentoring of line ministries will continue for the duration of the project

Annex 9: Economic and Financial Analysis

1. The project is financed as a grant, which the recipient (UNMIK) will pass on to the Kosovo Consolidated Budget (KCB) for the purposes specified in the project documentation. To the extent that the grant replaces other revenues that would have been used for these purposes, it will increase the general budgetary resources of the KCB. The public sector management component may imply eventual increases in certain staff salaries, however, to prevent the departure of staff once they are trained. As the number of such positions is small, this would not have any significant fiscal implications for the KCB as a whole.

2. The fiscal situation of the KCB itself has fluctuated in recent years. Considerable progress was made in raising domestic revenues and controlling expenditures in the immediate post-conflict years. Buoyed by the introduction of new taxes and a post-conflict boom, tax revenues exceeded projections. At the same time, public spending was discouraged by certain budgetary practices.[13] As a result, budget surpluses were achieved in every year until 2004 and a cash surplus of approximately €300 million had accumulated by the beginning of 2003.

3. Growth in tax revenues leveled off in 2003 and 2004, while the constraints to expenditure management have largely been removed. As a result, the budget recorded a cash deficit of €130 million (6.8 percent of GDP) in 2004. The prospects for further growth in the tax base are not encouraging. Between 1999 and 2003 the international donor community spent an estimated €1.96 billion in Kosovo, while remittances from the Kosovo diaspora added another €550 million per annum over this period. Since 2000, donor grants have fallen by 70 percent, and are forecast to continue to decline. As a result, over the next four years, Kosovo's medium term fiscal framework will require an absolute reduction in general government expenditures from the levels in 2004. Beginning in 2006, the government will have to maintain a balanced budget, using the remaining cash surplus as a liquidity buffer. The PEIR, currently under preparation (and due out in gray cover in June of this year) will assist the authorities in ensuring that fiscal policy is prudent and that the surpluses accrued to date are spent in a sustainable way, in line with short and long term priorities. The PEIR will also identify numerous contingent liabilities, as yet not explicitly included in the medium term fiscal framework.

Trends in Kosovo General Budget Finances
(% of GDP)

	2001	**2002**	**2003**	**2004 Est**	**2005 proj**
General government revenues	21.4	30.1	32.8	32.6	30.2
General government expenditures	15.0	23.1	30.3	39.5	35.5
Surplus/Deficit (after grants)	6.4	7.0	2.5	-6.8	-5.4

Source: IMF estimates

[13] Budget managers, for example, had no incentive to meet expenditure targets as unused appropriations were routinely rolled over into the following year appropriation.

Annex 10: Safeguard Policy Issues

The project is a technical assistance project and is not expected to present any significant safeguards issues. The specific consultant contracts will include requirements that assistance will be guided by Bank Safeguard policies and procedures. Compliance will be monitored by the Bank during supervision.

Annex 11: Project Preparation and Supervision

	Planned	Actual
PCN review	10/29/2004	11/04/2004
Initial PID to PIC		11/09/2004
Initial ISDS to PIC		11/09/2004
Appraisal		4/07/2005
Negotiations	4/21/2005	
Board/RVP approval	6/14/2005	
Planned date of effectiveness	9/1/2005	
Planned date of mid-term review	3/1/2007	
Planned closing date	3/31/2009	

Key institutions responsible for preparation of the project:

Ministry of Economy and Finance
Ministry of Health
Ministry of Transport and Communication

Bank staff and consultants who worked on the project included:

Name	Title	Unit
William Dillinger	Lead Public Sector Management Specialist	ECSPE
Roland Clarke	Senior Public Sector Specialist	ECSPE
Shaun Moss	Lead Procurement Specialist	ECSPS
Devesh Mishra	Senior Procurement Specialist	ECSPS
Johannes Stenbaek-Madsen	Financial Management Specialist	ECSPS
Olav Rex Christensen	Senior Financial Management Specialist	ECSPS
Martin Humphreys	Senior Transport Economist	ECSIE
Richard Podolske	Transport Specialist (consultant)	ECSIE
Betty Hanan	Senior Operations Officer	ECSHD
Nedim Jaganjac	Health Specialist (ETC-consultant)	ECSHD
Tracey Lane	Country Economist	ECSPE
Mark Walker	Lead Counsel	LEGEC
Shpend Ahmeti	Program Officer	ECSPE

Bank funds expended to date on project preparation:

1. Bank resources: $129, 073 (as of January 24, 2005)
2. Trust funds: 0.
3. Total: $129,073

Estimated Approval and Supervision costs:

1. Remaining costs to approval: $85,927
2. Estimated annual supervision cost: $90,000

Annex 12: TOR for Budget Formulation

Background

The United Nations Interim Administration Mission in Kosovo (UNMIK) has received a technical assistance grant to support the strengthening of public expenditure management. The grant will finance technical assistance and training to strengthen the capacity of the Provisional Institutions of Self Government (PISG) in budget formulation, budget execution, and procurement, as well as specific policy and procedural reforms in the health and transport sectors.

The budget process is governed by a modern organic budget law (the Law on Public Financial Management and Accountability of May 2003), which clearly indicated the responsibilities and main processes for the preparation, approval and execution of the budget. Formally the processes are followed. However the quality of budget submissions prepared by line agencies is poor. Little capacity exists within the line ministries to prepare relevant and meaningful budget submissions linked to policies and priorities. In addition submissions are well outside initial ceilings provided by the MFE. Within the MFE, the budget department lacks the capacity to analyze and challenge budget users' proposals in any depth. Thus the discussion of budget proposals is very much a mechanical exercise in which the MFE allocates resources to agencies and municipalities without a clear understanding of their policy impact.

Substantial support is being provided by international advisers to the central institutions involved in the budget process. USAID is providing a team of advisors to the Ministry of Economy and Finance (MFE), particularly for macroeconomic forecasting, budget formulation, and treasury operations. The European Agency for Reconstruction (EAR) is financing major programs of technical assistance in public investment planning, internal audit, and procurement. This assignment would complement those efforts.

Objectives of Assignment

The objective of the assignment is to assist the PISG in increasing the institutional capacity for budgeting with an initial focus on the MFE and the 3 key line ministries (Labor and Social Welfare, Health and Transport and Communications). The component will focus on two major areas of budget formulation.

The first would be a consultancy and training program to build capacity in budget preparation in the three key line ministries. This will be provided by long-term consultants with specific knowledge of policy and technical issues in the area of each ministry, in addition to experience in budget preparation. The focus of the work will be to ensure the transmission of knowledge and capacity building of local staff, which can subsequently be extended beyond the three recipient ministries.

