



**ANNEX 2**

of the Commission Implementing Decision on the Annual Action Programme 2018 in favour of Georgia

**Action Document for EU4 Economic Governance and Fiscal Accountability**

**INFORMATION FOR POTENTIAL GRANT APPLICANTS**

**WORK PROGRAMME FOR GRANTS**

This document constitutes the work programme for grants in the sense of Article 110(2) of the Financial Regulation No 2018/486 and the action programme/measure in the sense of Articles 2 and 3 of Regulation No 236/2014.

<b>1. Title/basic act/ CRIS number</b>	EU for Economic Governance and Fiscal Accountability CRIS number: ENI/2018/041-405 financed under European Neighbourhood Instrument	
<b>2. Zone benefiting from the action/location</b>	Georgia The action shall be carried out at the following location: countrywide	
<b>3. Programming document</b>	Single Support Framework for EU support to Georgia 2017-2020	
<b>4. Sector of concentration/ thematic area</b>	Public Administration Reform, Public Finance Management	DEV. Aid: YES
<b>5. Amounts concerned</b>	Total estimated cost: EUR 18 640 000 Total amount of EU budget contribution: EUR 18 640 000 of which EUR 15 000 000 for budget support and EUR 3 640 000 for complementary support.	
<b>6. Aid modality(ies) and implementation modality(ies)</b>	Direct management: - budget support: sector reform contract; - grants – call for proposals; - procurement of services. Indirect management with an International Organisation (World Bank)	
<b>7 a) DAC code(s)</b>	15110 – Public sector policy and administrative management 15111 – Public finance management 15114 – Domestic revenue mobilisation	

<b>b) Main Delivery Channel</b>	Recipient Government - 12000			
<b>8. Markers (from CRIS DAC form)</b>	<b>General policy objective</b>	<b>Not targeted</b>	<b>Significant objective</b>	<b>Main objective</b>
	Participation development/good governance	<input type="checkbox"/>	<input type="checkbox"/>	X
	Aid to environment	X	<input type="checkbox"/>	<input type="checkbox"/>
	Gender equality (including Women In Development)	<input type="checkbox"/>	X	<input type="checkbox"/>
	Trade Development	X	<input type="checkbox"/>	<input type="checkbox"/>
	Reproductive, Maternal, New born and child health	X	<input type="checkbox"/>	<input type="checkbox"/>
	<b>RIO Convention markers</b>	<b>Not targeted</b>	<b>Significant objective</b>	<b>Main objective</b>
	Biological diversity	X	<input type="checkbox"/>	<input type="checkbox"/>
	Combat desertification	X	<input type="checkbox"/>	<input type="checkbox"/>
	Climate change mitigation	X	<input type="checkbox"/>	<input type="checkbox"/>
	Climate change adaptation	X	<input type="checkbox"/>	<input type="checkbox"/>
<b>9. Global Public Goods and Challenges (GPGC) thematic flagship</b>	GPGC #4: Democratization GPGC #7: Rich-poor gap			
<b>10. SDGs</b>	Main Sustainable Development Goal (SDG) #16: <i>Promote peaceful and inclusive societies for sustainable development, provide access to justice for all and build effective, accountable and inclusive institutions at all levels</i> Secondary SDG Goal #8: <i>Promote sustained, inclusive and sustainable economic growth, full and productive employment and decent work for all</i>			

#### SUMMARY

The general objective of the action is to reinforce economic governance and democratic accountability in Georgia. The specific objective is to strengthen fiscal governance through enhanced budgetary frameworks, external audit, independent monitoring as well as civic participation in and oversight of public finances.

The proposed action is in line with the two overall objectives of Sectors 1 and 2 of the Single Support Framework (SSF) for Georgia 2017-2020<sup>1</sup>, namely, support to structural reforms to improve economic governance (Sector 1) and to public finance policy processes as well as transparency, accessibility and quality of government services (Sector 2). The action also takes into consideration lessons learned and synergies from past and ongoing actions, including the EU-supported Public Finance Policy Reform, Public Administration Reform, Skills Development and Economic and Business Development programmes.

<sup>1</sup> Single Support Framework for EU support to Georgia (2017-2020): [https://eeas.europa.eu/sites/eeas/files/georgia\\_2017-2020\\_ssf\\_final.pdf](https://eeas.europa.eu/sites/eeas/files/georgia_2017-2020_ssf_final.pdf)

## 1 CONTEXT<sup>2</sup>

### 1.1 Sector/Country/Regional context/Thematic area

Georgia is a small developing economy with a population of about 3.7 million people and a gross national income (GNI) per capita of USD 3,864<sup>3</sup>. Over the past fifteen years, Georgia has undertaken significant economic, social and governance reforms resulting in, inter alia, progress in reforming the role of the state vis-à-vis the private sector, reducing corruption, and developing a more favourable environment for business. Sound fiscal and monetary policies supported by structural reforms strengthening supply-side dynamics also contributed to fostering economic growth, particularly in larger cities.

The effects of the global economic downturn in Georgia's main trading partners during 2013/2014 resulted in a decrease of exports and sharp depreciation of national currency. Despite such shock, Georgia has been able to regain macroeconomic stability and to progressively recover. Georgia's GDP increased by 5.0% in 2017, driven by external and domestic demand as well as investments. While GDP growth is expected to remain strong in 2018, current account deficit (8.6% of GDP in 2017 and around 10% of GDP expected in 2018) and external debt (114% of GDP in 2017 and 106% of GDP expected in 2018) are relatively high and represent a challenge to macroeconomic stability.

The political programme of the "Georgian Dream" coalition "Independence, Rapid Development, Prosperity" is the basis for policy formation after the October 2016 elections in which the Coalition maintained the majority of seats in the Parliament and then formed the new Government. The government programme is also reflected in the Basic Data and Directions (BDD) document (i.e. the country's medium-term budgetary policy document) which is approved together with the annual budget law by end-December each year.

The priorities in the 2018-2021 BDD include skills and labour market development, justice, and public administration reform. Sector priorities are based on the so-called "Four Point Plan" of the government, with strong emphasis on infrastructure development, which aims at addressing economic vulnerabilities and generating higher sustainable economic growth through strengthening private sector, public governance and education systems.

Within this policy context, the Georgian authorities recognise public finance reforms as a crosscutting element of economic policy, and a special emphasis is therefore put on the governance of public finances. The legal and institutional framework that defines the budgeting process at the state level ensures a certain coherence and consistency between

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<sup>2</sup> It should be noted that the Government, following the taking up of duties of a new Prime Minister on 19 June 2018, has reorganised its structure merging certain ministries and agencies. Whilst the new Government is fully committed to their process of political association and economic integration with the EU, individual policy areas may be subject to changes as notably reflected in a new Government Programme and as a consequence of new appointments as well as of merger and reorganisation of certain ministries and agencies. The implementation of the present Annual Action Programme will adapt to these changes while following the overall directions set out hereafter.

<sup>3</sup> Source: Geostat

policy priorities and budgetary allocations. The BDD policy objectives are being progressively reflected in the annual budget law which has also been gradually developed in the direction of programme budgeting. Increasing the quality and consistency between the programming and financial parts of the budget is however a long-term effort. In this context, improvements are also required in terms of reporting and monitoring. It is also worth noting that sector policies and priorities need to be better structured and integrated into a more coherent, comprehensive and comprehensible government policy.

### ***1.1.1 Public Policy Assessment and EU Policy Framework***

The EU is a leading partner of Georgia in the area of public finance and Georgia-EU collaboration via Budget Support programmes started in 2007, followed by a second phase in 2010. Building on shared interests and on increasing successful cooperation in this policy area, the most recent Georgia-EU programme was successfully completed in December 2017.

Over the last decade, Georgia has achieved significant progress in the area of public finance management, particularly with regard to the introduction of medium-term planning and policy based budgeting, modernising external audit according to the International Organisation of Supreme Audit Institutions (INTOSAI) standards, rolling out rules and procedures for the establishment of internal financial control and audit, taking proactive steps in increasing transparency and citizens engagement in the budget process, strengthening rules and procedures for fiscal discipline, revenue mobilisation and tax investigative functions. Georgia is often referred to as "frontrunner" of public management reforms in the Eastern Partnership region by international organisations based on its high scores in relevant international assessments (PEFA<sup>4</sup>, PER<sup>5</sup>, TADAT<sup>6</sup>) and reviews<sup>7</sup> of Georgia's public finance system.

The 2018-2020 policy priorities of the government are reflected in its so-called Five Point Reform Plan<sup>8</sup>. The plan is widely supported by international financial institutions and puts a strong focus on preserving macroeconomic and financial stability by reinforcing budgetary discipline, debt sustainability and fiscal space for selected public investment and social spending. Relevant measures also include a progressive reduction of budget deficit through a mix of expenditure and revenue measures as well as longer-term actions focused on capital market, pensions, public private partnership and support to private sector development.

