

Report No. 30848-YU

# Kosovo Operational Procurement Review

June 2004

Operations Policy and Services Unit  
Europe and Central Asia Region



Document of the World Bank

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## CURRENCY

Currency Unit = Euro

US\$ 1.00 = Euro 0.8239 (June 25, 2004)

## FISCAL YEAR

January 1 – December 31

## ABBREVIATIONS & ACRONYMS

BEEPS	Business Environment and Enterprise Performance Survey
BER	Bid Evaluation Report
CDF	Community Development Fund
CFA	Central Fiscal Authority
CPE	Central Procurement Entity
DFID	Department for International Development, United Kingdom
EAG	Economic Assistance Grant
EAR	European Agency for Reconstruction
EU	European Union
FAI	Finance Administration Instruction
FIDIC	International Federation of Consulting Engineers
IMF	International Monetary Fund
IDA	International Development Agency
IO	International Officer
ITF	Investigation Task Force
KCB	Kosovo Consolidated Budget
KEK	Korporata Energjetike e Kosovo
KIPA	Kosovo Institute of Public Administration
LPP	Law on Public Procurement
MEF	Minister of Economy of Finance
MSI	Management Systems International
NCA	Netherlands Court of Accounts
NGO	Non-Governmental Organization
OAG	Office of the Auditor General
OPR	Operational Procurement Review
PISG	Provisional Institutions of Self-Government
PIU	Project Implementation Unit
PPA	Public Procurement Agency
PPB	Public Procurement Bulletin
PPRB	Public Procurement Regulatory Body
PPRC	Public Procurement Regulatory Commission
SBD	Standard Bidding Documents
SIGMA	Support for Improvement in Governance and Management
SPAC	Senior Public Appointments Committee
SRSG	Special Representative of the U.N. Secretary General
TSS	Transitional Support Strategy
UNMIK	United Nations Interim Administration Mission in Kosovo
UNOPS	United Nations Office for Project Services
USAID	United States Agency for International Development

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## Executive Summary

### Purpose of the Report

The purpose of this Operational Procurement Report (OPR) is to provide an assessment of the public-sector procurement system in Kosovo, including the legislative framework, the responsibilities and capacity of the institutions entrusted with regulatory and review powers, the efficacy of current procurement practices and of the control environment. The report makes recommendations to bring about legislative, institutional and procedural improvements in the conduct of public procurement and to bolster the capacity of public-sector institutions to conduct procurement. The report also examines the performance of procurement in projects financed by the World Bank, assesses the fiduciary risk to Bank funds from procurement operations in Kosovo and makes recommendations for the design of procurement arrangements on new Bank-financed projects and for the future supervision of procurement to mitigate that risk.

The OPR, along with the Financial Accountability Assessment being conducted by the World Bank simultaneously, forms part of the Bank's analytical work which is necessary to underpin the Bank's program in Kosovo. Both reports are expected to contribute to the objective, identified in the Bank's current Transition Support Strategy (TSS) for Kosovo (April, 2004) of improving public financial management, transparency and accountability in the expenditure of public funds.

### Key Findings

*Since the establishment of the UNMIK administration in Kosovo in 1999, the legislative framework for public procurement has been incomplete.* Finance Administration Instruction (FAI) No. 2/99: "Public Procurement Using Kosovo Consolidated Budget Funds" was promulgated by the Central Fiscal Authority in December 1999 as a stop-gap measure to provide for the urgent procurement needs of the nascent UNMIK administration. However, it has remained in force as the main legislative instrument governing public procurement in Kosovo for three and a half years since then. FAI 2/99 provides a less than comprehensive framework for procurement operations, as it affords too much discretion to contracting authorities to choose the procurement procedure they will apply to a particular procurement transaction, which frequently results in insufficient attention being paid to the need for competition and transparency. The legislative framework is incomplete, as no implementing regulations have been promulgated to underpin the application of FAI 2/99 (see Section 1: Legal Framework and Procurement Practices).

*The practice of public procurement in Kosovo under FAI 2/99 is both inefficient and non-transparent.* Procurement requirements are often badly packaged for tendering purposes, which reduces competition and has led to many failed tenders. The Direct Single Source Procurement procedure is overused and the criteria applied in the evaluation of bids are overly subjective, thereby leaving the critical process of bid evaluation open to both error and manipulation.

***Oversight of the enforcement of the procurement rules is ineffective***, as the two key institutions which carry out regulatory and oversight functions, the Public Procurement Agency (PPA) and the Public Procurement Regulatory Body (PPRB), suffers from limited capacity and, because there are both under ministries of the Provisional Institutions of Self-Government (PISG), they lack the independence necessary to perform their functions effectively. A recent external audit of the Kosovo Consolidated Budget for 1999-2000 found many procurement abuses, including the use of single source procurement for contracts where the regulations required competitive tendering and financial commitments under public contracts being entered into without the required authorizations (see Section 4: Control Environment).

***A new Law on Public Procurement (LPP), substantially aligned with the EU Procurement Directives, was promulgated by the Special Representative of the U.N. Secretary General (SRSG) on February 9, 2004 and became effective on June 9, 2004.*** The new procurement law offers a much more comprehensive framework for public procurement than FAI 2/99, particularly in that establishes Open Tendering as the main procedure for awarding public contracts and imposes controls over the use of other, less competitive procedures. The new LPP also provides for a number of valuable safeguards, which are designed to make abuses of the procurement procedures more difficult, to improve transparency in decision-making related to procurement and to ensure that more than one pair of eyes review transactions in which competition may be restricted to a limited number of bidders.

***However, the current situation is confused, as the new LPP came into force on June 9, 2004 but the new oversight bodies have not yet been established.*** Because FAI 2/99 has now been superseded by the new LPP, the oversight bodies and approval arrangements which existed under that Instruction have lapsed. However, because the Kosovo Assembly has not yet been able to agree on the appointment of the members of the new Public Procurement Regulatory Commission (PPRC) and the new Public Procurement Agency (PPA), those new institutions have not yet been established. In the meantime, the current PPA and the Public Procurement Regulatory Body continue to function on the basis of the old arrangements laid down under FAI2/99 without an apparent valid legal basis. Also, as the implementing regulations and standard bidding documents (SBDs), which are required to underpin the new LPP, have not yet been promulgated, contracting authorities do not know whether they may continue to use the regulations and SBDs which had been in use under FAI 2/99.