The second part would focus on building capacity among the budget analysts in the budget department of the Ministry of Economy and Finance. These would include the counterparts of the three major line ministries (Labor and Social Welfare, Health and Transport and Communications) and the municipalities, as well as the counterpart of the Kosovo Trust Agency (KTA) responsible for public utilities. Again, this work would be carried out by long-term consultants with specific knowledge in these fields as well as in budget preparation and analysis, supported by local consultants, who would be able to continue the work of capacity building after the end of the project.

Scope of Work

The specific tasks of the advisers in the line ministries are to:

- Build analytical capacities for budgeting within a results oriented framework in a uniform and coherent manner across the line ministries (in close cooperation with other budget advisors, including particularly the USAID advisors in the MFE);
- Build links between the budgeting and strategic policy making capacity of the line ministries;
- Provide advice in the costing and evaluation of new policies and initiatives;
- Make proposals on the reorganization of the budgeting and policy making units of the line ministries together with internal procedures and regulation consistent with the legal framework and budget regulations issued by the MFE;
- Provide advice on the elaboration of forward estimates in line ministries (in close cooperation with the USAID advisors) and with due consideration for capacity of ministries to develop such estimates and the need to provide adequate resources for the development of the annual budget;
- Organize and perform relevant training in the areas mentioned above;
- Organize change management sessions, for top and middle management to assist the process of changing the culture and organization of budgeting in the line ministries;
- Work closely with other teams providing assistance under the project, including particularly those providing assistance in procurement, financial management and policy advice in the Health and Transport Sectors to ensure that the budgeting reforms are fully consistent with and link to the public management reforms being supported under this project and by other donors;
- Build capacity of the local officials to manage the process of budget preparation in general, and through the use of local consultants contracted under the project provide a sustainable mechanism to continue transferring capacity to the ministries not targeted by the assistance.

Specific tasks of advisers in the Ministry of Economy and Finance are to:

- Work with the Budget Analysts of the budget department of the MFE to assist them to identify the strengths and weaknesses of budget submissions of the line ministries and the KTA (for Publicly Owned Enterprises), particularly as these refer to the agreed priorities of the Kosovar authorities;
- Provide guidance and training to the budget analysts in evaluating budget submissions against proposed results and outcomes;
- Provide advice to budget analysts on giving useful feedback to line ministries on budget submissions so as to improve the quality of budget submissions;
- Organize or promote joint working groups between MFE budget analysts and line ministry counterparts to promote a common understanding of the requirements of the budget process methodology, particularly as it refers to budget submissions by ministries;
- Assist the MFE to draft guidance methodology for the line ministries for the preparation of budget submissions;
- Build capacity of the local officials in the MFE to manage the process of budget analysis, and through the use of local consultants contracted under the project provide a sustainable mechanism to continue training and development of budgetary analysis capability.

Suggested Methodology

The work under the project should be organized in four task forces, corresponding to the three key line ministries identified previously and the support to the budget analysis section of the MFE. They should cover the tasks listed above.

A team leader of the project who will be one of the advisers to the Ministry of Finance will coordinate the work of the four task forces. (S)he will meet the other three task force leaders on a continuous and regular basis in order to discuss the progress of their work, and ensure the application of a consistent methodology across ministries.

In addition to the MFE and 3 key ministries, representatives from other ministries should be invited to participate in the task forces.

Each of the three line ministry task forces should consist of the following members:

1. The Adviser responsible for the line ministry, as a task force leader;
2. The MFE budget analyst dealing with financing of this ministry, as a liaison officer;
3. The budget officer from the ministry;
4. An official responsible for policy development in the ministry;
5. 2-3 MFE budget analysts responsible for financing of other ministries;
6. Budget experts from other ministries;
7. The local task force coordinator assisting the Adviser.

The task force of the MFE will consist of the international and local advisors contracted to develop the budget analysis capacity of the MFE, together with the budget analysts of the MFE.

Each task force should meet on a regular basis, at least once a month, in order to discuss tasks being carried out, bottlenecks tackled and results delivered. The task force leaders will ensure that each member of their task force is actively involved and participates in the process of elaboration of tasks that should be completed.

To ensure that the task force leaders are able to provide effective on the job coaching and mentoring it is recommended the task force leaders be based in their respective ministries. From there they will also maintain regular contacts with other ministries involved. The task force leaders will be assisted in their work by local coordinators (consultants).

At the end of their assignment the consultants will be required to demonstrate that the officials of the ministries receiving the assistance are in a position to carry out their functions without external support. It is therefore essential that prior to the approval of the final report the consultants can show what skills and capacity have been transferred to local officials and indicate further weaknesses that may need to be addressed.

The authorities will consider proposals with alternative methodologies from that outlined above if these can be shown to produce the required results.

Required Outputs

- Annual budgets prepared according to pre-agreed calendar with budget submissions clearly linked to policy priorities and to initial ceilings given by MFE;
- Methodology and guidance notes prepared for preparation of budget submissions and used by line ministries;
- Methodology prepared for analysis of budget submissions within the Ministry of Finance and used by line ministries;
- Recommendations on restructuring of budget and policy units within the line ministries and necessary changes to internal procedures;
- Methodology for forward estimates prepared in line ministries;

Liaison and Reporting Requirements

The Advisers in the three line ministries will report to the Adviser in the MFE (the Team Leader) who will be responsible for overall consistency of the approach in the different line ministries. (S)he will be responsible to the Minister of Finance and the Permanent Secretary and will report on a regular basis. At the end of the second month the Team Leader will submit an inception report showing a work plan of significant tasks to be undertaken during the contract period, acceptable to the Ministry of Economy and Finance In addition (s)he will submit short (maximum 3 pages) monthly updates of the inception report to the Permanent Secretary and the Steering Committee which will show achievements over the previous month, work program for the next month and problems encountered, as well as progress toward achieving the goals set in the inception report. At the end of the contract (s)he will submit a final report on work undertaken which will include recommendations for future work and development in the area of budgeting and demonstrate the skills and capacity transferred to local officials.

Monitorable Indicators of Performance

The success of the advisers will be judged by the delivery of the Required Outputs. In addition the following indicators will be of importance:

- evidence of close collaboration with Advisers working under other contracts of the PEMTAG and with other advisers supporting public sector reform in Kosovo;
- satisfactory progress toward goals set out in the inception report as described in the previous section;
- close cooperation and communication established between the MFE and individual ministries in the area of budgeting;
- Clear indication that skills have been transferred to local officials.

