

**PEN ANALYTICAL BRIEF**

# Way ahead with IPA

Assessing Kosovo's  
absorption  
capacity



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## Assessing Kosovo's absorption Capacity

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Pen Strategy Consulting Group  
Str. "Rexhep Luci" 16/1  
Prishtinë 10 000, Kosovë



[www.penandgroup.com](http://www.penandgroup.com)  
[office@penandgroup.com](mailto:office@penandgroup.com)

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## Introduction

The approval of the Action Programme for 2016 in December 2016 pointed the passing of the halfway mark for the current segment of the Instrument for Pre-Accession Assistance (IPA), the so-called IPA II, stretching from 2014 to 2020. During the last decade, Kosovo has received almost a billion euro in assistance from the European Union, with the specific purpose of preparing it for an eventual Membership.

However, despite this long-standing commitment, Kosovo still remains far from that moment. Progress has been made, yet even more is needed to reach the ultimate goal. This moment is perfect for some reflection. How effective has IPA been so far?

Is Kosovo making a good use of the European assistance? Furthermore, has it the actual capacity to do so? These questions remain as crucial for the future development of the country as they were when IPA was first launched.

This paper tries to tackle those issues with a view on the future. To do so, it starts with a historical review of IPA and its current setup, including the latest developments in the case of Kosovo. Afterwards, it introduces the concept of absorption capacity, analyzing its implications for Kosovo. Based on that review, it extracts some lessons derived from the past experience.

## Instrument for Pre-Accession Assistance: Review and evolution

The IPA is a tool by which the European Union supports reforms in countries which are considered part of the enlargement strategy of the Union through financial and technical assistance.<sup>1</sup> It was launched in 2007, replacing several different preexisting programs.<sup>2</sup>

The financial and technical assistance offered through IPA helps increasing the capacities of candidate and prospective candidate countries during the enlargement process. By assisting these countries in reforming their political and economic systems, it prepares them to effectively assume the rights and obligations that come with EU membership. IPA I lasted for the period 2007 – 2013, with a budget of around €11.5 billion.<sup>3</sup> Assistance took place through five components, two available to all beneficiaries (Transitional Assistance and Institution Building and Cross-Border Cooperation), and three available only to candidate countries (Regional Development, Human Resources Development and Rural Development). This was in line with an underlying logic of preparing those countries for an eventual Membership, in which their administrations should be ready to efficiently manage a vast amount of resources resulting from cohesion funds and different schemes, such as the Common Agricultural Policy.

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<sup>1</sup> Current beneficiary countries are Albania, Bosnia-Herzegovina, the Former Yugoslav Republic of Macedonia, Kosovo, Montenegro, Serbia, and Turkey. [http://ec.europa.eu/enlargement/instruments/overview/index\\_en.htm](http://ec.europa.eu/enlargement/instruments/overview/index_en.htm)

<sup>2</sup> These programs were PHARE, ISPA, SAPARD and CARDS. More information available at [http://ec.europa.eu/enlargement/instruments/former-assistance/index\\_en.htm](http://ec.europa.eu/enlargement/instruments/former-assistance/index_en.htm).

<sup>3</sup> [http://ec.europa.eu/enlargement/instruments/overview/index\\_en.htm](http://ec.europa.eu/enlargement/instruments/overview/index_en.htm).

IPA II was launched in 2014 to cover the period of 2014-2020 with a budget of €11.7 billion. The IPA II regulation came into force on 16 March 2014 and applies retroactively from 1 January 2014.<sup>4</sup> It abandoned the narrow, accession-focused approach, replacing it with a broader action, revolving around administrative and economic reform. As such, the component-based framework disappeared, erasing all differentiation between candidate and potential candidate countries. According to the Commission, the 'most important novelty of IPA II is its strategic focus', meaning it is integrated into the broader EU action vis-à-vis the beneficiary country. Furthermore, IPA II gives more weight to performance measures, as indicators agreed with the beneficiaries will help assess whether the expected results have been achieved.<sup>5</sup>

It targets reforms in pre-defined sectors, which cover areas closely linked to the EU's enlargement strategy. This sector approach allows for more targeted assistance, according to the Commission, 'ensuring efficiency, sustainability and focus on results.'<sup>6</sup>

IPA II pursues the following four specific objectives:

- (a) support for political reforms;
- (b) support for economic, social and territorial development;

- (c) strengthening the ability of the beneficiaries to fulfill the obligations stemming from European Union membership by supporting progressive alignment with, implementation and adoption of the Union *acquis*;<sup>7</sup>
- (d) strengthening regional integration and territorial cooperation.