***Even the new procurement law fails to establish the fully independent institutions which are indispensable to the effective enforcement of the law.*** The Law on Public Procurement assembles a cumbersome and complex set of three institutions which mix executive procurement functions with some regulatory powers in a new Public Procurement Agency and proposes to continue affording the executive branch of government a formal role in writing the procurement rules under which it is required to operate by providing for the participation of the Ministry of Economy and Finance in the Public Procurement Rules Committee.

The control environment for public procurement in Kosovo is also under-developed. Internal auditing and control systems in UNMIK and the spending institutions of the PISG have yet to be effectively established, which is one of the factors contributing to the occurrence of unauthorized spending commitments. While an external audit body, the Office of the Auditor General (OAG)

has recently been set up, it is still under-resourced and has yet to achieve a credible audit record. External audit functions for the Kosovo Consolidated Budget (KCB) have to date been carried out by the Netherlands Court of Accounts, which has found significant abuses related to public procurement in its audit of the 1999-2000 budget.

While the available information on administrative corruption in Kosovo is not comprehensive, it suggests that corruption does not appear to be a pervasive force in the governance process. That said, there have recently been some high-profile incidences of corruption which have resulted in prosecution. Firms participating in an Investment Climate Assessment, conducted by the World Bank, report that corruption is one of the most severe constraints on their business operations. A recent major survey of corruption on Kosovo concluded that “the UNMIK administration has been a poor role model for the Kosovars when it comes to transparency and accountability” and highlighted the risk that corruption may flourish under current conditions in which UNMIK is increasingly handing over administrative functions to weak PISG organizations (see Section 4.2: Corruption and Anti-Corruption Measures).

The performance of UNMIK and the PISG of procurement on projects financed by the World Bank has for some time been unsatisfactory and has been hampered by high turnover of staff in UNMIK, resulting in a lack of ownership. Breaches of the procurement arrangements laid down in grant agreements between UNMIK and the Bank are common. Despite the introduction into implementing agencies of dedicated Project Implementation Units, the capacity of UNMIK and the PISG to conduct procurement in accordance with the World Bank’s guidelines has remained very weak through the period of the Bank’s engagement in Kosovo.

***This report rates the procurement risk in Kosovo as high***, in view of the fact that the new law, while an improvement over FAI 2/99, is as yet untested, because the institutional capacity in UNMIK, the PISG and local government bodies to conduct procurement is weak and because corruption is significant and no convincing programs to tackle it have yet been implemented.

## **Key Recommendations**

***The report recommends that UNMIK should enact a transitional legal instrument***, perhaps in the form of an executive order, to provide a legal basis for the continued functioning of the existing Public Procurement Agency and the Public Procurement Regulatory Body and to authorize them to carry out the functions of new PPA and PPRC on a transitional basis until such time as those new institutions are formally established.

***The legislative framework for public procurement should be completed*** by the promulgation of a comprehensive set of implementing regulations and standard procurement documents, whose use by all contracting authorities should be made mandatory.

***Greater transparency and accountability of public officials conducting procurement transactions should be ensured*** by the launch of a public-access Internet website carrying full details of public procurement operations in Kosovo and by publication of the decisions and the annual reports of the Public Procurement Agency, the Public Procurement Regulatory Commission and the Review Commission.

***Technical capacity for public procurement should also be built up in the public sector*** by launching a public procurement training program at the Kosovo Institute of Public Administration (KIPA). A cadre of procurement professionals should be trained as trainers and qualified to deliver courses resulting in the award of the “procurement professional certificate,” as foreseen by the new procurement law.

***Over the medium term, the new Law on Public Procurement should be amended*** in order to correct the flawed institutional arrangements for its oversight and regulation. In particular, the duties and powers of the Public Procurement Agency should be limited to executive procurement functions and its regulatory functions should be removed, as the PPA should not both conduct procurement transactions on behalf of public-sector institutions and simultaneously exercise authority over how procurement is regulated. The OPR recommends that all regulatory duties and powers should be concentrated in the Public Procurement Regulatory Commission. The Public Procurement Rules Committee should be abolished. Finally, in order to ensure the impartial review of bid protests, a new Public Procurement Review Commission should be established as an independent second-instance body to undertake administrative review of appeals.

With regard to procurement on projects financed by the World Bank, it is recommended that the financial thresholds for International Competitive Bidding (ICB) for goods and works should be kept low, in recognition of the weakness of public-sector procurement capacity in Kosovo and of the limited ability of the local private sector to meet public-sector demand for goods, works and services. The Bank should contain to prior review most procurement procedures which it finances.

## **Preface**

**Date of Report:** The date of completion of the final Operational Procurement Review (OPR) is June 28, 2004.

**Acknowledgments:** Clearance of this report within the World Bank has been provided by Françoise Bentchikou, Chief Counsel, Procurement and Consultant Services Unit, Legal Vice-Presidency; Sunil Bhattacharya, Regional Procurement Manager, Europe and Central Asia Region; and Pamela Bigart, Lead Procurement Specialist, Procurement Policy and Services Group.

**Government Counterpart Organizations:** This report is based on information collected during three missions to Kosovo undertaken by the World Bank team during November 2003, January and June 2004. An extensive series of meetings was held with UNMIK and with officials of the relevant Provisional Institutions of Self-Government (PISG), as well as with the private sector and with other donors active in Kosovo. Following submission of the draft OPR to UNMIK, the European Agency for Reconstruction (EAR) and the PISG in early June 2004, the draft report was discussed with key counterparts in Kosovo and this final version of the report reflects those discussions. The draft report was discussed with Mr. Thierry Bernard-Guele, Head of EAR Operations in Kosovo, and his staff; Mr. Alexander Borg Olivier, Legal Adviser, Office of the Legal Adviser, UNMIK and his staff; Mr. Marjan Perlaska, Chief Executive, Public Procurement Agency, Ministry of Public Services; Ms. Sevdije Mehaj, Director, Public Procurement Regulatory Body, Ministry of Economy and Finance. EAR also provided written comments on the draft OPR.