Consultants Qualifications

The Team Leader should have at least 8 years experience at a senior policy level in a Ministry of Finance or equivalent and have a detailed working knowledge of results oriented budgeting. The other Advisers should have at least 5 years experience and have a working knowledge budgeting techniques. It is desirable that the advisers in the three line ministries should have experience in the ministry's area of sectoral responsibility. In addition one of the advisors supporting the budget analysis section of the MFE should have experience in the areas of infrastructure and or public enterprise budgeting, while the others should ideally have knowledge or experience in the sectoral areas of health, transport, and social welfare and employment.

Other important qualifications for all advisers include:

- an advanced degree in economics or public finance;
- practical experience in developing budgets in market or transition economies;
- diplomatic skills and ease at working in an international environment.

The Advisers should be assisted by local coordinators who should have at least 5 years of experience in project work, have a good working knowledge of both written and spoken English and have a degree in economics or finance.

Contract Arrangements

The assignment is foreseen for the period ______ – ______ for a total working period of 48 months for the international advisers (i.e. 8 months average per line ministry and 24 months for the MFE) and 144 months for the local coordinators (i.e. 24 months per line ministry and 72 months in the MFE). The contract should cover all costs of travel, subsistence, interpretation and translation services and training.

The authorities will provide office space, use of personal computer, general office supplies and funds for domestic travel required for the assignment.

Annex 13: TOR for Preparation of Accounting Manual

Background

The United Nations Interim Administration Mission in Kosovo (UNMIK) has received a technical assistance grant to support the strengthening of public expenditure management. The grant will finance technical assistance and training to strengthen the capacity of the Provisional Institutions of Self Government (PISG) in budget formulation, budget execution, and procurement, as well as specific policy and procedural reforms in the health and transport sectors.

Objectives of the Assignment

The objective of this assignment is to enhance the reliability of the financial reporting of the PISG. Whereas it is assumed that the procedures used to operate the Treasury system (FREEBALANCE) are well described in the documentation given by the system provider, bookkeeping, accounting and financial reporting and indeed the principles behind sound accounting practices are not documented or promoted in a consistent manner. It is expected that the development and eventual endorsement of a comprehensive accounting manual will facilitate this.

In accordance with the statements of accounting policy presented in the reports of the external auditor on the Kosovo Consolidated Budget (KCB), the accounting standard applied by the KCB is the cash basis International Public Sector Accounting Standards (Cash Basis (CB) IPSAS). One of the objectives of developing the Accounting Manual will be to institutionalize and harmonize the accounting practices across the PISG and UNMIK administration in accordance with CB IPSAS.

Scope of Work

The work will consist of researching for, drafting and ensuring the submission for formal endorsement by the PISG and SRSG of a manual of accounting (hereafter the Manual) to be applied by the financial services of all KCB spending entities. The Manual must cover detailed written procedures for bookkeeping, accounting and compilation and presentation of financial statements. It should also contain job-descriptions for bookkeeping and accountancy functions at different levels and suggestions as to how to obtain and maintain the skills required to perform bookkeeping and accountancy functions. The draft Manual should be discussed and eventually agreed with the Ministry of Economy and Finance, including its internal audit department, and the SRSG. The draft should also be discussed with the Office of the Auditor General.

Activities

The work of the consultant must include:

- Analysis of legal and other background documentation
- Development and drafting of detailed written procedures for bookkeeping and accounting, including reconciliation and compilation and presentation of financial statements in accordance with CB IPSAS (for overview of standard, please see annex) and the procedures laid down for the Treasury system
- Addressing the issue of the need for current training of public sector accountants by proposing a concrete training plan attached as an annex to the Manual
- Discussion and eventual agreement with any regulatory authorities who are competent in the field of audit or accounting

- Discussion and eventual agreement with senior officials of the Ministry of Economy and Finance (MFE) on endorsement of the Manual by that Ministry.

Outputs and Timing

The Manual should be prepared for endorsement by the PISG and the SRSG no later than ____. The working time required to prepare the Manual will be an estimated 6 consultant- months.

Reference documents

Key reference documents include:
- Audit Report: External Audit of the 2001 Kosovo Consolidated Budget (and external audit reports for subsequent fiscal years)
- Manuals and procedures for operating the Treasury system
- The Law on Public Financial Management and Accountability
- The Law on Public Procurement
- Cash Basis International Public Sector Accounting Standards

Qualifications required

The consultant must fulfill the following requirements:
- Have at least 10 years of professional experience as financial accountant, preferably from a public sector institution such as a ministry or a state owned enterprise
- Must have some knowledge about Kosovo laws, regulations and practices as well as being familiar with international standards and practice for accounting and auditing
- Must hold an internationally recognized professional accountancy or auditing qualification (e.g. ACA, ACCA, CIPFA, CPA etc).

Annex 14: TOR for Procurement Consultants

Background

The United Nations Interim Administration Mission in Kosovo (UNMIK) has received a technical assistance grant to support the strengthening of public expenditure management. The grant will finance technical assistance and training to strengthen the capacity of the Provisional Institutions of Self Government (PISG) in budget formulation, budget execution, and procurement, as well as specific policy and procedural reforms in the health and transport sectors.

A new Law on Public Procurement (LPP) was promulgated in February, 2004 and was to become effective in June of the same year. Although it addressed many of the flaws in the prior legislation, it was extremely complex, particularly in calling for three separate enforcement agencies: a public procurement regulatory board, a regulatory authority, and a rules committee. The Government has now decided to amend the law. An EAR-financed consultant is now drafting the amendment. EAR is also financing the drafting of the law's implementing regulations and plans to finance a training program to support their implementation. The latter would consist of a series of periodic training courses for staff of the major line ministries, along with the development of a procurement training module in the Kosovo Institute of Public Administration.

But one-on-one mentoring by experienced procurement specialists will be required through this consultancy to ensure that the new procurement system is implemented as intended. In agreement with the EAR, the technical assistance grant will therefore finance international consultants to provide this assistance. Specific institutions will be selected, in consultation with the PISG, based on their responsibility for implementing procurement for critical, high-value public investments and their readiness to allocate dedicated resources to achieve high performance in their procurement operations. Likely candidates include the Ministries of Health, Transport, and Public Services.

Scope of Work

The objective of this assignment is to build capacity for procurement in a uniform and coherent manner in key line ministries, consistent with the newly revised LPP and procurement regulations. The work under the project should be organized in three subcomponents, corresponding to the three key line ministries identified previously. The consultant assigned to one of the components will also serve as a project team leader and will meet on a regular basis with the other procurement advisors and with the Public Procurement Agency to ensure the application of a methodology that is consistent across ministries.

The procurement activities under this assignment will include: (a) procurement planning; (b) preparation of bidding documents (with basic technical input provided by the line ministries); (c) bid evaluation; and (d) preparation of contract agreements. In the course of mentoring local procurement staff, the consultant will carry out at least two full procurement procedures in each ministry.