Furthermore, the IPA II Regulation states that financial assistance shall mainly address five policy areas:

- a) reforms in preparation for Union membership and related institution and capacity building,
- b) socio-economic and regional development,
- c) employment, social policies, education, promotion of gender equality, and human resources development,
- d) agriculture and rural development,
- e) regional and territorial cooperation.<sup>8</sup>

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<sup>4</sup> Regulation (EU) No 231/2014 of the European Parliament and of the Council of 11 March 2014 establishing an Instrument for Pre-accession Assistance (IPA II), Official Journal of the European Union, 15 March 2014,

[http://ec.europa.eu/enlargement/pdf/financial\\_assistance/ipa/2014/231-2014\\_ipa-2-reg.pdf](http://ec.europa.eu/enlargement/pdf/financial_assistance/ipa/2014/231-2014_ipa-2-reg.pdf).

<sup>5</sup>

[http://ec.europa.eu/enlargement/instruments/overview/index\\_en.htm](http://ec.europa.eu/enlargement/instruments/overview/index_en.htm).

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[http://ec.europa.eu/enlargement/instruments/overview/index\\_en.htm](http://ec.europa.eu/enlargement/instruments/overview/index_en.htm).

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<sup>7</sup> The *acquis* is the body of common rights and obligations that is binding on all the EU member states. European Commission, *Enlargement, Acquis*, available at:

[http://ec.europa.eu/enlargement/policy/glossary/terms/acquis\\_en.htm](http://ec.europa.eu/enlargement/policy/glossary/terms/acquis_en.htm).

<sup>8</sup> European Commission, *Instrument for Pre-Accession Assistance (IPA II), Indicative Strategy Paper for Kosovo\* (2014-2020)*, 20/08/2014, p. 3,

[http://ec.europa.eu/enlargement/pdf/key\\_documents/2014/20140919-csp-kosovo.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2014/20140919-csp-kosovo.pdf).

## Planning, Programming and Implementation

The process of planning and programming is now done through Indicative Strategy Papers, which are overarching strategic planning documents setting out the priorities and objectives for the seven-year period of the IPA. These Strategy Papers can be country specific or Multi-Country Strategy Papers.

Country Strategic Papers (CSP) provide the framework for the financial assistance to each of the individual IPA II beneficiaries. They identify key sectors where substantial reforms are needed for the beneficiaries to advance on the path towards EU membership. The CSPs also define the results that are expected to be achieved by the end of the IPA cycle, in 2020, the actions necessary to reach these results, as well as indicators that will allow for monitoring of the progress towards these results.<sup>9</sup> Multi-Country Strategic Papers (MCSP), on the other hand, set the priorities and conditions for horizontal support to sector policies and reforms, regional structures, and networks, regional investment support, as well as territorial cooperation including cross-border cooperation programs.<sup>10</sup>

The priorities outlined in the CSPs and MCSPs are then translated into detailed actions including in annual or multi-annual Action Programs. The IPA II Action Programs take the

form of financing decisions adopted by the European Commission.<sup>11</sup>

The implementation of IPA II funded activities is done in accordance with the Financial Regulation, which stipulates that implementation of the budget can take form under direct, shared or indirect management.<sup>12</sup> In direct management, the implementation of the budget is carried out directly by the European Commission. In the context of IPA, this method is used as long as the relevant national authorities are not yet able to manage the funds. Shared management, used only for cross-border cooperation, involves a Member State on the execution of the budget. Finally, indirect management entails a delegation of executive tasks to entities entrusted by the Commission.<sup>13</sup> For IPA projects, those are: the IPA II beneficiary or entity designated by it; an agency of an EU Member State or, exceptionally, a third donor country; an international organization; or an EU specialized agency.<sup>14</sup>

<sup>9</sup> [http://ec.europa.eu/enlargement/instruments/how-does-it-work/index\\_en.htm](http://ec.europa.eu/enlargement/instruments/how-does-it-work/index_en.htm).

<sup>10</sup> [http://ec.europa.eu/enlargement/instruments/how-does-it-work/index\\_en.htm](http://ec.europa.eu/enlargement/instruments/how-does-it-work/index_en.htm).

<sup>11</sup> [http://ec.europa.eu/enlargement/instruments/how-does-it-work/index\\_en.htm](http://ec.europa.eu/enlargement/instruments/how-does-it-work/index_en.htm).