**The Public Finance Management (PFM) strategy** of Georgia is well articulated in the different reform plans of the Ministry of Finance (MoF), the State Procurement Agency (SPA) and the State Audit Office of Georgia (SAO). It has undergone 3 phases (2007-2009, 2009-2013 and 2014-2017) and the government is currently elaborating the fourth one. As it is also recognised by the 2017 PEFA preliminary findings, over the past phases, the strategy

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<sup>4</sup> Public Expenditure and Financial Accountability

<sup>5</sup> Public Expenditure Review

<sup>6</sup> Tax Administration Diagnostic Assessment Tool

<sup>7</sup> <http://www.worldbank.org/en/news/feature/2015/02/18/georgia-an-e-procurement-success>,

[http://www.transparency.org/news/feature/corruption\\_perceptions\\_index\\_2016](http://www.transparency.org/news/feature/corruption_perceptions_index_2016)

<https://www.internationalbudget.org/opening-budgets/open-budget-initiative/open-budget-survey/country-info/?country=ge>

<sup>8</sup> [http://gov.ge/files/41\\_67105\\_252161\\_2018-2020programa\\_finalenl.pdf](http://gov.ge/files/41_67105_252161_2018-2020programa_finalenl.pdf).

contributed to improving the quality of policy and strengthening of institutions, with concrete results on the quality and transparency of public finances.

Following consultations with national and international stakeholders, the **2018-2021 PFM strategy** is at the final stages of elaboration under the steer of the Ministry of Finance (MoF). The strategy will cover the institutional development and include sub-sectoral strategies by the MoF and sub-ordinated entities<sup>9</sup>. The official approval of the strategy is pending the validation and formal approval of the 2017 PEFA review. The strategy document will summarise the results achieved so far (evidenced by the assessment of international organisations and business ranking agencies) and will include, inter alia, the deepening of reforms in the areas of i) management and result-orientation of budget and of public investment, ii) International Public Sector Accounting Standards (IPSAS)-oriented accounting and cash management reforms, iii) tax and customs harmonization with the EU acquis, iv) macro-fiscal planning v) public internal financial control and vi) supervision of the private sector financial accounting and reporting. The new PFM Strategy, which is to be published after the publication of the PEFA review, continues to benefit from the active participation of civil society and cooperating partners and will include a set of monitored performance indicators and a costed action plan. Furthermore, the PFM strategy remains an important component of the ongoing public administration reform (PAR) Roadmap and will contribute to the ongoing work led by the Administration of the Government for strengthening the overall monitoring and evaluation framework.

The coordination and monitoring of PFM strategies is ensured since 2011 by the PFM Inter-Agency Council (thereinafter, the PFM Council). The PFM Council is chaired by the Deputy Minister of Finance and includes representatives of line departments as well as of the State Audit Office, the State Procurement Agency and the Budget and Finance Committee of the Parliament. The PFM Council meets on a quarterly basis and its reports are made available online to Georgia's public and media.

**The Strategy of the State Audit Office (SAO) of Georgia for 2018-2021**, which was presented to stakeholders and adopted in December 2017, sets out five strategic objectives: i) independence and mandate ii) improving public finance governance through high quality audit work iii) strengthening accountability by fostering participation of national stakeholders, iv) improved efficiency of public finances through stronger governance and v) professional development of staff in line with EUROSAI standards. The Strategy acknowledges and highlights the importance that the Supreme Audit Institution of Georgia attaches to deepening the policy dialogue with the EU in a partnership framework further reinforced in the context of the preparation and implementation of this Action.

**The State Procurement Agency (SPA) has elaborated a Road Map 2016 - 2022** to ensure the gradual approximation of Georgian public procurement legislation with the EU acquis. The roadmap is still in discussion and a favourable opinion on the roadmap has not been agreed yet at the meeting of the Association Committee in Trade Configuration, as set out in article 145 of the AA. The document, albeit not covering EU standards on the award of

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<sup>9</sup> [Revenue Service Strategy for 2017-2020, following the IMF TADAT assessment. Guidelines for Public Internal Financial Control. Treasury PFMS and IPSAS reforms, establishment of fully fledged office and operations of SARAS.](#)

concessions and on remedies, determines the approximation in five phases as set out in the schedule in Annex XVI-B of the Association Agreement (AA). These five phases are distributed over a seven-year period in compliance with the phases and time schedules set out in Annex XVI-B of AA. The first phase covers the first three years after the entry into force of AA (2015-2017) and defines the activities to be undertaken by the SPA to meet the basic standards of the contract award principles of Article 144 of AA on "Publication", "Award of contracts rules" and "Judicial protection". Thus, approximation to these standards must ensure non-discrimination, equal treatment, transparency and proportionality. In order to meet the basic standards regulating the award of contracts required by Article 144 of the AA and to correct the abovementioned instances of non-compliance, the SPA prepared the draft amendments adopted by the Parliament in April 2017 (Amendments to the Public Procurement Law 617 II, 06/04/2017). The amendments are grouped into three main categories: basic principles, technical specifications and time limits.

Government policies in the sector also follow the provisions of the EU-Georgia Association Agreement (including a Deep and Comprehensive Free Trade Area, AA/DCFTA) signed in 2014<sup>10</sup>: Chapter 2 on 'Management of Public Finances and Financial Control', Chapter 3 'Taxation' Chapter 8 on 'Public Procurement', Annex 13 'Approximation of Customs Legislation'. To this end, the operational conclusions of the EU-Georgia Association Committee in Trade Configuration request the authorities to complete a set of actions in 2018 in the area of Customs, SPS (Sanitary and Phytosanitary measures), TBT (Technical Barriers to Trade) and Public Procurement.

The Parliament is in the process of gradually revising internal regulations and procedures to better reflect the enhanced mandate granted by the 2017 constitutional amendments. The authorities also recognise the need for improved financial oversight and follow-up of SAO recommendations. In this context, the EU Delegation is actively supporting policy dialogue and exchanges aimed at reinforcing the quality of reviews and follow-up of external audits and the participation of civil society in economic governance discussions. It is also worth noting that policy coordination and public participation also operate via the PFM Council which is open to Parliament Committee's members as well as to representatives of Civil Society Organisations (CSOs) and of the international community.

### ***1.1.2 Stakeholder analysis<sup>11</sup>***

The main stakeholders of the programme are the Ministry of Finance (MoF), the Budget Committee of the Parliament, the State Audit Office and the State Procurement Agency of Georgia. The Administration of the Government, which steers public administration reforms, is also closely associated with this programme.

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<sup>10</sup> Association Agreement between the European Union and the European Atomic Energy Community and their Member States, of the one part, and Georgia, of the other part, OJEU, L261, 30.8 2014.

<sup>11</sup> It should be noted that the Government, following the taking up of duties of a new Prime Minister on 19 June 2018, has reorganised its structure merging certain ministries and agencies. Relevant new state institutions have been reflected in this Annual Action Programme to the extent possible in August 2018. .

It is important to note that all main stakeholders commit to increase, via the implementation of this programme, transparency and accountability to the benefit of civil society organisations, media and the wider public. The publication of strategies and implementation reports as well as budget-related data (updated on a quarterly basis) will be continued on the MoF, Treasury, SAO and Parliament websites. The MoF and the PFM Council are committed to shift the focus from activity reporting towards better informing on results. The interactive IT modules (such as the budget monitor) will also be upgraded to enable better citizens' engagement during the audit planning and in monitoring the implementation of SAO recommendations.

Stakeholders also include bilateral donors (mainly USAID and some EU Member States) and International Financial Institutions (IFIs) involved in different forms of support to public finance reforms and, most importantly, civil society organisations which have been, and will be closely associated throughout the preparation and the implementation of this important governance programme.

This Action has been discussed with representatives of civil society organisations and they have at different occasions expressed their support for the undertaking of this programme. One of the main obstacles to a more active scrutiny of public finances is the complex nature of budgeting. It will thus be important to reinforce oversight and capacity also outside the Ministry of Finance. This will contribute to better informing and, therefore, empowering CSOs and professional associations with direct interests in different sectors (education, agriculture, health, etc.) in their activities related to public policy assessment and advocacy.

### ***1.1.3 Priority areas for support/problem analysis***

The Action is based on the success of the previous EU support programmes to Georgia. Past EU and international support has focused on putting in place the foundation of good public finance management practices and institutions. This Action enters into high level policy dimensions of public finances involving stronger checks and balances via improved economic governance and accountability.

Priority areas for support have been defined and confirmed also via sustained past and ongoing policy dialogue and analyses carried out by key stakeholders including the EU, the IMF and the World Bank (WB).

The preliminary findings of the 2017 PEFA assessment show that Georgia's PFM system benefits from a strong foundation following the implementation of consecutive PFM-related strategies and action plans. Aggregate expenditure management performance is in accordance with plans and, overall, information on performance in service delivery across the government sectors has been improved although more is needed in areas such as capital spending. Progress has been made also in the quality of Georgia's medium-term expenditure framework and programme budgeting although further progress is needed, for example, in terms of fiscal strategy (e.g., estimates of budgetary impact of policy changes, more timely reporting on fiscal outcomes, etc.). The revenue administration is relatively strong but some constraints remain, for example, in terms of arrears. A crosscutting positive feature of PFM-related reforms in Georgia has been the development of information technology (IT) in

budget preparation and execution (accounts, commitment control, and cash management), personnel and payroll management, revenue services and procurement.