At the end of their assignments the advisors will be required to demonstrate that the officials of the ministries receiving the assistance are in a position to carry out their functions without external support.

Required Outputs

- An annual procurement plan for each ministry, consistent with the revised LPP and its implementing regulations
- Bidding documents for at least two tenders in each ministry; along with the evaluation reports and contract agreements for those tenders.

- Recommendations for further procedural reforms and/or training in procurement.

Liaison and Reporting Requirements

The project team leader will report to the director of the Public Procurement Agency, who will be responsible to the Minister of Finance and the Permanent Secretary and will report on a regular basis. At the end of the second month the team leader will submit an inception report showing a work plan of significant tasks to be undertaken during the contract period, acceptable to the Ministry of Economy and Finance In addition (s)he will submit short (maximum 3 pages) monthly updates of the inception report to the Permanent Secretary and the Steering Committee which will show achievements over the previous month, work program for the next month and problems encountered, as well as progress toward achieving the goals set in the inception report. At the end of the contract (s)he will submit a final report on work undertaken which will include recommendations for future work and development in the area of procurement.

Monitorable Indicators of Performance

The success of the Advisers will be judged by the delivery of the Required Outputs. In addition the following indicators will be of importance:

- evidence of close collaboration with advisers working under other contracts of the PEMTAG and with other advisers supporting public sector reform in Kosovo;
- satisfactory progress toward goals set out in the inception report as described in the previous section;
- close cooperation and communication established between the MFE and individual ministries in the area of procurement;
- Clear indication that skills have been transferred to local officials

Consultants' Qualifications

The project team leader should have an advanced degree in engineering, law, or business administration, at least ten years of experience at a senior level in government procurement and a detailed working knowledge of World Bank and other donor procurement procedures. The other advisers should have at least 5 years experience and have a working knowledge procurement techniques. It is desirable that the advisers in the three line ministries have experience in the ministry's area of sectoral responsibility.

Contract Arrangements

The assignment is foreseen for the period ______ – ______ for a total working period of 36 months (i.e. 12 months average per line ministry). The contract should cover all costs of travel, subsistence, interpretation and translation services and training. The authorities will provide office space, use of personal computer, general office supplies and funds for domestic travel required for the assignment.

Annex 15: TOR for Primary Health Care Restructuring

BACKGROUND

The United Nations Interim Administration Mission in Kosovo (UNMIK) has received a technical assistance grant to support the strengthening of public expenditure management. The grant will finance technical assistance and training to strengthen the capacity of the Provisional Institutions of Self Government (PISG) in budget formulation, budget execution, and procurement, as well as specific policy and procedural reforms in the health and transport sectors.

Kosovo has a tradition of a publicly provided health care system financed through social health insurance. Until 1989, the system was typical of those in the Balkan, central and eastern European region, dominated by the large "policlinics" and hospitals. As part of the former Yugoslav Republic, the health system was financed through a social health insurance system. In the years leading up to the war, systems began to decay. From 1989 the health system suffered significant decline. Large sections of the population were excluded from using the main systems and became dependent on a parallel network of services provided by NGOs on a voluntary basis or by the private sector.

Since the conflict, Kosovo has initiated important reforms in the health sector aimed at increasing access to health care, improving financial sustainability, and improving quality of care. Kosovo has made substantive progress in the following areas: (i) policy development and re-organization of services, with emphasis given to PHC and gradual integration of vertical structures in the health care system; (ii) training, through the development and implementation of new curricula for family doctors, nurses and health care managers; (iii) infrastructure, with most health facilities refurbished and re-equipped; (iv) development of a Health Information System (HIS) although still in the design stage; (v) initiation of a modern approach to continuing professional education; and (vi) upgrading of nursing education to bachelor level. Although progress has been attained, the ongoing health reform process still encounters many difficulties.

The challenges for the Kosovo health care reform have been daunting. They include a radical change in the objectives and organization of the health care system, in management structures, tools and practices, and in the training of health care professionals. Successes and difficulties have characterized the reform process. The main difficulties that remain are: (i) lack of adequate managerial capacity and tools, particularly at the local level; (ii) lack of implementing regulations governing the private sector, including the private use of public health facilities; (iii) lack of quality assurance strategies and systems; (iv) lack of capacity to address emerging health issues, such as adolescent and youth health; (v) unsustainable financing mechanisms for the sector as well as mechanisms to address weaknesses in efficiency, equity, and quality of health services; (vi) poor health indicators; (vii) unequal access to health care, including lack of integration of health services in the minority areas; (viii) shortage of doctors and nurses; (ix) lack of a comprehensive human resource policy; and (x) lack of reliable statistics. MOH, as shown by the recent report "Health and Health Care in Kosovo", is aware of the problems and of the need of urgent policies to address them, starting with the rapid growth of a largely unregulated private sector.

According to the 2004 Poverty Assessment, in general, the provision of health services is quantitatively reasonable, but some important barriers to access exist, particularly for the poorest, the elderly, and the disabled. The health services network, both at primary health care (PHC) and secondary/tertiary care levels, is quantitatively adequate and geographically well distributed. However, in some cases, there is a lack of medical and nursing staff to ensure effective accessibility to PHC services. In addition, a limited number of areas need better infrastructure for tertiary care, including equipment and training. The main barriers to access to health services include, inter alia: (i) limited functioning of PHC in rural areas; (ii) costs - including informal payments and drugs that should be provided by the system but are not; (iii) lack of confidence by the public in the health system, particularly at the primary level. In principle, health facilities are accessible to everybody regardless of ethnicity. MOH supports a few small hospitals and health facilities run by Serbian health personnel. However, most of the Kosovar Serbs utilize a parallel health system directly subsidized by Serbia and Montenegro, which does not report to MOH.

Public health expenditures are relatively low. According to Government estimates, in 2003 public health expenditures were 4.4 percent of GDP, which is below the regional averages and well below the neighbor countries with the exception of Albania. Prospects for 2003-5 are for a very small increase of public expenditure in absolute terms (less than 5 percent in three years).

Private health expenditures as a proportion of total private consumption is relatively low on average. A notable proportion of households, particularly among the poorest, incur catastrophic expenditures. Because of the use of different survey methods, estimates of private health expenditures show substantial variation, ranging from 1.6 percent of GDP based on the 2002-3 HBS, to 3.4 percent based on the 2000 LSMS. Based on recent data, private health expenditures average Euros 7.05 per month, which corresponds to 1.9 percent of the total household consumption.