<sup>12</sup> Regulation (EU, EURATOM) No 966/2012 of the European Parliament and of the Council of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, EURATOM) No 1605/2002, Official Journal of the European Union, 26 October 2012, <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2012:298:0001:0096:EN:PDF>

<sup>13</sup> Ibid, Article 58.

<sup>14</sup> [http://ec.europa.eu/enlargement/instruments/how-does-it-work/index\\_en.htm](http://ec.europa.eu/enlargement/instruments/how-does-it-work/index_en.htm).

## IPA Assistance to Kosovo

As Kosovo does not have a candidate status, it was only eligible for assistance under components I (Transition Assistance and Institution Building) and II (Cross-Border Cooperation) of IPA I. From 2007 to 2013, it was allocated a total of around €630 million, with €71.4 million allocated in 2013.<sup>15</sup>

For the cycle of IPA II, the European Union has allocated a total of around €645.5 million to Kosovo. The allocation for 2016 comprised €88.7 million.<sup>16</sup> Those funds are currently managed under the so-called direct management system, which implies that the EU Office in Kosovo (EUOK) channel them directly to the local beneficiaries without the intervention of the Government.<sup>17</sup> The IPA II Regulation foresees an indirect management system, in which the national authorities are involved not only in programming, but also in implementing the Instrument. The object is to improve ownership and to enable candidate countries and potential candidates to implement EU funds themselves and demonstrate their ability to assume the relevant responsibilities.<sup>18</sup>

According to the European Commission, the 'ownership of Kosovo institutions and the overall capacity to plan, programme, implement and monitor financial assistance

have significantly increased over the years', and 'staff at the Ministry of European Integration [MEI] is well-trained on EU-matters.'<sup>19</sup> However, 'the level of knowledge and expertise is less developed among other institutions, especially at the local level.'<sup>20</sup> To remedy this, a roadmap for indirect management of EU assistance should have been developed by 2015. Based on this roadmap, the government should 'upgrade existing structures and set up new ones to implement EU funds.'<sup>21</sup> The Commission also stated that if the sector approach, envisaged for IPA II, is to be applied in Kosovo, certain criteria have to be met and the government needs to put in place 'policies and strategies, medium-term budget frameworks, coordination and monitoring mechanisms, and arrangements that allow for the evaluation of results and impact.'<sup>22</sup>

At the time a certain consensus was formed within the Kosovo Government to push for sector budget support and postpone the transition towards indirect management until a later moment, closer to the end of the current IPA cycle, to avoid the backlog and inefficiencies usually associated with the local bureaucracy stepping in.<sup>23</sup> As a result, the 2016 Programme for Kosovo included direct budget support for the first time, with Public Administration Reform as a pilot field for its implementation.<sup>24</sup>

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<sup>15</sup> Communication from the Commission to the European Parliament and the Council, *Instrument for Pre-accession Assistance (IPA) Revised Multi-annual Indicative Financial Framework for 2013*, COM(2012) 581 final, Brussels, 10 October 2012, p. 9, [http://ec.europa.eu/enlargement/pdf/key\\_documents/2012/package/miff\\_adopted10-10-12\\_en.pdf](http://ec.europa.eu/enlargement/pdf/key_documents/2012/package/miff_adopted10-10-12_en.pdf).

<sup>16</sup> European Commission, *Indicative Strategy Paper for Kosovo\* (2014-2020)*, p. 37.

<sup>17</sup> Interview with EU Office official, 12 December 2014, Prishtina.

<sup>18</sup> European Commission, *Indicative Strategy Paper for Kosovo\* (2014-2020)*, p. 11.

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<sup>19</sup> Ibid.

<sup>20</sup> Ibid.

<sup>21</sup> Ibid.

<sup>22</sup> Ibid.