An increasing amount of information has also been made public. The IMF Fiscal Transparency Evaluation<sup>12</sup> published in autumn 2017 notes that many elements of sound fiscal transparency practices are in place and Georgia meets the standard of good or advanced practice on 18 out of 36 principles and basic standards on a further 10 principles. Areas for improvement (remaining 8 principles) include: addressing the need for fiscal reports that show the complete picture of government finances; reconciling the change in the stock of the government's debt with the budget deficit, providing independent verification of the accuracy of the government's fiscal statistics and annual financial statements; reporting on performance against fiscal objectives; management of fiscal risks associated with public corporations and power purchasing agreements.

The IMF's 2016 TADAT Performance Assessment<sup>13</sup> also finds that Georgia is making good progress in implementing modern tax administration practices, particularly in using technology to modernise operations. Areas for improvement are identified as follows: organisation-wide weakness in operational planning and performance monitoring; flaws in the design and operation of the VAT refund system that result in accumulation of arrears, lack of control of the tax register; general failure to evaluate the impact of (legal) initiatives.

The World Bank's Public Expenditure Review (PER) 2017<sup>14</sup> build on previous PERs recommendations and highlights the need to consolidate spending through containing public wages, curtailing new programmes or extensions and improving efficiency in expenditure management (removing tax expenditures, increasing availability and affordability of medicines, standardizing service rates and introducing quality standards). The 2015 PER on Selected Fiscal Issues<sup>15</sup> also highlights the need for fiscal deficit reduction, rule-based compensation for public employees, strengthening the oversight of public investment, mainstreaming the quasi-fiscal operations of state owned enterprises (SOEs) into the budget and broadening and strengthening the expenditure and revenue decision-making authorities of sub-national administrations.

Looking ahead, further progress is needed for more inclusive policy development and dialogue on fiscal governance and accountability. This should include, for example, medium-term budgeting in particular with respect to the depth of analysis in the BDD, external audit and follow up of audit recommendations, managerial and internal control mechanisms for policy monitoring, public investment and assets management, Parliament's budget oversight, public procurement. Relevant recommendations released in recent and forthcoming assessments, including PEFA and OECD/Support for Improvement in Governance and Management (SIGMA) Policy Development baseline assessment against the Principles of

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<sup>12</sup> <http://www.imf.org/en/Publications/CR/Issues/2017/09/27/Georgia-Fiscal-Transparency-Evaluation-45274>

<sup>13</sup> <http://www.imf.org/external/pubs/cat/longres.aspx?sk=44213.0>

<sup>14</sup> <https://openknowledge.worldbank.org/bitstream/handle/10986/27138/114062-PER-P156724-PUBLIC-PERFINAL.pdf?sequence=1&isAllowed=y>

<sup>15</sup> <http://documents.worldbank.org/curated/en/116651467999346482/Georgia-Public-expenditure-review-selected-fiscal-issues>



Public Administration<sup>16</sup> will be taken into account in the preparation and implementation of ongoing and future Georgia-EU cooperation.

Finally, it is important to note that this Action will also support the oversight work of the Parliament and facilitate cooperation between the Parliament, the Supreme Audit Institution and the executive as well as more informed exchanges between those key institutions, the media and the civil society. In addition, this Action will support other important elements critical for economic governance such as a more comprehensive analysis to be made publicly available on the general government budget and regarding state-owned enterprises, and better quality of medium-term policy planning, costing and (financial and non-financial) performance information. While Georgia has made significant progress in the last 10 years, the need for further capacity and reform measures is acknowledged by all stakeholders in order to improve quality, result-orientation and accountability in the governance of public finances.

## **1.2 Other areas of assessment**

The following assessment is based on foregoing analysis and the track record with EU budget support operations in the country.

### ***1.2.1 Fundamental values***

Fundamental values of democracy and human rights are protected by the Georgian Constitution, in line with the main international standards. Georgia is considered to be a country adhering to the rule of law, although improvement is still needed in the areas of enforcement of judicial decisions and the independence of the judiciary. Freedom House assesses Georgia as "partly free". Both for political rights and civil liberties Georgia is assessed with the score 3/7 (1 being the best possible level).

### ***1.2.2 Macroeconomic policy***

Georgia's economy has shown strong resilience and continues to recover from the external shock. Overall, the authorities' macroeconomic policy has remained relevant and credible over the last election cycle (2014-2017). Georgia's GDP increased by 5.0% in 2017, driven by external and domestic demand as well as investments. GDP growth is expected to remain strong in 2018 and reach a similar level.

The macroeconomic outlook for Georgia remains vulnerable. The economy faces risks due to external imbalances (notably, a large current account deficit and significant external debt), as well as international reserves that remain below the adequate level.

The unemployment rate in Georgia (13.9% at end-2017) has been on a downward trend since 2009 (18.3%). However, it remains an important challenge, also for young people (around 28% unemployment in the age group of 15-24 years at end-2017). While employment opportunities have been created in new growth sectors, especially in tourism and other services, high unemployment persists due to challenges associated with skills mismatch and large regional disparities.

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<sup>16</sup> <http://www.sigmaxweb.org/publications/Baseline-Measurement-Report-2018-Georgia.pdf> - May 2018

Inflation reached 6.7% in 2017 as an impact of higher excises on tobacco, fuel and motor vehicles. To ease inflationary pressures, the central bank raised its refinancing rate three times in 2017: from 6.5% to 6.75% (in January), to 7% (in May) and to 7.25% (in December). The IMF projects that inflation will gradually decline to the 3% target by the end of 2018. Average inflation decreased to around 3% in the first three months of 2018.

The National Bank of Georgia (NBG) monitors closely exchange rate and inflation developments but the broad monetary stance is neutral. NBG remains committed to the exchange rate flexibility, limiting FX intervention to smoothing excessive volatility. The lari was broadly stable against the US dollar in 2017. However, the overall trend belied substantial intra-annual volatility: the lari appreciated against the dollar by around 12% from the beginning of 2017 until mid-August and lost this gain in the following four months. In 2018 until mid-May, the lari has appreciated against the US dollar by around 6%. This exchange rate volatility, coupled with the still high dollarisation (64% of deposits and 56% of loans were denominated in US dollars as of February 2018), makes Georgia's financial sector vulnerable to exchange rate risk.

An over-performance on the back of the faster-than-expected economic growth is expected to have allowed reducing the fiscal deficit of the general government to 3.9% of GDP in 2017, compared to 4.0% in 2016. The deficit is forecast to decrease slightly further in 2018. The level of Georgia's public debt was broadly stable in 2017 and 2016 (around 45% GDP in 2016) and is likely to remain at a similar level in 2018. The fiscal strategy of the Georgian authorities is based on further consolidation. Notably, the Georgian authorities plan to reduce current spending (a reduction in the wage bill and administrative expenses, efficiency gains in healthcare spending, and new spending controls on local governments), whilst increasing capital spending, mainly in infrastructure, and introducing a second (funded) pillar of the pension system. On the revenue side, the Georgian authorities increased taxes (notably, excise duties on tobacco products, vehicles and fuel) to compensate for revenue losses due to the corporate income tax reform that entered into force in January 2017

Georgia's balance-of-payments position remains vulnerable due to a large current account deficit (8.6% GDP in 2017 and around 10% GDP expected in 2018) and high external debt (114% GDP in 2017 and 106% GDP expected in 2018). The current account deficit is mainly driven by the trade in goods deficit, which is only partly offset by the trade in services surplus and income and transfers from abroad, including remittances. The inflows of foreign direct investment have been lower than expected in 2017 (10.5% of GDP) due to the fact that some large investment projects are nearing completion. Georgia's international reserves have been broadly stable in absolute terms since 2011, totalling USD 3.0 billion at end-April 2018 (less than 4 months of imports). However, reserve needs have been increasing (mainly due to the larger current account deficit, higher external debt and additional liquidity buffers warranted by dollarisation-associated risks in a floating exchange rate regime) and are currently below the level estimated by the IMF to be adequate.

Georgia's structural reform agenda, supported by the ongoing IMF programme and by the new macro-financial assistance (MFA) programme (see below), focuses on improving the business environment, education and public administration as well as investing in infrastructure. Additional measures include fiscal reforms (notably, improving the management of risks stemming from public-private partnerships and state-owned enterprises), strengthening of the financial sector (notably, introducing a deposit guarantee scheme and improving regulatory, supervisory and resolution frameworks for banks), as well

as the ongoing adaptation to the requirements of the Association Agreement with the EU, including the Deep and Comprehensive Free Trade Area.

The authorities have reaffirmed their commitment to macroeconomic priorities, fiscal consolidation and infrastructure investment and continue to benefit from an overall positive assessment from Bretton Woods Institutions. In this context, it is thus worth noting that the IMF completed the second review of its EFF (Extended Fund Facility) programme on 16 April 2018, and that the Council of the European Union adopted a decision on 12 April 2018 providing up to EUR 45 million in macro-financial assistance to help cover Georgia's financing needs, economic stabilisation and structural reforms.

### ***1.2.3 Public Financial Management (PFM)***

Overall monitoring of the PFM Reform Strategy is undertaken by the PFM Council chaired by the MoF. The implementation of the PFM-related strategies is done through action plans developed by the State Audit Office, MoF and the Budget and Finance Committee of the Parliament and progress on implementation is reviewed by the PFM Council.