**World Bank Team:** This report was written by a team comprising Shaun Moss, Lead Procurement Specialist, Operations Policy and Services Unit, Europe and Central Asia Region (Task Team Leader), and Belita Korreshi, Team Assistant, World Bank Country Office in Albania.

## Context

Following the cessation of hostilities in June 1999, Kosovo<sup>1</sup> was placed under United Nations administration by authority of UN Security Council Resolution 1244. This Resolution established the United Nations Interim Administration Mission in Kosovo (UNMIK) and called upon it to:

- perform basic civilian administrative functions;
- promote the establishment of substantial autonomy and self-government in Kosovo;
- facilitate a political process to determine Kosovo's future status;
- coordinate humanitarian and disaster relief of all international agencies;
- support the reconstruction of key infrastructure;
- maintain civil law and order;
- promote human rights; and
- assure the safe and unimpeded return of all refugees and displaced persons to their homes in Kosovo.

Kosovo has been gradually progressing toward self-government since 1999. In order to help prepare for the first phase of self-government, the Kosovo Transitional Council was established early on to include representatives from ethnic Albanian, Serb and other groups. Local participation was broadened in early 2000 with the establishment of the Joint Interim Administrative Structure in which 20 departments (equivalent to ministries) were co-managed by international and local experts. In May 2001, a further significant key step towards self-government was taken with the adoption of the Constitutional Framework, which sets out the Provisional Institutions of Self-Government (PISG), including the President of Kosovo, the Assembly and the Government. While the responsibilities of the PISG are growing, the Special Representative of the U.N. Secretary General (SRSG) retains authority over key areas, such as security; setting “broad parameters” for fiscal policy, including setting the budget; and for signing new laws into force and effect after they have been passed by the Kosovo Assembly.

The current trend is towards a marked reduction in the number of international civil servants working in UNMIK and a concomitant increase in the role of local Kosovar officials in carrying out the functions of government, including procurement, as UNMIK progressively hands over functions to the PISG departments.

In December, 2003, the SRSG elaborated detailed “Standards for Kosovo”, which have been endorsed by the U.N. Security Council and which are intended to define the minimum conditions – functioning democratic institutions, rule of law, freedom of movement etc. – which Kosovo would have to meet to be considered a “normal society.” In its approach of “standards before status”, the U.N. has made it clear that these standards would have to be met before discussions on Kosovo’s final status could begin. Political uncertainty and continuing security concerns have continued to hamper Kosovo’s progress towards achieving those standards.

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<sup>1</sup> Kosovo, Serbia and Montenegro, hereinafter Kosovo.

## **Purpose of the Operational Procurement Review (OPR)**

The objectives of the OPR are to:

- provide an assessment of Kosovo's public sector procurement system, including the existing legal framework, organizational responsibilities and control and oversight functions;
- examine current procurement procedures and practices, how effectively they work in practice and identify procurement practices unacceptable for use in Bank-financed projects;
- undertake an assessment of the institutional, organizational and other risks associated with the procurement process;
- make recommendations to bring about legislative, institutional and procedural improvements in the conduct of public procurement;
- assess the fiduciary risk associated with procurement on Bank-financed projects, including recommending appropriate procurement arrangements and the necessary level of procurement supervision for future Bank projects.

The OPR, along with the Financial Accountability Assessment being conducted simultaneously, and the Public Expenditure Review, scheduled for FY05, forms part of the Bank's analytical work which is necessary to underpin the Bank's program in Kosovo. As well as facilitating the management of procurement-related fiduciary risk in Bank-financed operations, the OPR contributes to the objective, identified in the Bank's current Transition Support Strategy (TSS) for Kosovo (April, 2004) of improving public financial management, transparency and accountability in the expenditure of public funds.

## **Section 1: Legal Framework and Procurement Practices 1999 – June, 2004**

At the time of this assessment, the legal framework for public procurement in Kosovo is undergoing a fundamental change, with the development of a new Law on Public Procurement (LPP), which was promulgated by the SRSG on February 9, 2004 as UNMIK Regulation UNMIK/REG/2004/3<sup>2</sup> and which became effective on June 9, 2004. The LPP replaces Finance Administration Instruction (FAI) No. 2/99: Public Procurement Using Kosovo Consolidated Budget Funds, which was issued by UNMIK's Central Fiscal Authority on December 15, 1999.

The approach taken in this report is to review the legal framework provided by FAI 2/99 and the procurement practices observed under it, as it is likely that experience built up within Kosovo's institutions in three and a half years of applying FAI 2/99 will have an impact on how those institutions apply the new LPP. The report also assesses the legal framework that is provided by the new LPP and looks ahead to how it might counter some of the negative practices developed under FAI 2/99.

### **1.1 Legal Framework under FAI 2/99**

Following the adoption of United National Security Council Resolution No. 1244 on June 10, 1999<sup>3</sup>, which provided the mandate for the establishment of the UNMIK administration in Kosovo, the legal framework for public procurement was hastily prepared by a drafting team within the Central Fiscal Authority (CFA), which took the World Bank's procurement and consultant guidelines as a template for their work. The legal instrument which resulted from their efforts was CFA Finance Administration Instruction (FAI) No. 2/99: Public Procurement Using Kosovo Consolidated Budget Funds (December 15, 1999). At the time of its promulgation, this instruction was intended to be a stop-gap measure which would be valid for only six months, yet it has remained in force for three and a half years until the recent effectiveness of the new Law on Public Procurement on June 9, 2004.