<sup>23</sup> Mrak, Mojmir and Kalaja, Arben, *Challenges for absorption of EU pre-accession funds in Kosovo under the Multiannual Financial Framework 2014 – 2020*, Kosovar Civil Society Foundation, March 2016, p. 19

<sup>24</sup> European Union Office in Kosovo, *European Commission grants EUR 70.5 million to Kosovo*, Press release, Brussels, 29 December 2016

## Absorption Capacity: Concept and implications for Kosovo

In the context of EU financing, absorption capacity has been defined as 'the extent to which a state (Member or non-member) is able to spend the allocated financial resources fully and in an effective and efficient way.'<sup>25</sup> Experience has shown that states' capacity to absorb external investment effectively and efficiently is limited.<sup>26</sup> Absorption capacity has three main elements:

1. **Macroeconomic absorption capacity:** defined and measured in terms of GDP. Experience in Central and Eastern European countries showed that they were able to process around 4% of the GDP in the best of cases, and usually far less than that.<sup>27</sup>
2. **Financial absorption capacity:** the ability to co-finance EU supported programs and projects, to plan and guarantee these national contributions in multi-annual budgets, and to collect these contributions from multiple partners involved in a particular program or project. In order to increase the incentive for their efficient use, EU structural assistance only finances a part of the total costs of a program or a project,

which means that there is a need for national co-financing.<sup>28</sup>

3. **Administrative/institutional absorption capacity:** the ability and skill of central and local authorities to prepare and select suitable plans, programs and projects in time, to arrange the co-ordination among principal partners, to meet the administrative and reporting requirements, and to finance and supervise implementation properly, avoiding irregularities as far as possible. This element has two components:

- a. On the *demand side*, administrative capacity is determined by the ability to generate new projects.
- b. On the *supply side*, it is determined by the ability of the country to manage the Structural Funds efficiently and effectively. This depends on things such as the assignment of responsibilities and tasks to institutions, the ability to estimate the required number and qualification of staff, the recruitment of appropriate staff, and the availability of various kinds of tools such as guidelines, manuals, etc. that may enhance effectiveness.<sup>29</sup>

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<sup>25</sup> Mrak, Mojmir and Tilev, Dragan, *Absorption for EU Pre-Accession Funds: Concept and Implications for Kosovo*, Forum 2015 and Kosovo Civil Society Foundation, April 2008, p. 30.

<sup>26</sup> Ibid.

<sup>27</sup> Ibid, p. 31

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<sup>28</sup> Ibid, p. 31-32.

<sup>29</sup> Ibid, p. 30-31.



Experience, both from the 12 EU Member States that joined the Union in 2004 and 2007 and the Western Balkan countries receiving assistance under IPA, show that institutional absorption capacity represented the major problem.<sup>30</sup>

The case of Kosovo is no exception, and so macroeconomic absorption has not become a problem so far, as the assigned funds have never come close to the established mark. In fact, for 2015, the last year for which GDP estimates are available, the assistance provided by IPA amounted to about 1.3% of it.<sup>31</sup>

Regarding financial absorption, assessing the capacity of Kosovo to meet the co-financing requirements requires a detailed, in-depth analysis of the yearly budget. For purely indicative purposes, the Action Programme for 2016 foresees a total investment of €71.150 million, of which €25.650 million are expected to be funded by the local authorities, making for a rate of 36%. Meanwhile, the budget of Kosovo for 2017, when the Action Programme is to be implemented, foresees revenue of €1.725 billion and €2 billion of expenses.<sup>32</sup>

Thus, as in most other cases, the main impediment at this point is the institutional capacity. In fact, it is here where Kosovo is still lagging behind the rest of the region in many areas.<sup>33</sup>

On the demand side, a certain institutional development has provided for an increased participation in the project design phase. Since 2012, a Department of Development Assistance has existed within the MEI with the specific mandate of coordinating the assistance received from the EU and other donors, fulfilling the role of National IPA Coordinator, working with other sectoral departments of the Ministry and the respective line ministries.<sup>34</sup> Still, coordination remains the main problem, despite the efforts to establish a strategic framework.<sup>35</sup>

However, while the situation has improved within the central level, it remains not so bright in the local one. A report by the Committee of Regions in 2014 found out that the municipalities in Kosovo were still predated by a lack of resources to meet the co-financing requirements, as well as of professional staff with the necessary knowhow to participate of IPA, with the situation being marginally better for the largest entities, resulting in an unbalanced use of European funds.<sup>36</sup> Furthermore, they suffered from the same lack of coordination. Nevertheless, the European Commission has recently noted some progress in that regard, which should provide for a certain development of the role of the municipalities within the IPA process.<sup>37</sup> However, this is a side effect of the ongoing general attempt at public administration reform in Kosovo, and a more pointed effort is needed.

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<sup>30</sup> Ibid, p. 49.