As evident from many reviews and evaluations, including repeated PEFA reviews, PFM-related progress in recent years has contributed to improve policy outcome, dialogue and capacity in Ministries, State Audit Office and Parliament as well as overall transparency of Georgia's public finance system. See also sections 1.1 and 1.1.1 above for more information.

### ***1.2.4 Transparency and oversight of the budget***

The Open Budget Index (OBI) published end-January 2018 ranks Georgia as number five amongst all the assessed countries and demonstrates an increase of 14 points compared to the 2015 OBI score. In particular, Georgia makes all key budget documents publicly available online in a timeframe consistent with international standards.. Such progress puts Georgia ahead of other countries in the Neighbourhood and Western Balkans regions and confirms the impact of past and ongoing EU-Georgia policy dialogue and cooperation to deliver strong results in a critical governance area.

It can also be noted that the Parliament holds hearings on the SAO's annual report as well as the report on the execution of the state budget, and parliamentary hearings are carried out timely. The technical capacities of the Budget Office of the Parliament are progressing but more is needed also to provide more timely services to all relevant Committees.

As a direct result of the EU-Georgia policy dialogue and cooperation, the Ministry of Finance is now making a 'Citizen's Guide to the State Budget' publicly available in Georgian and in English languages thereby contributing to better inform citizens and the media on budget planning and priorities. It is also worth noting that the Government is following up on audit recommendations and has committed to increase transparency also by providing better information in the documentation annexed to the annual budget execution report submitted to the Parliament.

Main weaknesses relate to the oversight function of the Parliament, to public participation in the budget process and as regards the capacity of civil society organisation to engage in a substantive policy dialogue. Such weaknesses will be targeted by this Action thus strengthening opportunities for civil society and business associations to better engage budget decision-makers at national and sub-national levels.

## 2 RISKS AND ASSUMPTIONS

<b>Risks</b>	<b>Risk level (H/M/L)</b>	<b>Mitigating measures</b>
Macroeconomic instability, economic crises may divert authorities commitment/attention	L/M	Continuous policy dialogue with the government; monitoring of the macroeconomic situation; provision of financial and technical assistance.
Delays in the start and implementation of complementary measures (TA, grants)	L	EU Delegation takes timely actions to launch tenders and calls for proposals. Moreover, dialogue with the World Bank continues in a productive manner both at headquarter and at local levels.
High turnover of civil servants in line ministries involved in the programme implementation and limited technical capacity	L/M	Continuous policy dialogue with the authorities; reinforced analysis and regular monitoring of programme implementation; identification of key supportive measures, joint development of enabling policies and remedial actions
Evidence-based policy making and reporting remains a weakness across the line ministries.	M	Sustained and open policy dialogue focused on gradually improving evidence-based policymaking will continue to be part of high-level policy discussions as well as the direct involvement of international partners, civil society and media via this Action and via other Actions. Relevant policy dialogue and assistance is implemented also via the strategic framework on public administration reform including gradual strengthening of policy coordination and of evidence-based policy in line with OECD Principles of Public Administration
<b>Assumptions</b>		
The 2017 PEFA report, validated by the PEFA Secretariat, is published on the website.		
The updated PFM Strategy and action plan are developed by also taking into account the 2017 PEFA findings.		

The responsible authorities of Georgia, namely the Parliament, the Ministry of Finance and the State Audit Office, provide the commitment and the resources necessary to implement this Action.

### **3 LESSONS LEARNT, COMPLEMENTARITY AND CROSS-CUTTING ISSUES**

#### **3.1 Lessons learnt**

The programme builds on the success and lessons learnt of the previous programme Georgia - Support to Public Finance Policy Reforms (PFPR): Policy dialogue and cooperation confirm a good progress but point also to the need to move the dialogue to a higher, more political level and work on the checks and balances system. This includes a need to strengthen the capacity of the Parliament to fully exercise its oversight function on the budget and increase fiscal accountability.

Experience also highlights, on the one hand, the importance of being progressive in critical economic governance reforms and in the selection of a reduced number of annual measures but also, on the other hand, on the crosscutting importance of a sustained long-term commitment and policy dialogue.

Reforms in the areas of public finance have indeed been pursued, albeit with varying degree of success, by the responsible authorities and such reforms have contributed to the achievement of an internationally acknowledged solid foundation in public finance policy and management which, combined with continued stability-oriented macroeconomic policy and an improved business environment, have contributed to progressively improve the quality of the country's economic governance.

The progress in the EU-Georgia cooperation in this crosscutting governance area is also positively assessed by programme reviews and by the 2017 Thematic Evaluations on support to Public Administration Reform, including fiscal aspects of economic governance. Finally, it is worth noting that, despite recently publicised successes, the commitment of the authorities to further reforms in economic governance has not declined as evidenced also in the quality and openness of ongoing EU-Georgia policy dialogue and in the authorities' commitment to further improve the quality of dialogue and of our joint actions.

#### **3.2 Complementarity, synergy and donor coordination**

Coordination and policy dialogue are taking place in various formats, both government and donor led, varying according to the thematic area. Important platforms include the Association Committee and the sub-committees that provide the opportunity to strengthen the policy dialogue. Key institutions such as EU, Department for International Development (DFID), World Bank (WB), United States Agency for International Development (USAID), *Gesellschaft für Internationale Zusammenarbeit* (GIZ), Swedish International Development Cooperation Agency (SIDA) are involved in PFM-related areas. Apart from PFM Coordination Council meetings that are conducted on a quarterly basis, development partners meet internally on thematic topics. EU Member States are regularly consulted within the

"development counsellors meeting". Another platform for dialogue on selected fiscal issues is the IMF de-briefings organised under its programme reviews.

The parallel programmes implemented by development partners in the sector are as follows:

- GIZ and Swedish National Audit Office are supporting the SAO in sharing experience and practice on programme budgeting. GIZ also helps the Parliament to strengthen the financial oversight mechanisms and establish designated structures for scrutinizing audit reports. Germany is also helping the MoF in development of internal audit methodology according to IIA standards and working with the Revenue Service on audit related elements of the Tax Code.
- USAID is financing the Good Governance Initiative (GGI) in Georgia (2015-2020). The project objectives are to enhance overall transparency, accountability and effectiveness of the government, covering legislative and executive branches at the key levels.
- The World Bank's "Private Sector Competitiveness Development Policy Operation (DPO)", with a total amount of USD 50 million, targets private sector competitiveness and is implemented during 2017/2018. The second pillar of the programme establishes prior-actions to be taken by the government for financial sector deepening and diversification. Namely, introduction of a deposit insurance system, financial reporting and disclosure framework. A comprehensive pension reform that incentivizes savings in pension funds and harmonization of public procurement system to EU directives are also benchmarked. Furthermore, the "Second Programmatic Inclusive Growth DPO", with a total amount of USD 50 million, targets public administration reforms and is operational from April 2017. The prior actions under the first pillar include adoption of capital budgeting guidelines, establishment of a financial database for SOEs and the adoption of the new Law on Civil Services.
- The World Bank also allocated USD 0.5 million for the development of the IT audit at the State Audit Office. The project aims at investing in hard IT infrastructure as well as trainings of auditors in the respective field.
- The World Bank Public Investment Management (PIM) technical assistance project was implemented during 2016-2017 with the total amount 0.83 million. The action had two main phases/dimensions: i) support to establishing a regulatory basis for PIM, involving advice on improvements to regulations, procedures and methods; and ii) capacity building for application of new regulations, procedures and methods, involving strengthening the overall capacity to prepare, appraise and select projects, at both central government and local government levels. The first phase, mainly performed in FY16, focused on system-design activities involving development of an overall framework for managing public investments and setting the legal framework. The next phase, during FY17, involved preparing the ground for piloting of the new framework in select central ministries and municipalities, and then actual piloting. The IMF's Public Investment Management Assessment (PIMA) of 2018 will lay out the basis for next phase of assistance.
- The Asian Development Bank (ADB) is providing a TA in managing the dual challenge of maintaining government debt sustainability while setting up legal, regulatory, and institutional frameworks facilitating availability of long-term capital for productive

business and infrastructure investments. Key development issues to be addressed by the TA include enhancing generation of domestic savings, providing investment opportunities by developing money and debt markets, and managing public debt and fiscal risks better.

- The IMF generally does not implement specific TA projects but "structural benchmarks" related to fiscal governance are established under the 3-year Extended Fund Facility USD 285 million programme. The benchmarks are broadly in line with the WB DPOs and are focused on capital market development, pension reform, PPP framework, private sector governance and competition.

The list of the EU-funded projects that will complement this action includes:

EU-funded projects	EUR million	Duration	Complementarity with this programme
Institutional strengthening of the State Audit Office of Georgia	2.2	2017-2019	Strengthen institutional and operational capacity of the SAO in audit planning and reporting
Supporting Revenue Service of MoF in NCTS	1.5	2018-2020	Supporting accession to the Conventions on Transit Area and launching of the new Computerised Transit System
Public Administration Reform (PAR)	30.0	2015-2021	Pilot ministries will benefit in terms of improved strategic planning and policy development, monitoring and reporting capacity
Strengthening Parliamentary Democracy in Georgia (UNDP implemented)	3.3	2014-2018	Increased transparency of the Parliament's operation and Improved communication with the public; Development and implementation of the institutional reform of the Parliament of Georgia.