The benefits of the system of universal coverage practiced in Kosovo are compromised by inefficiency and corruption that cause undue out-of-pocket expenditures. According to the Poverty Assessment, the cost of drugs account for 65 percent of private expenditures, but a high proportion of these out-of- pocket payments are for drugs that are supposed to be provided for free, or that are not essential and, therefore, should not be prescribed. Informal payments are also widespread and affect the poorest population. The rapidly growing private sector undermines efforts to improve service delivery and does not guarantee better quality of care. Private sector regulation is thus a priority to avoid further leaking of resources from the public sector and to protect consumers from poor quality.

OBJECTIVES AND EXPECTED RESULTS

The health component will support the Ministry of Health to initiate improvements in service delivery by introducing in demonstration municipalities, the family medicine model of primary health care and performance based incentives focusing on quality, efficiency and access to PHC. These efforts will represent important steps towards financial sustainability of the health care system and support the analytical, planning and management capacity at the central and municipality level to improve the chances for sustainability of future health reforms.

The health component will have three sub-components: (i) Primary Health Care Restructuring, (ii) development and test performance based payment mechanism, and (iii) skills development. This TOR refers to the first of these subcomponents.

SCOPE OF WORK

With support from the European Agency for Reconstruction (EAR), MOH has been implementing a 2 and 3 year training program for family doctors. As of the end of June 2004, more than 400 physicians have received this training. In addition with support from Finland, training for family medicine nurses is being provided. One important achievement of the physicians training is that the program was accredited by the

Royal College of Physicians of the UK. However, changes in the organizational model of PHC are yet to be developed to ensure that the principles of the family medicine model are implemented in the PHC.

The TA will support development and implementation of the following tasks:

- Review of legislation and drafting of necessary amendments to allow for family medicine implementation, including introduction of performance-based payment mechanisms for PHC to provide incentives for efficiency. Since these reforms are new, the current management capacity and infrastructure do not allow for full implementation of these changes and therefore it is essential to identify gaps and make necessary changes.

- Development and implementation of micro and macro organizational changes. The transition to the family medicine model would require changes in the internal organization of health centers as well as redistribution of staff and tasks. The current organizational model of delivery system is highly fragmented within the health centers and can not adequately accommodate for full implementation of the family medicine model. Therefore, it is essential that local plans are developed and implemented that would facilitate internal restructuring and relocation of staff. The family medicine model would be based on teams rather than on dispensaries.

- Changes in the flow of patients and patients-doctor relations. The family medicine model requires systematic planning and proactive outreach towards disease prevention. The current practice of queuing in without an appointment system in place prevents family medicine teams to adequately plan and organize their activities and to devote adequate amount of time for individual patients. Development of an appointment system should be based on phone or in person scheduling with allowance for emergency interventions as needed. In addition, adequate record keeping of patients and family members will be developed at the level of a family medicine team which will promote better patient-doctor relations.

- Development of guidelines for disease management and disease prevention and standards for practical use in primary health care. Clinical protocols and therapeutic guidelines will be developed for about 20 most common diseases to standardize treatment and preventive activities at the primary care level. Special emphasis will be put on clear instructions for the family medicine teams on how to organize preventive services for their population. Working groups comprising of staff from the Institute of Public Health (IPH), university, hospitals, PHC, medical associations and MoH will be established for this purpose. The guidelines will serve as a basis for contracting and assessment of quality standards. Also they will serve as a basis for the development of family medicine annual work plans.

- A media campaign to promote patients registration with a doctor of their choice (once the previous steps have been completed). The family medicine model requires that a family medicine team serves a defined population in the municipality. In this regard, communication activities will support information and awareness of the public at large regarding the new model of service delivery and encourage registration of the population with a family doctor of their choice.

DURATION OF ASSIGNMENT

It is estimated that task (i) would take 2 months of international and 8 months of local consultants, (ii) 2 months of international and 8 of local consultants, (iii) 1 month of international and 2 of local consultants, (iv) 1 month of international and lump sum for working groups, and (v) 1 month of international and 3 of local consultants.

EXPERIENCE AND QUALIFICATIONS

The assignment would require multi-sectoral expertise including public health, health planning and management, legislation, and communications. The consultants would have to have experience with successful implementation of similar assignments and change management processes in similar economic and organizational settings, preferably from the ECA region.

OUTPUTS

Within the provided framework, the consultants will deliver the tasks as described above and prepare quarterly and a final report on completed activities. Before finalizing the final report, the consultants will prepare a draft report to be finalized when comments are received from MOH. The report will be provided in English and with translated copies in Serbian and Albanian.

Annex 16: TOR for Development of Performance Based Payment Mechanism

BACKGROUND

(Same Text as Annex 15)

PROBLEM DESCRIPTION

The current flow of public health funds includes two types of disbursements: (i) the central level health budget to the Ministry of Health (MOH), who pays health facilities and programs and (ii) the PHC health allocation directly to municipalities. The Ministry of Finance (or of Health Care in collaboration with PHC providers) is responsible for implementation. At the municipality level, around 80 percent of spending is financed by central government allocations for primary health care, education and general spending, which are nominally driven by formulas. About 20 percent is paid by own resources. In theory, the health grant commission defines the annual PHC budget allocated to municipalities based on the population size, the "fair share financing" rule to ensure adequate financing of minority communities, the territorial characteristics, and the number of health facilities. In reality, the final amounts are negotiated by the commission members and derive from the theoretical formula-driven amounts. The current input-based flow of health funds from the MOF to the MOH and to municipalities does not provide the opportunity to set incentives for expenditure management in the public sector. The Health Care Commission Agency (HCCA) is responsible for contractual arrangements between MOH and health providers. However, HCCA encounters serious limitations in playing this role.

Compared with neighboring countries, Kosovo spends a similar percentage of the total government budget on health, but gets less health outcomes for the money. The limited public health finance envelope should thus be allocated to improve efficiency in the provision of care and the population's health status.

Utilization rates in PHC facilities seem to be low, considering that only 47 percent of the women interviewed in the 2003 DHS reported visiting a health facility for either themselves or their children in the last 12 months. HIS diagnostic hospital information suggests that PHC facilities do not fulfill their gate-keeper and referral function. Consequently, a relevant proportion of hospital contacts are requested for problems that should be dealt at the PHC level, pointing to efficiency gains by PHC centers playing their gate-keeper role.

SCOPE OF WORK

The objective of the assignment will be to change the current health allocation system from the MOF to municipalities to include a performance-based element that rewards providers for contributing to improve quality of care, and efficiency in the provision of care. The work will build on the experience of an earlier provider payment pilot designed with support from the Bank-financed Education and Health Project.