The scope of application of FAI 2/99 was to all institutions spending funds from the Kosovo Consolidated Budget (KCB), publicly-owned enterprises and any entities in which UNMIK holds a significant ownership interest. This included 10 ministries, 17 entities subordinated to ministries, 8 separate offices, 30 municipalities and 9 other entities, such as the Kosovo Trust Agency and Korporata Energjetike e Kosovo (KEK), the electrical power company. In total, 74 institutions fell within the scope of the instruction. The full list of institutions covered is attached at Annex A: List of Contracting authorities Governed by FAI 2/99.<sup>4</sup>

FAI 2/99 was supported by a number of standard procurement documents, which also have their origins in the Bank's standard bidding documents and forms. However, no implementing regulations or secondary legislation were enacted to underpin and clarify the application of the Instruction. The legislative framework of FAI 2/99 has, therefore, been incomplete throughout its period of application. Also, there were no user manuals to guide the contracting authorities' staff,

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<sup>2</sup> The text of the law is available on the UNMIK website at: <http://www.unmikonline.org/regulations/index.htm>

<sup>3</sup> Full text available on the United Nations website at <http://www.un.int/usa/sres1244.htm>

<sup>4</sup> Source: Public Procurement Agency.

who are invariably very inexperienced in procurement, in applying the Instruction and the SBDs correctly. The range of procurement procedures provided under FAI 2/99 and their salient features are summarized in Table 1.

**Table 1: Procurement Procedures under FAI 2/99**

<b>Procurement Procedure</b>	<b>Conditions for Use</b>	<b>Salient Features</b>
<b>Competitive Tendering</b>	The “preferred” method for the procurement of goods or works for large, complex requirements.	There should be at least 3 available bidders. Requires publication of an Invitation to Tender, use of SBDs published by the PPRB, public bid opening simultaneous with the expiry of the deadline for submission of bids. Bid evaluation is based on weighting of price and non-price criteria. Contract negotiation is permitted “on terms equal to or more favorable than” the terms and conditions specified in the winning bid.
<b>Two-Stage Competitive Tendering</b>	Used for large, complex contracts where the technical requirements cannot be precisely defined in advance.	Technical, unpriced bids are invited in the first stage. In the second stage, a price and revised technical bid is submitted. Other procedural features are similar to Competitive Tendering.
<b>Restricted Competitive Tendering</b>	Used for the procurement of goods or works that are available from a register of qualified bidders maintained by the contracting authority.	There is no advertising requirement. Instead, the bidding documents are sent directly to a limited number of bidders selected from the registry.
<b>Competitive Shopping</b>	Used for simple requirements for the procurement of goods or services <€25,000.	There should be at least 3 available bidders. Award of contract is to the lowest-priced quotation. Price negotiation is prohibited.
<b>Emergency Procurement</b>	Used where the requirement is urgent and the conditions giving rise to urgency could not have been foreseen by the contracting authority.	Procedural requirements are that the contracting authority should use the same procedures as under Competitive Tendering or of another procurement procedure “excepting only such of those procedures as would be inconsistent with completing the procurement as rapidly as feasible.”
<b>Normal Procurement Procedure for Consultant Services</b>	Used in all cases where the conditions for use of the other consultant procedures are not met.	Procedure is based on Quality and Cost-Based Selection, using shortlisting and a two-stage evaluation process of technical proposals in the first stage and financial proposals in the second.
<b>Selection based on Consultants’ Qualifications</b>	Used for very small assignments for procurement of consultant services <€25,000.	Shortlisted firms are invited to submit Expressions of Interest. The contracting authority invites only the firm with the most appropriate qualifications and references to submit a joint technical-financial proposal, based on which a contract is negotiated.

<b>Procurement Procedure</b>	<b>Conditions for Use</b>	<b>Salient Features</b>
<b>Least-Cost Selection of Consultants</b>	Used for routine consulting services assignments and for assignments <€25,000.	Award of contracts is to the firm that submits the lowest-priced proposal, providing its technical proposal attains a predefined minimum technical score.
<b>Consultant Services under a Fixed Budget</b>	Used where the assignment is simple and the budget is fixed.	Award of contract is to the highest-ranked technical proposal whose price is below the predefined fixed budget.
<b>Direct Single Source Procurement</b>	Used for the procurement of goods, works or physical services where there is only one possible supplier, for contract amendments <€1,250, for perishable commodities <€1,250 and for readily available goods <€1,250.	The contract is negotiated directly with a single supplier, without competition. Contracting authority is required to record the justification for the use of this procedure in the Procurement Record.
<b>Single Source Selection of Consultants</b>	Used where (i) there is only one qualified consultant, (ii) rapid selection is essential, (iii) contract is a continuation of previous services, or (iv) for small-value assignments <€1,250.	The contract is negotiated directly with a single consultant, without competition. Contracting authority is required to use the same procedures as for the Normal Procurement Procedure for Consultant Services "excepting only such of those procedures as would be inconsistent with Single Source Selection." Contracting authority is required to record the justification for the use of this procedure in the Procurement Record.

## **1.2 Procurement Practices under FAI 2/99**

In a series of interviews with the PPA, PPRB, contracting authorities and bidders, conducted in Kosovo during two missions undertaken for this assessment, this review identified the following salient features of public procurement practices in Kosovo.

### **1.2.1 Procurement Planning and Authorization of Procurement Procedures**

FAI 2/99 contains inadequate prohibitions against the splitting of procurement requirements to avoid use of the most open, competitive procurement procedures. As a result, contracts are often procured by procedures other than those required by the Instruction and projects are badly designed for procurement purposes, leading frequently to failed tenders where no contract can be awarded. One example, notorious in Kosovo, is the civil works contracts for Bankos Building, which, at the time of this assessment, had suffered from two failed tenders and was the subject of a third procedure.

Despite the fact that FAI 2/99 stipulates clear procedures for Authorizing Officers in contracting authorities to authorize the initiation of procurement procedures, the external audit of the Kosovo Consolidated Budget for 1999-2000, conducted by the Netherlands Court of Accounts, found many instances where procurement procedures and commitments had been entered into without the required authorizations and contracts had been authorized without adequate documentation on the evaluation of bids (see Section 4.1).