Significant envelopes are provided for Georgia under the CSO Component of the Development Cooperation Instrument (DCI); these will be geared towards increased participation of CSOs in fiscal governance, whether at sector level or for cross cutting fiscal matters.

### 3.3 Cross-cutting issues

All activities under the programme will be designed and implemented in accordance with principles of good governance, human rights and gender equality.

The action will strengthen the governance system and make roles, responsibilities, procedures and reporting more transparent. It will also strengthen national institutions involved in

auditing and financial oversight. The action will also enhance the anti-corruption efforts of the government, which in return, are essential for improved PFM record.

The objective of gender equality, to which Georgia is committed in its national policies as well as through its international commitments, is embedded in the programme at national policy level by disbursement indicators that include gender-specific targets where important differences exist between men and women. The complementarity measures, in particular concerning capacity building, will include gender mainstreaming in the budgetary process.

Tools for data gathering and analytical skills development will be promoted for a gender-based assessment of budgets, incorporating a gender perspective at all levels of the budgetary process, and restructuring revenues and expenditures in order to promote gender equality.

This action will indirectly address environmental issues. Increasing compliance with obligations under environmental conventions to which Georgia is a party and further approximation with EU's overall environmental policies and legislation requires adequate policy planning and PFM systems and capacities to optimise access to funds and their optimal use. The action will also contribute to the gradual integration of environmental and climate change commitments in the budgeting system via strengthening Georgia's medium-term expenditure frameworks and by reinforcing relevant capacity amongst key stakeholders. It is also expected that more efficient revenue mobilisation and expenditure will contribute to finance climate change-related interventions.

## **4 DESCRIPTION OF THE ACTION**

### **4.1 Objectives/results**

This programme is relevant for the Agenda 2030, the 2016 EU Global Strategy for the European Union Foreign and Security Policy<sup>17</sup> and the review of the European Neighbourhood Policy 2015<sup>18</sup> and contributes to fulfilment of the Association Agenda. It contributes primarily to the progressive achievement of SDG Goal 16, but also promotes progress towards SDG Goal 8. This does not imply a commitment by Georgia benefiting from this programme.

The **general objective** of the Action is to reinforce economic governance and democratic accountability in Georgia.

The **specific objective** is to strengthen fiscal governance through enhanced budgetary frameworks, external audit, independent monitoring as well as participation and oversight of public finances.

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<sup>17</sup> Shared Vision, Common Action: A Stronger Europe – A Global Strategy for the European Union's Foreign And Security Policy: [http://www.eeas.europa.eu/archives/docs/top\\_stories/pdf/eugs\\_review\\_web.pdf](http://www.eeas.europa.eu/archives/docs/top_stories/pdf/eugs_review_web.pdf)

<sup>18</sup> Joint Communication to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Review of the European Neighbourhood Policy, JOIN (2015) 50 final



The proposed Action is in line with the two overall objectives of Sectors 1 and 2 of the new Single Support Framework (SSF) for Georgia 2017-2020, namely, support to structural reforms to improve economic governance (sector 1) and to public finance policy processes as well as transparency, accessibility and quality of government services (sector 2).

It is envisaged that the Action will pursue the following **expected results**:

### **Result 1: Strengthened fiscal governance framework**

R 1.1: Fiscal governance strengthened through gradual alignment with Council Directive 2011/85/EU on requirements for budgetary frameworks.<sup>19</sup>

R 1.2: Improved budget coverage and credibility including through reinforced monitoring and inclusion of State-Owned Enterprises in published annual financial statements;

R 1.3: Improved transparency and accountability in fiscal governance at subnational level with a specific focus on inter-governmental fiscal transfers to local authorities;

R 1.4: Improved governance and accountability of taxpayer services;

R 1.5: Improved internal financial management and control system in line with EU PIFC guidelines.

### **Result 2: Strengthened independence and capacity of external audit**

R 2.1: Improved governance accountability including broadened audit coverage and enhanced independence of the SAO;

R 2.2: Strengthened delivery and communication on performance audits by the State Audit Office.

### **Result 3: Strengthened oversight of public finances**

R 3.1: Improved economic governance and oversight of the Parliament with priority given to strengthening the Budget and Finance Committee of the Parliament and to progressively operate a full-fledged Public Accounts Committee;

R 3.2: Strengthened participation of Georgia's civil society and business associations in the budget oversight of fiscal governance institutions, such as State-Owned Enterprises and public procurement, and areas required for gradual approximation with EU-oriented fiscal governance at national and subnational levels.

## **4.2 Main activities**

The main activities envisaged under Sector Reform Performance Contract (SRPC) are policy dialogue, capacity building, performance assessment and financial transfers. Such activities

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<sup>19</sup> <http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1517929530259&uri=CELEX:32011L0085>

support the implementation of the public policy and of the objectives and results described in this Action.

#### ***4.2.1 Budget support***

Budget support is proposed for the areas where a sound level of policy framework, coordination and ownership of the reforms has been shown. The main activities are geared towards policy targets that the Government will commit to achieve in relation to the policy areas and results described in section 4.1 above.

At this stage, it is foreseen that EUR 15 000 000 will be disbursed through fixed and variable instalments of budget support for conditions to be achieved during the 2019-2021 period. The amount defined for budget support is expected to impact on the fulfilment of the conditionality and to add leverage for policy dialogue.

#### ***4.2.2 Complementary support***

Complementary support is envisaged under indirect and/or direct management with international organisation<sup>20</sup> and grants (twinning) with the EU Member State respective institution for a high quality technical advice to the authorities for the implementation of this Action in relation to results mentioned in Section 4.1. Special attention shall be paid to institutional and operational capacities of the Budget and Finance Committee, the Public Accounts sub-committee and of other relevant bodies of the Parliament. Further, compliance reviews by independent experts and evaluation of the programme are planned.

In addition to the complementary support described in this Action Document, additional complementary support is expected to be deployed under the CSO-LA (local authorities) component of the DCI instrument, starting with Local Authorities in 2018, and addressing civil society subsequently to develop accountability and the capacity for civic participation in this domain.

### **4.3 Intervention logic**

The intervention logic of the programme is driven by the objective of better economic governance and accountability in Georgia. It is based on the 2016-2020 Four Point Plan of the government and strategies of the PFM institutions as well as Georgia's Association Agreement commitments.

The proposed intervention responds to the current gaps and needs in the economic governance framework of Georgia identified above. Different elements of financial governance of Georgia need to be elevated up to EU and international standards thus creating additional fiscal space for more efficient service delivery. This joint programme will also contribute to explaining and disseminating relevant expertise and practices related to EU economic governance and will offer a structured forum open to representatives of civil society and the Parliament to discuss not just amongst experts but also involving key stakeholders at national and subnational level. Special attention is also paid to support the oversight function of the Parliament having an enlarged mandate and responsibility in this critical governance area.

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<sup>20</sup> The implementing partner was selected on a competitive basis following a call for expression of interest during formulation phase.

As for Result 1 "strengthened fiscal governance framework": The action will streamline institutional set-up and procedures for monitoring fiscal risks through inclusion of state owned enterprises, enhancing policy planning and non-financial performance reporting in the budget framework, improved taxpayer services and private sector financial reporting, enhanced internal financial control systems and more transparent and predictable inter-governmental fiscal relations. In the long run, this will result in a more comprehensive, transparent and accountable system of state finances.

For Result 2 "strengthened independence and capacity of external audit": The action will support the SAO to exercise granted rights (appeal to the Constitutional Court, audit of budget revenues) and improve public awareness on quality and performance of public spending.

As for Result 3 "strengthened oversight of public finances": The establishment of a Public Accounts Committee dealing with monitoring of the implementation of SAO recommendations is envisaged. The budget oversight will also imply increased participation of civil society and business associations in the Parliamentary work that in the long run should lift the financial oversight up to EU standards.

In addition and contributing to all results, the programme will reinforce the credibility of supervision of public finances by supporting the development of a Fiscal Council in line with EU policies. In a medium-term framework, this action will contribute to reinforce credibility, accountability and public participation in relation to effectiveness and efficiency dimensions of economic governance.

The monitoring framework of the policy will aim to capture lessons learnt and facilitate feeding successful practices and approaches in the policy-making process. The national policy implementation will be supported by budget support as well as complementary measures. The effectiveness of the EU intervention will be assessed through indicators that measure policy implementation and concrete outcomes.

## **5 IMPLEMENTATION**

### **5.1 Financing agreement**

In order to implement this action, it is foreseen to conclude a financing agreement with the partner country.

### **5.2 Indicative implementation period**

The indicative operational implementation period of this action, during which the activities described in section 4.1 will be carried out and the corresponding contracts and agreements implemented, is 60 months from the date of entry into force of the financing agreement.

Extensions of the implementation period may be agreed by the Commission's authorising officer responsible by amending this decision and the relevant contracts and agreements; such amendments to this decision constitute technical amendments in the sense of point (i) of Article 2(3)(c) of Regulation (EU) No 236/2014.