The technical assistance will work with MOH to further define, design, test, evaluate and plan for possible roll-out a new provider payment system, which harbors the incentives to improve effectiveness and efficiency of patient treatment at the primary health care level and reduces unnecessary referrals to specialists and hospitals. In this connection, the consultants will:

(i) analyze the current provider payment mechanisms in use and design a provider payment system, develop specific contracts outlining goals, related indicators and performance benchmarks. The contracts will be based on newly developed guidelines under sub-component 1 emphasizing preventive services and will be consistent with legislation in effect at the time of the assignment;[14]

(ii) identify information needs/flow and help adjust the existing health information system designed with EAR financing in support of preparation, implementation and evaluation of new provider mechanisms at demonstration sites. This task will support data collection and a management system on resource allocation, cost and utilization of health services;

(iii) train HCCA, other staff and participating providers in the essentials of the new system, including development of training programs and materials and delivery of formal and on-the-job training. This will promote change from input to performance-based incentives and allocation of resources;

(iv) provide guidance and support during implementation to ensure:

- the analytical capacity to set performance targets to define a performance-based allocation of health funds for primary health care facilities; to interpret results on provider performance against benchmarks specified in the contracts and specify payments for family medicine teams;
- To communicate providers' performance results to ensure transparency, accountability and to increase peer-pressure for better performance;
- Systematic identification and correction of weaknesses in the overall process

(v) evaluate pilots at six months intervals, with a final evaluation during the last year of project implementation.

DURATION OF ASSIGNMENT

It is estimated that task (i) would require 4 months of international and 6 months of local consultants, (ii) 2 months of international and 3 local consultants, (iii) 5 months of international consultants, (iv) 4 months of international and 3 months of local consultants and (v) 2 months of international and 4 months of local consultants.

EXPERIENCE AND QUALIFICATIONS

This assignment requires a team of health systems management and payment specialists with substantial prior experience in the design, implementation, monitoring and evaluation of new provider payment mechanisms, including prior experience in this area in other transition economies. Prior knowledge of the health care systems of countries of former Yugoslavia is a plus.

It is expected that the consultant will provide a team of highly qualified specialists (health economist/ health care provider payment specialist, health specialist, practice manager and accounting specialist). The consultant may combine two or three areas of expertise in one specialist, provided the proposed specialist has the relevant qualifications and experience in all areas. All international experts are expected to have a minimum of 7 years experience in their area of expertise.

OUTPUTS

[14] Under the Kosovo Health Insurance Law, currently under consideration in Parliament, the volume and content of services to be contracted will be defined by a specific program approved by Parliament.

Within the provided framework, the consultants will deliver the tasks as described above and prepare quarterly and a final report on completed activities. Before finalizing the report, the consultants will prepare a draft report to be finalized when comments are received from MOH. The report should be delivered in English and translated copies in Serbian and Albanian.

Annex 17: TOR for Strengthening the Financial Sustainability of the Road Sector

BACKGROUND

The United Nations Interim Administration Mission in Kosovo (UNMIK) has received a technical assistance grant to support the strengthening of public expenditure management. The grant will finance technical assistance and training to strengthen the capacity of the Provisional Institutions of Self Government (PISG) in budget formulation, budget execution, and procurement, as well as specific policy and procedural reforms in the health and transport sectors.

The road network in Kosovo amounts to an estimated 8,500km, comprising 647km of main, or Magisterial, roads, 1,304 km of secondary roads, 571 km of city roads and approximately 6,000 km of rural roads, of which the vast majority of the latter is unpaved. The main and regional road network has been estimated to carry 60 percent of all vehicle journeys. There is little robust data on the quality of the road network, but one recent study[15] estimated that 35 percent of the paved network required reconstruction or rehabilitation, and that 97 percent of the unpaved network requires upgrading. It is also estimated that all bridges and structures are in need of urgent repair, with the exception of those that have been recently constructed.

The responsibilities for managing and maintaining the road network in Kosovo are split between the Ministry of Transport and Communications (MTC) of the Kosovo Provisional Institutions of Self Government (PISG), which is responsible for the Main and Regional road network, and the 30 Municipalities, which are responsible for local roads. Within the MTC, the programming of maintenance is the responsibility of the Department of Roads (DOR), with the supervision of works being undertaken by an implementing agency, the Directorate of Roads (DIR). The split of responsibilities between these two units was formalized in an Administrative Instruction dated September 8, 2003.

The funding for the maintenance of the road network is allocated to the MTC, as part of its overall budget, by the Ministry of Economy and Finance (MFE) from the Kosovo Consolidated Budget (KCB). A recent study for the World Bank[16] concluded that the present allocation was insufficient to meet the maintenance and rehabilitation needs of the sector. The overall funding requirement for the whole network is estimated at €14 million per annum for routine maintenance and €48 million per annum for rehabilitation, suggesting a total annual funding requirement for the whole road network of €62 million. The current expenditures were estimated as amounting to €15 million for MTC and some €11.8 million at the Municipal level, suggesting a current funding gap of some €35 million per year.

The earlier study made a number of recommendations to try and close this funding gap, and this technical assistance has been provided to assist the MTC and the MFE to confirm the earlier analysis and define a detailed action plan to introduce those recommendations.

OBJECTIVES

The primary objective of this assistance is to assist the MTC and the MFE to define a detailed action plan to introduce defined mechanisms to address the funding gap in recurrent expenditures in the road sector in Kosovo.

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[15] Roughton International (2004) *Kosovo Urgent Road Project – Road User Charges Study*, A study undertaken for the World Bank.

[16] Roughton Intl. (2004) *Ibid.*

The following represent the secondary objectives of the assistance:

- To review and confirm the analysis contained in the earlier study in terms of current revenues and expenditures, potential needs, and the estimated funding gap, in the sector;
- To identify/confirm appropriate measures to address that gap, in terms of changes in the structure and level of road user charging system, introduction of transit taxes, increases in fuel duty and vehicle registration taxes;
- To confirm the earlier assessment of the impact of the recommendations, in terms of ability to pay of firms and individuals in Kosovo;
- To develop capacity in the MTC to update the analysis in future, and use the Road User Charges Model of the World bank; and
- To detail an action plan, agreed with all official stakeholders, of the legislative and procedural changes necessary to introduce these measures.

THE SCOPE OF THE ASSISTANCE

The assistance is being provided to establish a system, which achieves cost recovery, on a user-pays basis, and provides for sustainable and secure road needs financing. It is expected this will include confirmation of the previous analysis of current road user cost recovery and infrastructure user charging, for all road classes. The primary concern is to achieve and secure adequate levels on maintenance and rehabilitation funding in the short term, with development needs to be considered as a longer-term option once the loan financing is available.

The following represent the specific activities envisaged to be required to meet these objectives:

Task 1 A comprehensive review of the earlier Road User Charges Study

The consultant should review, confirm and update the analysis contained in the earlier road user charging study.