### **1.2.2 Application of Procurement Procedures**

One of the major weaknesses of FAI 2/99 is the lack of clarity pertaining to the use of the different procurement procedures. Excessive discretion is allowed to the individual contracting authority to choose the procurement procedure it will apply to a particular procurement transaction, which frequently results in insufficient attention being paid to the need for competition and transparency. In particular, the Direct Single Source Procurement procedure is overused and abused. Although data on the performance of public procurement in Kosovo are very hard to obtain, the Public Procurement Agency reports being left with no option but to issue many *ex post facto* approvals of the use of Direct Single Source Procurement in cases where the contracting authority has already awarded a contract by this procedure and the PPA can only rubberstamp it after the fact. As contracts above €500,000 are approved by the Deputy Special Representative of the Secretary General (SRSG), it must also be recognized that the PPA has frequently been presented with a *fait accompli* when the Deputy SRSG approves the use of Direct Single Source Procurement for such contracts. Therefore, the PPA is not solely responsible for such cases.

### **1.2.3 Use of Standard Bidding Documents (SBDs)**

The SBDs issued by the PPRB, which are closely modeled on the World Bank's SBDs, are in widespread use throughout Kosovo. While the procurement staff of contracting authorities interviewed for this assessment generally said they found the SBDs useful, many reported that they experienced difficulty in applying them in practice, particularly the SBD for Large Works, which is based on International Federation of Consulting Engineers (FIDIC) conditions. Given that FIDIC is in worldwide use, their difficulties may stem more from lack of experience in the procurement of large works using such complex documents, rather than specifically from the documents themselves.

Several contracting authorities expressed concern that, when they address questions about the application of the SBDs to the PPA, they do not receive satisfactory answers, as PPA staff are no more experienced than they themselves are and, therefore, are unable to advise them. It must be recognized that the PPA is in a somewhat difficult position, as contracting authorities turn to it for advice on the application of SBDs which the PPA did not prepare: SBDs are promulgated by the PPRB. The practical application of the SBDs looks like an obvious area for improved collaboration between the PPA and the PPRB. Several contracting authority staff expressed the opinion that it would be helpful to have staff in the PPA who are specialized in various aspects of public procurement (goods, civil works, consulting services, etc.) and to have a detailed user's guide for each SBD.

### **1.2.4 Evaluation of Bids and Award of Contracts**

Criteria used in bid evaluation usually combine price and other non-price criteria, typically delivery time, payment terms and the technical quality of the goods offered, with price being weighted at 70 percent and non-price criteria making up the remaining 30 percent in a system of evaluation based on merit points. This is a very subjective method of bid evaluation, which is open both to mistakes in the hands of inexperienced procurement staff and, indeed, to manipulation and abuse. The widespread use of such a subjective system for the evaluation of

bids also undermines accountability and the arrangements for review of bid protests because, when public officials are allowed so much latitude in the way they evaluate bids and select the winning bidder, it is almost impossible to prove that a mistake has been made or that wrongdoing has taken place.

### **1.2.5 Review of Bid Protests**

The arrangements for the review of bid protests are unsatisfactory in three important respects.

First, the procedures defined in FAI 2/99 are unfair to bidders, in that protests for contracts below <€25,000 in value are reviewed only by the contracting authority against whose actions the protest is lodged. No bidder can be expected to believe that such a review would be impartial or fair.

Second, the procedural requirements for handling bid protests are unclear. For example, FAI 2/99 imposed no firm time limits on the contracting authority or the Public Procurement Regulatory Body (PPRB) to review protests and, should the bidder remain dissatisfied after having received the response from the contracting authority or PPRB, the only recourse offered by FAI 2/99 is arbitration. There was no clear provision for recourse to a competent court.

Finally, the PPRB as established under FAI 2/99, has lacked the independence essential to the impartial, credible review of bid protests, as it was a department within the Ministry of Economy and Finance.

### **1.2.6 Record Keeping**

FAI 2/99 contained clear requirements for record-keeping and placed an obligation on contracting authorities to maintain procurement records in sufficient detail to enable the PPRB to verify that the applicable procedures had been followed. Despite these provisions, the external audit report of the KCB for 1999-2000, compiled by the Netherlands Court of Accounts (NCA), found that record-keeping was wholly inadequate in many cases and that the absence of documentary records often rendered it impossible to attain the accountability of public officials for procurement decisions. .

## **Section 2: Legal Framework under Law on Public Procurement No. 2004/3**

For the past year, UNMIK and the PISG have been working on the drafting of the new procurement law, with the clear objective of bringing Kosovo's procurement legislation into alignment with the European Union (EU) Procurement Directives. Given that FAI 2/99 is based on the World Bank's procurement and consultant guidelines, this represents a significant shift in direction.

Both the World Bank and SIGMA (Support for Improvement in Governance and Management: a joint EC-OECD program) provided technical commentary on various versions of the law during the drafting phase. The adoption of the law by the Government and submission to the Kosovo

Assembly was one of the conditions under the Bank's Economic Assistance Grant (EAG) to Kosovo, which was successfully met in May 2003. The law also received a favorable opinion from SIGMA with regard to its alignment with the EU Procurement Directives. The new Law on Public Procurement (LPP) was promulgated by the SRSG on February 9, 2004 as UNMIK Regulation UNMIK/REG/2004/3 and became effective on June 9, 2004.

The new LPP is a very lengthy, complex and comprehensive piece of legislation. While the Bank, in its technical comments made on various drafts during the first half of 2003, expressed concern about the law's complexity, particularly in an environment where the level of experience and expertise in procurement is very low, the drafters were strongly of the opinion that the situation of Kosovo demanded a law with a high degree of specificity, in order to counteract the abuses which had been observed under FAI 2/99. As the new LPP has yet to be applied in practice, the soundness of that judgment has yet to be tested.

The following are the salient features of the LPP, with particular emphasis on the sections intended to remedy previously identified weaknesses and abuses in the procurement system.