## **5.3 Implementation of the budget support component**

### ***5.3.1 Rationale for the amounts allocated to budget support***

The amount allocated for the budget support component is EUR 15 000 000, and for complementary support EUR 3 640 000. This amount is based on the commitment of the partner country to allocate national budget resources (including EU budget support) for support to the (1) fiscal governance framework, (2) independence and capacity of external audit and (3) oversight of public finances. The amount is commensurate with the financing needs related to the reforms supported and will provide substantial leverage for the policy dialogue. All institutions concerned with the performance targets have demonstrated sufficient absorption capacity and a good track record in fulfilling the conditions under the previous EU funded budget support programmes. Overall, three instalments are planned. Instalments will be disbursed upon compliance with the general and specific conditions for the tranche release.

### ***5.3.2 Criteria for disbursement of budget support***

The general conditions for disbursement of all tranches are as follows:

- Satisfactory progress in the implementation of the economic governance and fiscal accountability and continued credibility and relevance of that of any successor strategy;
- Maintenance and implementation of a credible and relevant stability-oriented macroeconomic policy or progress made towards restoring key balances;
- Satisfactory progress in the implementation of reforms to improve public financial management, including domestic revenue mobilisation, and continued relevance and credibility of the reform programme;
- Satisfactory progress with regard to the public availability of timely, comprehensive and sound budgetary information.

b) The specific conditions for disbursement that may be used for variable tranches are based on government commitments and are the following:

- The medium term budgetary framework (Basic Data and Directions document) defines ongoing and new policy commitments;
- State owned enterprises are integrated in government's financial statements;
- Comprehensive non-financial performance information are delivered to the public for selected sectors;
- Taxpayer services and overall performance of the Revenue Administration has further improved;
- Internal Financial Management and Control system is functioning according to EU PIFC guidelines;
- Improved system for intergovernmental fiscal relations are established and functioning;
- Increased competences and implementation of SAO related constitutional guarantees
- State Audit Office further improves its governance, effectiveness and communication with stakeholders;
- Capacity established of an independent Fiscal Council;
- Improved parliamentary oversight;
- Strengthened participation of civil society and business associations in the oversight.

The chosen performance indicators and targets to be used for disbursements will apply for the duration of the programme. However, in duly justified circumstances, the Ministry of Finance of Georgia may submit a request to the Commission for the targets and indicators to be changed. The changes agreed to the targets and indicators may be authorised by exchange of letters between the two parties.

In case of a significant deterioration of fundamental values, budget support disbursements may be formally suspended, temporarily suspended, reduced or cancelled, in accordance with the relevant provisions of the financing agreement.

### ***5.3.3 Budget support details***

Budget support is provided as direct untargeted budget support to the national Treasury. The crediting of the euro transfers disbursed into Georgian Lari will be undertaken at the appropriate exchange rates in line with the relevant provisions of the financing agreement.

## **5.4 Implementation modalities for complementary support**

The envisaged assistance to Georgia is deemed to follow the conditions and procedures set out by the restrictive measures adopted pursuant to Article 215 TFEU<sup>21</sup>.

### ***5.4.1 Grants: indicatively 1 call for proposals for a Twinning Project for the implementation of activities under the Result 3 (direct management)***

(a) Objectives of the grant, fields of intervention, priorities of the year and expected results

The Twinning modality via call for proposals will be used for supporting the implementation of activities under Result 3:

- Improve Parliamentary capacity (Budget and Finance Committee and Public Accounts sub-Committee) to analyse draft budgets and audit reports, discuss expenditure policies and follow-up implementation of SAO and Parliament recommendations
- Support the establishment of the independent Fiscal Council
- Strengthen participation of CSOs and business organisations in the budget oversight and support reaching common understanding of their roles and responsibilities

(b) Eligibility conditions

In line with Article 4 (10)(b) of Regulation (EU) No 236/2014, participation in Twinning calls for proposals is limited to public administrations of the EU Member States, being understood as central or regional authorities of a Member State as well as their bodies and administrative structures and private law bodies entrusted with a public service mission under their control provided they act for the account under the responsibility of that Member State.

(c) Essential selection and award criteria

The essential selection criteria are financial and operational capacity of the applicant

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<sup>21</sup> [https://eeas.europa.eu/headquarters/headquarters-homepage/8442/consolidated-list-sanctions\\_en](https://eeas.europa.eu/headquarters/headquarters-homepage/8442/consolidated-list-sanctions_en)

The essential award criteria are relevance of the proposed action to the objectives of the call: design, effectiveness, feasibility, sustainability and cost-effectiveness of the action

(d) Maximum rate of co-financing

The maximum possible rate of co-financing for grants under this call is 100%<sup>22</sup>.

(e) Indicative timing to launch the call

3<sup>rd</sup> quarter 2019.

(f) Use of lump sums/flat rates/unit costs

Twinning contracts include a system of unit costs and flat rate financing, defined in the Twinning Manual, for the reimbursement of the public sector expertise provided by the selected Member State administrations. The use of this system of unit costs and flat rate financing, which exceeds the amount of EUR 60,000 per beneficiary of a Twinning contract, is authorised through the Commission decision C(2017)1122.

In case of failure in selecting and awarding the Twinning contract, the alternative implementation modality will be procurement of services.

	Type (works, supplies, services)	Indicative number of contracts	Indicative trimester of launch of the procedure
Strengthening the Financial Oversight Processes in the Parliament	Services	1	1 <sup>th</sup> quarter 2020

**5.4.2 Procurement (direct management)**

	Type (works, supplies, services)	Indicative number of contracts	Indicative trimester of launch of the procedure
External review missions	Services	1	4 <sup>th</sup> quarter 2019

**5.4.3 Indirect management with the World Bank under the umbrella of the Programmatic Trust Funds "EC-World Bank Partnership on Europe and Central Asia (EPP)"**

A part of this action may be implemented in indirect management with the World Bank. . This implementation entails improvement of the fiscal governance on budgetary frameworks and strengthening the independence and capacity of external audit thus supplementing actions of the authorities anticipated through the budget support operation.

<sup>22</sup> As provided for in the Twinning Manual

#### Activities under Result 1:

- Support authorities to align with 2011/86/EU directive on budgetary frameworks. These includes budgetary accounting/reporting, forecast for budgetary planning, fiscal rules for deficit debt and expenditure, budget process preparation with a medium-term budget framework, transparency.
- Support to consolidate public sector fiscal data in GFS format compliant with IPSAS. The activity would also imply ensuring completeness of nonfinancial asset data from local governments and SOEs and strengthening respective monitoring tools of MoF.
- Improve design and implementation of the equalization reform of intergovernmental transfers and introduction of new incentives for empowering local economic development initiatives.
- Improved governance of revenues and taxpayers' services. The support would target tax registration, VAT refund schemes, management of tax arrears and mechanism for evaluation of impact initiatives on taxpayers (satisfaction surveys, impact of audit and compliance mitigation programs).
- Improved internal financial management and control and audit systems, policies and procedures.

#### Activities under Result 2:

- Enhance the technical capacity of the SAO through integration of financial, compliance, performance and IT audit methodologies in the Audit Management Software; improved government reporting, statistics and data analysis; IT security procedures and software.
- Increase and sustain impact of the supreme audit work through effectively engaging with the Parliament and citizens.

This implementation modality is justified because the World Bank has the necessary organisational, human and management capacities as well as solid experience of financial sector reform in Georgia. The World Bank has a well-established policy dialogue with the Georgian authorities and key national stakeholders in the public finance system such as the MoF and SAO. In the sector, the Bank is already implementing the PEFA validation and assessment project at national and subnational levels through the Europe 2020 Programmatic Trust Fund.

The entrusted entity would carry out the following budget-implementation tasks: sub-contracting and/or hiring external experts.

If in the course of the negotiations with the World Bank it would prove to be more feasible to implement all or part of the above-mentioned activities in direct management mode under the Europe 2020 Programmatic Trust Fund, these activities would be implemented in accordance with the implementation modalities identified in section 5.4.4.1

If negotiations with the World Bank fail, the part of the action related to Result 1 and Result 2 may be implemented in direct management in accordance with the modalities identified in section 5.4.4.2 for procurement of services.

#### ***5.4.4 Changes from indirect to direct management mode due to exceptional circumstances***

#### 5.4.4.1 Grant: direct award to the World Bank (direct management)

Direct award may be used if in the course of the negotiations with the World Bank it would prove to be more feasible to implement all or part of the activities in direct management mode under the Europe 2020 Programmatic Trust Fund.

(a) Objectives of the grant, fields of intervention, priorities of the year and expected results

As defined in Section 4 above.

(b) Justification of a direct grant

Under the responsibility of the Commission's authorising officer responsible, the grant may be awarded without a call for proposals to the World Bank.

Under the responsibility of the Commission's authorising officer responsible, the recourse to an award of a grant without a call for proposals is justified because this action has specific characteristics requiring a specific type of beneficiary for its technical competence and specialisation.

The World Bank has the necessary organisational, human and management capacities as well as solid experience of financial sector reform in Georgia. The World Bank has a well-established policy dialogue with the Georgian authorities and key national stakeholders in the public finance system such as the MoF and SAO.

In the sector, the Bank is already implementing the PEFA validation and assessment project at national and subnational levels through the Europe 2020 Programmatic Trust Fund. Thus, deep knowledge and understanding of the economic governance context of Georgia, its strength and weaknesses is essential to engage in a highly technical policy dialogue and provide good quality expertise that the WB possesses.