Task 2 The identification of current and potential financing needs

The consultant should identify potential recurrent and capital funding requirements, based on the comprehensive assessment of the condition of the road network and associated structures, which is to be undertaken by the MTC in the spring of 2005, and estimate the current and future funding gap in the sector in terms of financing requirements, under a number of realistic scenarios. This review should also consider the elements to be included in a common accounting framework for assessing the various road infrastructure costs at a national level (principally internal costs at this stage).

Task 3 A review of the current Road User Charging System

The consultant should review the principles to be used in calculating road costs and review and describe in detail the current system for road user charging in Kosovo. This review should cover the revenue from the current system, the equity of the system, in terms of the overall objective of cost recovery for each vehicle class.

Task 4 An assessment of the effectiveness and coverage

The consultant should also, in collaboration with the Kosovo Police Force, consider the effectiveness of the current system, including an assessment of the extent of avoidance, on the part of users, and the revenue implications, and an assessment of the effectiveness of current sanctions, in terms of recovery of imposed fines for individuals and firms.

Task 5 The identification of suitable measures
The consultant should confirm/identify clear recommendations to address the funding gap, and achieve the objective of cost recovery for each user class. The scope of the recommendations is expected to focus on the structure and level of road user charging system; the enforcement regime and the scale of the legal sanction; and the introduction of appropriate transit taxes. This will also include and reflect an assessment of the affordability of each of the recommendations. The consultant should also review and recommend appropriate changes in terms of the scale of road user charges necessary, if the environmental and social externalities of road use, consistent with EU transport policy, are to be included in the road user charging system in future.

Task 6 The definition of an Action Plan
The final task is the development of a detailed action plan, agreed with all stakeholders, of the requisite legislative and procedural changes necessary to introduce these measures, together with a timetable for their introduction.

In developing the recommendations in terms of the structure and scale of the system of road user charges, the following, *inter alia*, EU requirements and guidelines are to be considered:

- Minimum rates of tax (registration charges) for heavy goods vehicles are stipulated in Council Directive 1999/62/EC. This directive also covers tolls and user charges;
- Council Directive 1999/62/EC specifies maximum values of user charges reflecting the damaging effects of heavy axle loads; and
- Minimum rates of fuel tax are stipulated in Council Directives 92/81/EEC and 92/82/EEC, as amended respectively by 94/74/EC and 96/1/EC.

Other related activities

There are a number of complementary activities in the sector, and the consultant should make contact and liaise with the responsible parties for the following activities:

- MTC and UNMIK EUPILLAR jointly initiated the gradual development of a transport policy framework and a multi modal transport approach in mid 2004, a project that will be continued till Spring 2005;
- Assistance is provided to MFE in 2005 to "Strengthen the Strategic Planning and Budget Process", MTC being one of the line Ministries involved;
- There will be a parallel project on Optimizing the Institutional Framework to facilitate the introduction of the Private Sector in the Provision of Transport Infrastructure;
- A comprehensive assessment of the condition of the road network and associated structures to be undertaken in early 2005; and
- Technical assistance to strengthen the Road Information Database and the use of economic evaluation (including HDM4) in the management of the road network.

Expected outputs

The Consultant shall produce the following outputs, which will be delivered in Albania and English, in four (4) hard copies, for the initial outputs, and ten (10) hard copies for the draft final and final) to the MTC as the implementing Ministry, and to both the MTC and the World Bank in soft copy, by e-mail and CD:

a) **An Inception Report**, 4 weeks after contract signing, providing the detailed planning and associated timetable for the work;

b) **An Interim Report**, 10 weeks after contract signing, including the review of the findings of the previous report, the estimate of the capital and recurrent financing needs of the sector, and the review of the current road user charging system in Kosovo;

c) **A Draft Final Report,** 20 weeks after contract signing, presenting the final analysis/ results/recommendations and detailed action plan from the work; and

d) **Final Report,** which will be due no later than 2 weeks after the receipt of client comments on the draft final.

Rresources required for the work

The consultant is expected to maintain a presence in Kosovo for the period of the assignment, and office facilities, comprising a desk, space and access to the telephone network will be provided by the MTC. The following represents a provisional assessment of the attributes of the individual sought for this position:

Team Leader/Transport Economist. This person should have at least 10 years experience in the practice of transport economics. The individual must have excellent written and oral communication skills in the English language, and have the experience in the policy and practice of determining road user charges necessary to convince senior policy makers of their recommendations. Work experience in a government road authority would be advantageous, but not essential. Familiarity with EU Infrastructure pricing policy and Directives, as well as World Bank guidelines would be considered necessary.

Annex 18: Outline Terms of Reference for other Transport Technical Assistance

Traffic Engineering / Transport Planning Advisor (9.5 person-months)

The traffic engineering / transport planning advisor will assist Transport Department staff over a two year period (2006 and 2007)[17] on the following tasks:

- Conducting an organized program of traffic data collection and development of a tactical traffic assignment model.
- Preparing a costed 5 year traffic circulation improvement program (comprehensive corridor improvements, isolated intersection improvements, bus priority measures, measures to improve pedestrian safety) including specifically low cost signing and marking to be implemented under the project.
- Preparing a plan and prioritized program for implementing paid parking in the city center, including a parking program to be implemented under the project.

The same advisor will provide advice to the Municipality of Pristina and the MTC on the following tasks:

- Reviewing mid-term and long-term transport investments with a view to determining their relative priority, their likely interaction, and their feasibility taking into account likely funding levels.
- Creating an urban transport unit within the Ministry of Transportation and Communications to provide guidance on traffic management, parking, public transport, and road maintenance and rehabilitation to urban areas of Kosovo which are not able to staff fully competent transport departments.

Traffic Signals Specialist (4.0 person months)

The traffic signals specialist will, based on circulation plans developed under the guidance of the traffic engineering advisor:

- Prepare a costed 5 year traffic signalization program.
- Design and prepare specifications and bidding documents for installation of traffic signals under the project.

Public Transport Advisor (2.5 person-months)

[17] This advisor might start work during 2005 if the Transport Department staff is increased as proposed and suitable office space is provided.

The public transport advisor will provide advice to the Transport Department by:

- Reviewing and making recommendations on the route structure, ticketing and transfers, and pricing.

- Preparing a scheme for introducing multi-year competitive concessions or contracts for the provision of services as a means of improving service quality and the quality of vehicles.

Annex 19: Terms of Reference: Assistance to Grants Unit Treasury Dept.

Job Description

The Financial Management Specialist (FMS), will work under the guidance of the Director and Assistant Director of Treasury.