## **2.1 Application of Procurement Procedures**

The new LPP provides for an appropriate range of procurement procedures (see Table 2) and, indeed, sets a higher standard than the EU Directives in some important respects. For example, the new LPP clearly establishes the Open Procedure as the main method of awarding a public contract; less competitive methods may be used only under clearly specified conditions. By contrast, the EU Directives allow the contracting authority to choose freely between using the Open Procedure and the Restricted Procedure. Also, the conditions for use of the procedures other than the Open Procedure are more limited under the LPP than under the EU Directives. For example, the General Restricted Procedure may be used only when the goods, civil works and services can be supplied only by suppliers with appropriate technical, professional and financial qualifications or when pre-qualification of only qualified bidders would be more economically efficient than an Open Procedure. However, the General Restricted Procedure can be applied only after the prior approval of the PPA has been obtained.

The new LPP also has a number of safeguards, which are designed to make abuses of the procurement procedures more difficult, to improve transparency in decision-making related to procurement and to ensure that more than one pair of eyes review transactions in which competition may be restricted. These include requirements that:

- the use of all procurement procedures other than Open Tendering be subject to prior approval by the PPA;
- where the Executive Director of the PPA gives such an approval in response to an application from a contracting authority, his authorization must be published in the Procurement Register;
- under any procurement procedure, if fewer than three bids are received, the contracting authority can proceed to award a contract only with the prior approval of the Public Procurement Regulatory Commission (PPRC), the new body established to replace the PPRB.

Preliminary reactions from some of the contracting authorities, with which the draft law was discussed as part of this assessment, indicate strong doubts about the workability of the law, in particular because of its complexity and heavy bureaucratic burden which it is likely to impose on contracting authorities. There are also concerns about the requirement in the LPP to obtain *ex-ante* approvals from the PPA for every usage of procurement procedures other than Open Tendering. These concerns may be well-founded, as the PPA does not appear to have the resources to respond promptly to the high volume of requests for such approvals which it is certain to receive.

## **2.2 Procurement Planning, Design of Requirements, Authorization and Consolidation**

The LPP seeks to improve procurement planning by requiring all contracting authorities to submit to the PPA, 60 days before the beginning of each fiscal year, a detailed procurement forecast, identifying all the goods, works and services that they intend to procure in the next fiscal year, together with their estimated values. This forecast must be updated within ten days of the contracting authorities' receipt of their final budgetary allocations for the fiscal year. The PPA's review of these forecasts will give it the opportunity to check that there is no splitting of procurement requirements to avoid the application of the law and that the correct procurement procedures are planned to be used, according to the thresholds specified in the LPP. Based on its review, the PPA has the authority to consolidate common items and either procure them itself on behalf of the contracting authorities or establish a separate contract award committee to procure them. It is clear that these measures will have the desired effect only if the PPA has the technical and manpower capacity to undertake thorough and timely reviews of procurement forecasts and to conduct consolidated procurement transactions itself, where it decides to do so. As currently resourced and staffed, it does not.

## **2.3 Procurement Procedures under LPP 2004/3**

The procurement procedures provided under the new LPP are summarized in Table 2.

## **2.4 Use of Standard Bidding Documents (SBDs)**

The new LPP also foresees the use of SBDs, which have yet to be written. However, the European Agency for Reconstruction (EAR) recently awarded a contract to finance a €1.0 million Technical Assistance assignment for public procurement in Kosovo, under which UNMIK and PISG will receive external assistance in drafting SBDs in line with the new LPP. The fact that the SBDs required under the new LPP were not ready at the time the law came into force is regrettable and is one of the factors which contributes to the reluctance of contracting authorities to apply the new LPP immediately, as they are unsure of whether they should apply the old SBDs, promulgated under FAI 2/99 in the interim.

**Table 2: Procurement Procedures under the Law on Public Procurement 2004/3**

<b>Procurement Procedure</b>	<b>Conditions for Use</b>	<b>Salient Features</b>
<b>Open Procedure</b>	In all cases where conditions for use of other procedures are not met.	Used for the procurement of goods, civil works and services. Minimum 3 bids are required. If fewer than 3 bids are submitted, a contract may be awarded subject to PPRC waiver.
<b>General Restricted Procedure</b>	(i) The goods, civil works and services, because of their technical or specialized nature, can only be supplied by suppliers with appropriate technical, professional or financial qualifications; (ii) prequalification of only qualified bidders would be more economically efficient.	Used for the procurement of goods, civil works and services, subject to the prior approval of the PPA, which must be published in the Public Procurement Register. Minimum 3 bids are required. If fewer than 3 bids are submitted, a contract may be awarded subject to PPRC waiver.
<b>Special Restricted Procedure</b>	(i) The consulting services required, because of their complexity, can be provided only from qualified firms; (ii) it is more economically efficient to first review firms' qualifications, then invite proposals in separate technical and financial envelopes.	Used for intellectual or highly complex consulting services. Subject to the prior approval of the PPA, which must be published in the Public Procurement Register. Minimum 3 proposals are required. If fewer than 3 bids are submitted, a contract may be awarded subject to PPRC waiver.
<b>Negotiation Procedure After Publication of a Contract Notice</b>	For large-value service contracts >€100,000 where the nature of the services cannot be defined precisely in advance because of their nature, e.g., highly intellectual, technical-intensive, insurance, banking or investment services.	Subject to the prior approval of the PPA, which must be published in the Public Procurement Register. Minimum 3 bids are required.
<b>Negotiation Procedure Without Publication of a Contract Notice</b>	(i) if, for technical reasons, the contract may be awarded to a single supplier (single source); (ii) if, because a particular supplier has exclusive rights over the requirement, the contract may be awarded to a single supplier; (iii) for delivery of water, electricity, heating or gas, where the requirement can be met by only one supplier for technical reasons; (iv) in cases of extreme urgency.	Subject to the prior approval of the PPA, which must be published in the Public Procurement Register.
<b>Price Quotation</b>	(i) where the goods or services are readily available from a number of suppliers; (ii) they do not need to be specifically produced or customized (iii) there is an established market for such goods or services.	Used for contracts for goods or services, where the contract value is of low value (€500-10,000) or of minimal value (<€500). The request for quotations must be sent to at least 3 bidders, allowing at least 10 days for submission. Minimum 3 quotations required.
<b>Procedure for Minimal-Value Contracts</b>	Used for contracts for goods, civil works or services, the value of which is <€500.	PPRC shall publish special procedures, which must provide for adequate competition, transparency and cost-effectiveness.