(c) Essential selection and award criteria

The essential selection criteria are the financial and operational capacity of the applicant.

The essential award criteria are relevance of the proposed action to the objectives of the call; design, effectiveness, feasibility, sustainability and cost-effectiveness of the action.

(d) Maximum rate of co-financing

The maximum possible rate of co-financing for this grant is 100%.

(e) Indicative trimester to conclude the grant agreement

2<sup>nd</sup> trimester 2019.

#### 5.4.4.2 Procurement (direct management)

	Type (works, supplies, services)	Indicative number of contracts	Indicative trimester of launch of the procedure
Alternative to:	Services	2	3 <sup>rd</sup> quarter



5.4.3 Indirect management with WB; 5.4.4.1 Grant: direct award to the WB			2019
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## 5.5 Scope of geographical eligibility for procurement and grants

The geographical eligibility in terms of place of establishment for participating in procurement and grant award procedures and in terms of origin of supplies purchased as established in the basic act and set out in the relevant contractual documents shall apply subject to the following provisions.

The Commission's authorising officer responsible may extend the geographical eligibility in accordance with Article 9(2)(b) of Regulation (EU) No 236/2014 on the basis of urgency or of unavailability of products and services in the markets of the countries concerned, or in other duly substantiated cases where the eligibility rules would make the realization of this action impossible or exceedingly difficult.

## 5.6 Indicative budget

	<b>EU contribution (amount in EUR)</b>	<b>Indicative third party contribution, in currency identified</b>
5.3 - Budget support Sector Reform Performance Contract	15 000 000	N.A.
5.4.1 – Grants: call for proposals for up to 1 twinning for implementation of activities under the Result 3	1 140 000	N.A.
5.4.2 – Procurement: external review missions	100 000	N.A.
5.4.3 – Indirect management with World Bank - for the implementation of activities under the Result 1 and 2	2 200 000	N.A.
5.9 – Evaluation, 5.10 - Audit	200 000	N.A.

## 5.7 Organisational set-up and responsibilities

The action will be directly managed by the European Commission through its Delegation in Georgia. All contracts and payments are made by the Commission on behalf of the beneficiary. All initiatives will be conducted with the support and engagement of the authorities, civil society and development partners ensuring that implementation of economic governance policies is well coordinated.

The steering of the programme will be entrusted to the PFM Coordination Council under the MoF, which will oversee and guide the overall direction and policy of the programme. It will assess progress in the implementation of the action and decide if any modifications are

needed. It shall devote separate session on the implementation of this Action once a year and can be convened whenever the programme implementation requires strategic decisions.

## **5.8 Performance monitoring and reporting**

By the end of the first quarter of the year, the external review mission will submit to the EU Delegation an evidence-based technical report assessing the degree of compliance in line with mutually agreed conditions for disbursement.

The day-to-day technical and financial monitoring of the implementation of this action will be a continuous process undertaken in an inclusive manner by consulting key stakeholders and part of the implementing partner's responsibilities and of the EU operational manager. To this aim, the Ministry of Finance shall use the PFM Coordination Council as a permanent internal, technical and financial monitoring system for the action and elaborate regular progress reports (not less than annual) and final reports. The State Audit Office and the Parliament will provide inputs regularly for the progress report in an agreed format.

Every report shall provide an accurate account of implementation of the action, difficulties encountered, changes introduced, as well as the degree of achievement of its results (outputs and direct outcomes) as measured by corresponding indicators, using as reference the strategy, policy or reform action plan of the partner country (for budget support). For project modality, the report shall be laid out in such a way as to allow monitoring of the means envisaged and employed and of the budget details for the action. The final report, narrative and financial, will cover the entire period of the action implementation.

The Commission may undertake additional project monitoring visits both through its own staff and through independent consultants recruited directly by the Commission for independent monitoring reviews.

## **5.9 Evaluation**

Having regard to the importance of the action, a final evaluation will be carried out for this action or its components via independent consultants contracted by the Commission.

This final evaluation will be carried out for accountability and learning purposes at various levels (including for policy revision), taking into account in particular the fact that the programme targets two priority areas of cooperation within the SSF.

The Commission shall inform the implementing partner at least three months in advance of the dates foreseen for the evaluation mission. The implementing partner shall collaborate efficiently and effectively with the evaluation experts, and inter alia provide them with all necessary information and documentation, as well as access to the project premises and activities.

The evaluation of this action may be performed individually or through a joint strategic evaluation of budget support operations carried out with the partner country, other budget support providers and relevant stakeholders.

The evaluation report shall be shared with the partner country and other key stakeholders. The implementing partner and the Commission shall analyse the conclusions and recommendations of the evaluations and, where appropriate, in agreement with the partner

country, jointly decide on the follow-up actions to be taken and any adjustments necessary, including, if indicated, the reorientation of the project.

Indicatively, one contract for evaluation services shall be concluded under the framework contract in 2022.

### **5.10 Audit**

Without prejudice to the obligations applicable to contracts concluded for the implementation of this action, the Commission may, on the basis of a risk assessment, contract independent audits or expenditure verification assignments for one or several contracts or agreements.

Indicatively, one audit contract for audit services shall be concluded under the framework contract in 2022.

### **5.11 Communication and visibility**

Communication and visibility of the EU is a legal obligation for all external actions funded by the EU.

This action shall contain communication and visibility measures which shall be based on a specific Communication and Visibility Plan of the Action, to be elaborated at the start of implementation and supported with the budget indicated in section 5.4.2 above.

In terms of legal obligations on communication and visibility, the measures shall be implemented by the Commission, the partner country, contractors, grant beneficiaries and/or entrusted entities. Appropriate contractual obligations shall be included in, respectively, the financing agreement, procurement and grant contracts, and delegation agreements.

The Communication and Visibility Manual for European Union External Action shall be used to establish the Communication and Visibility Plan of the Action and the appropriate contractual obligations shall be included in the financing agreements or delegation agreements.

With regards to the Neighbourhood East, all EU-supported actions shall be aimed at increasing the awareness level of the target audiences on the connections, the outcome, and the final practical benefits for citizens of EU assistance provided in the framework of this action. Visibility actions should also promote transparency and accountability on the use of funds.

Outreaching/awareness raising activities will play a crucial part in the implementation of the action, in the case of budget support the national government shall ensure that the visibility of the EU contribution is given appropriate media coverage. The implementation of the communication activities shall be the responsibility of the implementing organisations, and shall be funded from the amounts allocated to the Action.

All necessary measures will be taken to publicise the fact that the action has received funding from the EU in line with the Communication and Visibility Manual for EU External Actions. Additional Visibility Guidelines developed by the Commission (European Neighbourhood Policy and Enlargement Negotiations) will be strictly adhered to.

Where relevant, the provisions of the Financial and Administrative Framework Agreement concluded between the European Union and the selected international organisations shall apply.

It is the responsibility of the implementing organisation to keep the EU Delegations and, where relevant, the Commission (DG NEAR), fully informed of the planning and implementation of the appropriate milestones specific visibility and communication activities.

The implementing organisation shall report on its visibility and communication actions, as well as the results of the overall action to the relevant monitoring committees.

This action will be communicated externally as part of a wider context of EU support to the country, and where relevant to the Eastern Partnership region in order to enhance the effectiveness of communication activities and to reduce fragmentation in the area of EU communication.

The implementing organisation shall coordinate all communication activities with EU Delegations as well as regional communication initiatives funded by the European Commission to the extent possible. All communication strategies developed as part of this action shall ensure they are in line with the priorities and objectives of regional communication initiatives supported by the European Commission and in line with the relevant EU Delegation's communication strategy under the "EU4Georgia" umbrella initiative.

**APPENDIX - INDICATIVE LIST OF RESULT INDICATORS (FOR BUDGET SUPPORT)<sup>23</sup>:**

	<b>Results chain</b>	<b>Indicators</b>	<b>Baselines (incl. reference year)</b>	<b>Targets (incl. reference year)</b>	<b>Sources and means of verification</b>
<b>Overall objective: Impact</b>	Reinforce economic governance and fiscal accountability in Georgia	Positive trend is confirmed via analyses and indicators included in relevant reports published by IMF, WB, OECD/SIGMA, Open Government Partnership and International Budget Partnership.	Georgia applies some elements of good or advanced principles linked to economic governance.	Georgia applies most elements of good or advanced principles linked to economic governance.	OECD/SIGMA, PEFA, IMF, WB, OBI reports

<sup>23</sup> Mark indicators aligned with the relevant programming document with '\*' and indicators aligned to the EU Results Framework with '\*\*'.