The main responsibility of the Financial Management Specialist will be to ensure that all fiduciary duties with regard to designated donor grants are adhered to in particular World Bank grants. The FMS will also be responsible for mentoring staff in the unit and for development of unit job instructions and check lists.

In this context the duties will be as follows:

- Develop on the job instructions and check lists for all activities of the DDG unit;
- Mentor staff in the unit so that the unit will be self sustaining within 12 months;
- Liaise with the World Bank, implementing agencies, UNMIK and Treasury regarding all matters pertaining to DDGs;
- Ensure that all accounting records and bank accounts are up-to-date using the Kosovo financial management information system (KFMIS).
- Ensure payments are made to suppliers, contractors and consultants in a timely manner and in accordance with contract conditions.
- Every quarter, or in accordance with the terms of DDG agreements, and in coordination with the relevant implementing agencies, ensure that Project Management Reports (PMRs) are submitted to donors and UNMIK.
- Undertake education and information sessions for the various parties to DDGs as required;
- Make arrangements for audit by independent auditors where this responsibility falls to the DDG Unit;
- Create and maintain a comprehensive correspondence filing system to underpin the operations of the DDG unit;
- Assist the implementing agencies in financial and budget planning for the relevant projects;
- Resolve financing and budgeting problems related to DDGs; and
- Any other activities as requested by the Director and Assistant Director Treasury.

Main Qualifications

- Qualified Accountant, (or similar qualification) with at least 3 years related experience.
- Experience in carrying out accounting and auditing work, application of internal control systems and procedures.
- Experience with donor organizations.

- Experience in computerized accounting system, including applications of Microsoft Excel/Word or similar programs.

Annex 20: Documents in the Project File

European Agency for Reconstruction Support to the Ministry of Economy and Finance, Public Investment Programme. 2005. Project Inception Report. Draft.

Helm Corporation and Public Administration International. 2004. Kosovo Civil Service: Proposed New Pay and Grading System. Final Report.

IMF. 2004. Kosovo: Preliminary Findings on Budget Processes.

IMF. 2003. Staff Visit to Kosovo: Concluding Statement.

McCool, C., et al. 2003. Limited Scope Assessment of Local Governance in Kosovo: Recommendations for USAID/Kosovo's 2004-2008 Strategic Plan.

The World Bank. 2004. Kosovo: Economic Memorandum

The World Bank. 2002. Kosovo: Supporting the Provisional Institutions of Self Government-A Policy Note on Economic, Fiscal and Sector Priorities.

The World Bank. 2004. Kosovo: Operational Financial Accountability Review.

The World Bank. Kosovo: Operational Procurement Review.

United Nations Interim Administration Mission in Kosovo and The Provisional Institutions of Self-Government. 2004. Kosovo: Standards Implementation Plan.

Health Sector

Transport Sector

BCEOM. 2004. Kosovo Urgent Road Project Road Safety Improvement Study, Report for the World Bank, Kosovo Urgent Road Project

Roughton International. 2004. Road User Charges Study -Report for the World Bank, Kosovo Urgent Road Project

European Commission. 2002. CARDS Assistance Programme to the Western Balkans, DGExtRel

TRL/DFID. 1998.Guidelines for the Design and Operation of Road Management Systems, Overseas Road Note 1

United Nations. 2004. Kosovo *Urgent Road Project: Consulting Services for Road User Charges by Roughton Internationa*l. Final Report.

Annex 21: Statement of Loans and Credits

Project ID	FY	Purpose	Original Amount in US$ Millions: IBRD	IDA	SF	GEF	Cancel.	Undisb.	Difference between expected and actual disbursements: Orig.	Frm. Rev'd
		Total:	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

KOSOVO
STATEMENT OF IFC's
Held and Disbursed Portfolio
In Millions of US Dollars

		Committed				Disbursed			
		IFC				IFC			
FY Approval	Company	Loan	Equity	Quasi	Partic.	Loan	Equity	Quasi	Partic.
	Total portfolio:	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

		Approvals Pending Commitment			
FY Approval	Company	Loan	Equity	Quasi	Partic.
	Total pending commitment:	0.00	0.00	0.00	0.00

Annex 22: Country at a Glance

Kosovo at a glance

POVERTY and SOCIAL	Kosovo estimates	Europe & Central Asia	Lower-middle-income
2003			
Population, mid-year *(millions)*	1.9	473	2,655
GNI per capita		2,570	1,480
GNI *(millions)*		1,217	3,934
Average annual growth, 1997-03			
Population *(%)*	..	0.0	0.9
Labor force *(%)*	..	0.2	1.2
Most recent estimate (latest year available, 1997-03)			
Poverty *(% of population below national poverty line)*	37	..	..
Urban population *(% of total population)*	37	63	50
Life expectancy at birth *(years)*	74	69	69
Infant mortality *(per 1,000 live births)*	35	31	32
Child malnutrition *(% of children under 5)*	..	..	11
Access to an improved water source *(% of population)*	61	91	81
Illiteracy *(% of population age 15+)*	6	3	10
Gross primary enrollment *(% of school-age population)*	95	103	112
Male	96	104	113
Female	97	102	111

KEY ECONOMIC RATIOS and LONG-TERM TRENDS

	1983	1993	2002	2003
GDP *(US$ billions)*	..	..	1.6	2.0
Gross domestic investment/GDP	..	..	34.5	29.3
Exports of goods and services/GDP	..	..	12.5	10.4
Gross domestic savings/GDP	..	..	-51.5	-47.5
Gross national savings/GDP	..	..		
Current account balance/GDP	..	..	-62.0	-56.2
Interest payments/GDP	..	..	..	..
Total debt/GDP	..	..	..	..
Total debt service/exports	..	..	..	..
Present value of debt/GDP	..	..	..	..
Present value of debt/exports	..	..	..	..

	1983-93	1993-03	2002	2003	2003-07
(average annual growth)					
GDP	..		1.2	3.1	..
GDP per capita	..		2.0	4.0	..
Exports of goods and services	..		..	..	..

STRUCTURE of the ECONOMY

	1988	1996	2002	2003
(% of GDP)				
Agriculture	20.4	28.8	..	..
Industry	47.4	33.8	..	..
Manufacturing	..	..	..	..
Services	32.2	37.4	..	..
Private consumption	..	..	96.9	96.1
General government consumption	..	..	14.6	17.9
Imports of goods and services	..	..	98.6	97.1

	1983-93	1993-03	2002	2003
(average annual growth)				
Agriculture	..	..	..	..
Industry	..	..	..	..
Manufacturing	..	..	..	..
Services	..	..	..	..
Private consumption	..			
General government consumption	..			
Gross domestic investment	..			
Imports of goods and services	..			

Note Data are estimates for Kosovo