## **2.5 Evaluation of Bids and Award of Contracts**

The provisions of the LPP regarding criteria to be used in the evaluation of bids closely follow the EU Directives, in that they allow bid evaluation on one of two bases: (i) the lowest priced bid or (ii) the economically most advantageous bid, determined by the application of a series of price and non-price criteria, such as payment terms, operating and maintenance costs, delivery period, functionality, after-sales service and warranty. The LPP again sets a more demanding standard than the EU Directives, as it requires that, when a contracting authority applies non-price criteria “to the greatest extent practicable, the contracting authority shall specify each criterion in an objective and quantifiable manner and express the weighting assigned thereto in monetary terms.”

While the use of objective criteria in bid evaluation is a welcome advance over the use of subjective criteria under FAI 2/99, it will have the intended effect of increasing transparency in procurement procedures and the accountability of public officials only if procurement officers are trained in how to apply objective criteria in an appropriate and accurate manner.

## **2.6 Review of Bid Protests**

The LPP establishes a Public Procurement Regulatory Commission (PPRC), which replaces and takes over some of the functions of the PPRB under FAI 2/99. The PPRC is better placed to perform those functions, given that it is designed to enjoy greater freedom from the Government. The PPRC is a regulatory commission, whose President and members are nominated by the Government and appointed by the Assembly (see Section 3: Institutional Framework for Public Procurement). One of the functions that it takes over from the PPRB is that of review of procurement procedures.

The LPP provides that the PPRC shall establish one or more Review Panels which have the power to:

- review complaints received by the PPRC;
- conduct investigations into the facts surrounding such complaints;
- issue an order to require a contracting authority or other party to submit information to the panel or appear before the panel;
- issue an order to suspend or terminate a procurement procedure, set aside a contract award;
- issue an order to a contracting authority to cancel or revoke a decision made by a contracting authority in relation to a procurement procedure; and
- issue an order requiring a contracting authority to pay compensation to a complainant.

The LPP has very detailed and comprehensive provisions on the procedures for submission and review of complaints, including:

- specification of the minimum contents of a complaint, required to establish its validity;

- specification of clear time limits within which the various parties to the review procedure are required to act;
- automatic suspension of a procurement procedure once a valid complaint is filed with the PPRC; and
- establishment of the bidder's right to appeal a decision to a competent court, should the bidder remain dissatisfied with the Review Panel's final decision on the complaint.

Taken together, both the procedural and the institutional arrangements of bid protests under the new LPP are very comprehensive and, if properly applied, should go a long way to addressing one of the major weaknesses of FAI 2/99.

### **Section 3: Institutional Framework for Public Procurement**

The public procurement system in Kosovo is essentially decentralized, in that contracting authorities carry out procurement transactions themselves; however, the system also features a degree of centralized control, in that, under FAI 2/99 the implementation of procurement procedures above €25,000 has been subject to review and approval by the Public Procurement Agency.

The following section describe the powers and obligations of each of the key institutions for public procurement, both under FAI 2/99 and as planned under the new LPP.

#### **3.1 Procurement under FAI 2/99**

##### **3.1.1 Public Procurement Agency (PPA)**

The institutional structure of UNMIK comprises several units under the Deputy Special Representative in charge of Reconstruction, among them a Central Fiscal Authority (CFA) and Central Procurement Executive (CPE). With the establishment of the PISG, the CPE was transformed into the Public Procurement Agency (PPA), under the Ministry of Public Services (MPS) and the responsibility for implementation of procurement was transferred from UNMIK's international personnel to local officials in December 2002. Before this date, both local and international staff had jointly signed procurement authorizations and documents.

The primary role of the PPA under FAI 2/99 was the review, approval and signature of procurement procedures and contracts above €25,000. Below €25,000, procurement responsibility was fully decentralized to the contracting authorities, which were authorized to conduct procurement transactions without reference to the PPA. Above €25,000, the PPA reviewed the bidding documents, checked that the procurement procedure had been conducted in accordance with the relevant legislation and, for contracts in the range of €25,000 to €500,000, the Director of the PPA signed the contracts. Above €500,000, contracts were signed by the relevant Deputy Special Representative of the Secretary General (SRSG), but only after the PPA Director had verified that the procedure by which the contract was awarded had been in compliance with the relevant legislation. These arrangements are summarized in Table 3.

**Table 3: Authority to Sign Public Contracts under FAI 2/99**

<b>Financial Threshold</b>	<b>Authority to Sign Contract</b>
<€25,000	Approving Officer of Contracting Authority
€25,000 - €500,000	Director of PPA
>€500,000	Deputy SRSG

For low-value contracts below €25,000, compliance with the procurement regulations appears to have been very low, as the absence of effective controls made it easy for contracting authorities to break down procurement requirements below this threshold and award a high number of low-value contracts, while avoiding the supervision of the PPA. This abusive use of splitting was one of the key procurement-related findings of the external audit of the Kosovo Consolidated Budget for 1999 and 2000, conducted by the Netherlands Court of Audit (NCA) (see Section 4).

The PPA currently has only 13 staff, who handle some 1,400 contracts annually. Although the procurement officers within the PPA have a technical background in economics, engineering and law, they are mostly young and inexperienced. An international procurement adviser, who had been contracted by UNMIK to provide advice to the PPA throughout 2003, completed his assigned at the end of the year and has been withdrawn without replacement. PPA staff have had some introductory-level training in procurement, but this is insufficient to build up their skills to the required level. Therefore, the PPA is understaffed and its capacity is too weak to perform its mandated functions effectively.

To date, under FAI 2/99, the placement of the PPA in the Ministry of Public Services has been less than ideal, as it means that the PPA Director was subjected to political pressures from within the PISG in giving approvals for certain procurement procedures and contracts. The fact that the PPA Director reports having been left with no option but to issue *ex post facto* approvals for the use of Direct Single Source Procurement already completed by certain contracting authorities may be evidence of such influence.