	Results chain	Indicators	Baselines (incl. reference year)	Targets (incl. reference year)	Sources and means of verification
Specific objective(s): Outcome(s)	To strengthen fiscal governance, through enhanced budgetary frameworks, external audit, independent monitoring as well as civic participation in and oversight of public finances	The values of SIGMA PA assessment report indicators	Completeness of financial estimates in sector strategies is equal to 1/5; Alignment between planned costs in sector policy plans and medium-term budget is equal to 0/3; Regulation and use of budgetary impact assessment prior to approval of policies is equal to 1/3 (2018)	Completeness of financial estimates in sector strategies is equal to 3/5; Alignment between planned costs in sector policy plans and medium-term budget is equal to 2/3; Regulation and use of budgetary impact assessment prior to approval of policies is equal to 2/3 (2021)	2018-2020 SIGMA assessment report
		The values of IMF fiscal transparency assessment indicators	Georgia does not meet the good practice of fiscal transparency principles of IMF in the areas of integrity and the quality of fiscal reports (2017)	Georgia meets good practice of fiscal transparency principles of IMF by improving the coverage, integrity and the quality of fiscal reports (2021)	2017 and 2022 Fiscal Transparency Reports;
		IMF TADAT performance indicator values	TADAT performance indicators linked with treatment of VAT claims, tax arrears, taxpayer registration, impact evaluation, are assessed as low (2017)	TADAT performance indicators are improved, linked with treatment of VAT claims, tax arrears, taxpayer registration, impact evaluation. (A or B score, 2021)	2016 TADAT assessment; 2020 TADAT assessment
		SAI PMF assessment indicator values	The performance of the SAO operates on a performance level of average between '1' and '3' (2017).	The performance of the SAO operates on a performance level of average between '3' and '4' (2021)	2021 SAI PMF assessment
		Open Budget Data	82/100 OBI (2017 score)	2018-2021 OBI scores are not downgraded	Open Budget Data

	<b>Results chain</b>	<b>Indicators</b>	<b>Baselines (incl. reference year)</b>	<b>Targets (incl. reference year)</b>	<b>Sources and means of verification</b>
<b>Induced outputs</b>	R .1: Strengthened fiscal governance framework/ progress in public finance policy reforms*	<p>Semi-annual reports on budget execution</p> <p>% of positive assessment in taxpayers' opinion surveys*</p> <p># of annual financial statements submitted to SARAS by the private businesses</p> <p>% of VAT refund claims that are repaid automatically subject to risk screening is increased compared to previous year.</p> <p>Application of 2<sup>nd</sup> pillar of FMC procedure and guidelines in X line ministries</p> <p>#/% of state owned enterprises reflected in annual financial statements;</p> <p>Quality and predictability of intergovernmental fiscal relations (IGFR)</p>	<p>Sectoral policies are not adequately reflected in the BDD (2017)</p> <p>The tax procedures and services are positively assessed by 71% of respondents (2017)</p> <p>0 (2017)</p> <p>0 (2017)</p> <p>0 (2017)</p> <p>0 (2017)</p> <p>IGFR requires improvement in terms of understanding and predictability at local level (2018)</p>	<p>Sectoral policies are clearly reflected in BDD for 2021-2024 (including gender indicators) for six sectors</p> <p>The tax procedures and services are positively assessed by 80% (2021) (VAT refund, tax audit and dispute resolution, financial reporting procedures)</p> <p>10% of private enterprises (2021)</p> <p>30% (2021)</p> <p>Half of the line ministries (2021)</p> <p>Large state enterprises are integrated and consolidated in quarterly budget execution reporting (2021)</p> <p>Improved understanding and transparency of IGFR at local level (2021)</p>	<p>BDD for 2019-2022 and sub-sequent years</p> <p>Business Perception Survey on Policy Reforms</p> <p>SARAS database</p> <p>Revenue Service reports</p> <p>Fact finding missions to line ministries</p> <p>State Budget of Georgia for 2019, 2020, 2021,2022 years</p> <p>Reports by independent experts and institutions.</p>

	<b>Results chain</b>	<b>Indicators</b>	<b>Baselines (incl. reference year)</b>	<b>Targets (incl. reference year)</b>	<b>Sources and means of verification</b>
<b>Induced outputs</b>	R.2: Enhanced independence and capacity of State Audit Office	Compliance rate by the government to SAO recommendations	GoG compliance rate 45% (2017)	60% (2021)	SAO annual reports
		Financial and performance audits conducted in security sector, public procurement, SOEs, LEPLs, quasi-fiscal institutions.	86 audit reports over the last 2 years;	200 audit reports during 2019-2021, at least 40 performance audit reports;	SAO website;
		Existence of external peer review of SAO/ EUROSAI alignment	n.a	Positive assessment/reflection (2021)	Peer Review report produced by the respective EU MS SAI
		Implementation of SAO related constitutional guarantees for independence and impartiality	n.a	Number of cases appealed to the Constitutional Court (2021)	Court files



	<b>Results chain</b>	<b>Indicators</b>	<b>Baselines (incl. reference year)</b>	<b>Targets (incl. reference year)</b>	<b>Sources and means of verification</b>
<b>Induced outputs</b>	R.3: Strengthened scrutiny and oversight of public finances	Establishment of Public Accounts Committee and its full operation  Number of Parliamentary Committee hearings devoted to SAO audit reports and number of issued recommendations to the government	Not existing  11 audit reports discussed; 3 Parliamentary Committee resolutions made on performance audit results	# of Parliamentary Committee resolutions (to foster implementation) made on all performance audit reports  At least 30 (from 200) of audit reports discussed by the Parliament.	Budget and Finance Committee reports; Pubic Accounts sub-Committee reports  Budget and Finance Committee reports; Pubic Accounts sub-Committee reports
	R4: Reinforced credibility in the supervision of public finances	Fiscal Council established and fully operational	Not existing (2018)	Fiscal Council publishes its first report in 2021 on the draft State Budget.	Fiscal Council Report

	<b>Results chain</b>	<b>Indicators</b>	<b>Baselines (incl. reference year)</b>	<b>Targets (incl. reference year)</b>	<b>Sources and means of verification</b>
<b>Direct outputs</b>	R 1.1: Strengthened thematic sector coordination	# of meetings/platforms for public participation in MTEF, budget preparation and monitoring	PFM Coordination Meetings organised at MoF on a quarterly basis. No sectoral/thematic meetings in line ministries (2017)	PFM Coordination Meetings organised at MoF on a quarterly basis; Budget/policy preparation platforms organised in six sectors/ministries (2021)	PFM/Sectoral policy coordination meetings
	R. 1.2 Strengthened medium term and policy planning	The quality of medium term policy and programme budgeting guidelines	Guidelines do not contain clear instructions how to report non-financial performance data through the state budget execution	Guidelines contain clear instructions how to report non-financial performance data (including gender responsive results) (2021)	MoF programme budgeting instruction
	R 1.3: Improved monitoring and inclusion of State-Owned Enterprises in published annual financial statements	Adoption of regulation/procedures for inclusion of SOEs in annual financial statements	Not available (2018)	Regulations/procedures enacted and applied (2021)	Budget Code, MoF Decrees
	R 1.4: Improved transparency and accountability in fiscal governance at subnational level	Existence of formula for distributing transfers without having clear equalization objectives	Current procedures/regulations for inter-governmental is not fair and transparent (2018)	Procedures/regulations are updated by the MoF, defining a clear objective and mechanism for transfer distribution based on the needs (2021)	Budget Code, MoF Decrees
	R 1.5: Improved governance and accountability of taxpayer services	Establishment of proper Taxpayer's database	The tax register is not adequate for tax administration (2017)	Procedures for taxpayers' registration revised and applied (2021)	Tax Code; GRS regulations

	<b>Results chain</b>	<b>Indicators</b>	<b>Baselines (incl. reference year)</b>	<b>Targets (incl. reference year)</b>	<b>Sources and means of verification</b>
<b>Direct outputs</b>	R 1.6: Improved Internal Financial Management and Control system across the Public sector in line with EU PIFC guidelines	Adoption of FMC Guidelines	Existence of FMC Guidelines not tailored to Public Administration (PA) system (2017)	Existence of FMC Guidelines linked with PA system and practices (2021)	FMC Guidelines
	R 2.1 Broadened audit coverage and enhanced independence of the SAO	Amendments to the SAO law regarding the audit of the budget revenues	n.a.	Amendment to the Law on External Audit drafted and submitted to the Parliament;	SAO law; fact finding mission at SAO
	R 2.2: Strengthened delivery and communication on performance audits by the State Audit Office	#/quality of communication on performance audit reports	6 instances of communication during 2016/2017  n.a	30 instances of communication on performance audit reports (including 3 pilot audits on gender performance) in 2018-2021	Media reports

	<b>Results chain</b>	<b>Indicators</b>	<b>Baselines (incl. reference year)</b>	<b>Targets (incl. reference year)</b>	<b>Sources and means of verification</b>
<b>Direct outputs</b>	R 3.1: Improved Parliamentary oversight	Adoption of the communication strategy of the Budget and Finance Committee Parliament	not existing (2017)	Communication strategy and plan of the Budget and Finance Committee containing at least six public hearings per year with the participation of CSOs and business associations devoted to budget preparation and implementation (2021)	Parliament website; fact finding missions
	R 3.2 Strengthened participation of Georgia's civil society and business associations in the budget oversight of fiscal governance institutions	Adoption of proper Parliamentary resolutions concerning the approval of the draft budget and budget execution reports	Not properly documented resolutions	Resolutions containing clear opinion and targeted recommendations (including on gender responsive policy planning)	Parliamentary resolutions
	R 4.1: Capacity established to support the work of an independent fiscal council consistent with Council Directive 2011/85/EU of 8 November	Adoption of Fiscal Council regulations	n.a	Fiscal Council regulations publicly discussed and then approved.	Regulations of the Fiscal Council