<sup>31</sup> The Action Programme for 2015 assigned €81 million of assistance. According to the World Bank, the GDP of Kosovo for that year was USD 6.401 billion, around €6.027 billion with an exchange rate of 0.9415 EUR/USD. <http://data.worldbank.org/country/kosovo>

<sup>32</sup> Law No. 05L-125 on the Budget of the Republic of Kosovo for the year 2017, 25 January 2017, p. 19 <http://mf.rks-gov.net/desk/inc/media/319C5CEF-38CF-4E34-A1F3-A581FC1DE627.pdf>

<sup>33</sup> Mrak and Kalaja, p. 15

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<sup>34</sup> <http://www.mei-ks.net/en/department-of-development-assistance>

<sup>35</sup> Mrak and Kalaja, p. 17

<sup>36</sup> Committee of the Regions, *The efficient use of funds for local and regional authorities under the IPA-II regulation*, November 2014, p. 33.

<sup>37</sup> European Commission, *Commission Staff Working Document Kosovo\* 2016 Report*, COM(2016) 715 Final, Brussels, 9 November 2016, p. 8

On the other hand, with regard to the supply side, the management of EU funds after the planning phase has proved so far less problematic than in neighboring countries, since Kosovo is still operating on a regime of Direct Management, where the EUOK is still executing the tendering, contracting and project monitoring, with a very limited intervention of the local institutions in this phase.<sup>38</sup> And this is so by desire, as the Government has been reluctant to initiate the transition towards indirect management. While this ensures a certain short-term stability, in the long-term this strategy is self-defeating, as said transition must necessarily take place before accession to the EU, and the planning is still at a very early stage.

Instead, the focus so far has been put on preparing the field for receiving the so-called direct budget support from the EU, a newly introduced modality of assistance in which funds are directly transferred to the budget of the receiving country for their use based on a strict conditionality as established in a Sector Reform Contract. To ensure access to the program, Kosovo had to overhaul its budgetary practices, including that proper transparency and oversight is set up, ensuring sustainability and establishing higher coherence between the yearly budget and the medium term framework.<sup>39</sup> While the effects of that are far reaching, since they are not limited to the implementation of assistance, affecting the whole use of public funds instead, it is still early to judge the degree of success of budget support. Close attention should be paid to the development of the programme, and Kosovo should be careful to ensure it does not delay the much needed transition towards indirect management.

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<sup>38</sup> Mrak and Kalaja, p. 19

<sup>39</sup> Ibid. p. 23

## Lessons learnt

### From a demand perspective:

*1. The strategic framework needs to be completed.*

Ensuring a proper planning is still critical. Although much work has been devoted in the last decade there are plenty of dysfunctions. More specifically, sectoral strategic planning is still non-harmonized, which prevents line ministries from using a common frame and reduces the overall coherence, which then turns into a lower capacity to design effective projects. To overcome this situation, the government should focus on homogenizing planning documents and procedures across the different organizations and levels of the administration.

*2. The role of the municipalities is still weak.*

So far, Kosovo has prioritized staffing and training officials at the central level. Consequently, while the Ministries now take an active part on project design, the municipalities are still struggling to come by with feasible projects under IPA. In the short term, the government should focus on offering assistance from the central level to the municipalities to identify, draft and co-finance projects while they build up their own teams. In the long term, the local financing framework needs to be completed, with a higher level of transfers and sufficient own resources for municipalities that ensure they can act independently.

### From a supply perspective:

*1. No preparatory work for a switch to Indirect Management has taken place yet.*

The current management method is not sustainable, and so far the strategy of the government has been to ignore the issue altogether, postponing sine die not only the switch as such, but even the planning for it. Transitioning from an EU managed implementation to a local one is not an easy task, as new structures need to be put into place, responsibilities shift between organizations and an extra burden is put to the administration. This is precisely why some long-term planning is required, involving all relevant stakeholders, including MEI, line ministries and municipalities. Starting now a debate does not imply an immediate implementation, but will ease it down the road, when it is up to Kosovo institutions to process IPA projects.

*2. The long sought-for budget support assistance is still at an early stage.*

Budget support is now on a pilot project phase. Only achieving this required an extensive effort, but this is just the beginning. For it to be extended to other fields, the respective frameworks need to be first defined, with clear priorities and long-term goals that can be translated into specific policies and aligned with the respective budgets. That demands a complete new level of cooperation between state organizations that was not been necessary to implement a project-based assistance. Eventually, it will require ensuring coordination with and between municipalities, which can prove challenging. Consequently, the government needs to take a proactive stance here, identifying any problem at an early stage and using that experience for future references.

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