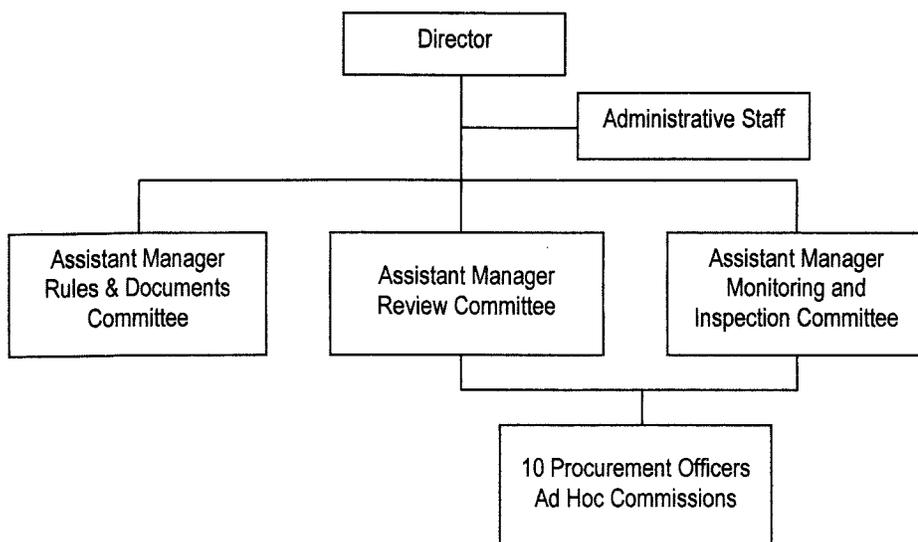
### **3.1.2 Public Procurement Regulatory Body (PPRB)**

The PPRB was established by FAI 2/99, originally within the Central Fiscal Authority but later within the Ministry of Economy and Finance. Its functions were conceived primarily as:

- taking the lead in developing new legislation and regulations;
- promulgating standard procurement documents for use by contracting authorities;
- providing contracting authorities with guidance on the legal interpretation of the regulations applicable to public procurement;
- printing a Public Procurement Bulletin (PPB);
- provide contracting authorities with training in public procurement;
- reviewing bidders' appeals;
- inspecting the activities and records of contracting authorities; and
- providing UNMIK/PISG with annual reports on the activities of the contracting authorities and on the functioning of the public procurement system.

Under the provision of FAI 2/99, the PPRB's Director is appointed by the Minister of Economy of Finance and PPRB's staff of some 26 people is organized into three functional units, responsible for (i) Rules and Procurement Documents (ii) Review Committee and (iii) Monitoring and Inspection. The organization chart of the PPRB is presented at Figure 1 below.

**Figure 1: Public Procurement Regulatory Body - Organization Chart**

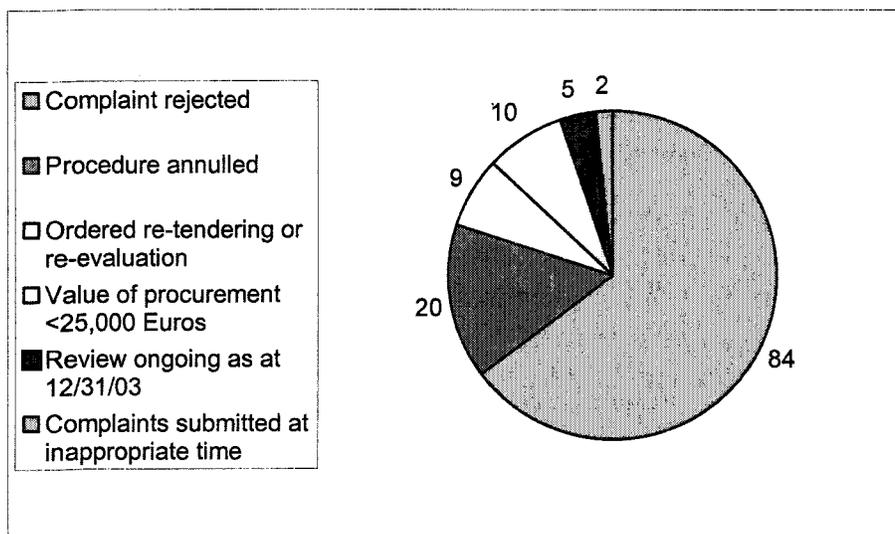


The PPRB has promulgated standard bidding documents (SBDs) for the procurement of goods and works, standard invitations to quote for the competitive shopping procurement method, guidance notes on each of these documents, and standard bid evaluation report (BER) formats. The standard documents, which are in wide use by contracting authorities, are based on the World Bank's standard procurement documents, with a similar structure that comprises standard instructions to bidders, a data sheet where variable information is entered, and both general and specific conditions of contract.

In 2003, the PPRB undertook 29 inspections, 15 of which were of municipalities, only one of a ministry and the remainder of public entities or other services.

A review of complaints handled by the PPRB in 2003 demonstrates that it reviewed 130 complaints (up from 40 in 2001), upholding the contracting authority's position in 84 cases (representing 65 percent of total cases) and either annulling the tender or ordering the contracting authority to re-evaluate or re-tender in 29 cases (22 percent).

**Figure 2: Review of Procurement Appeals by PPRB, 2003**



*Source: PPRB Annual Report, 2003.*

While an examination of the correctness of the PPRB's decisions in these cases is beyond the scope of this assessment, the high incidence of support for contracting authorities' actions may be a cause for concern, particularly when taken in the context of the external audit report prepared by the Netherlands Court of Audit (NCA) for 1999-2000, which identified "shortcomings in compliance with instructions, internal controls and the retention of supporting documentation for procurement transactions" among its principal findings.

The most immediate source for concern about the PPRB is its lack of independence. When originally established, it was under the CFA within UNMIK and it has until recently been under the Ministry of Economy and Finance, with the PPRB Director reporting to the Permanent Secretary of the Ministry. Given that the PPRB has historically been part of the same governmental structures as the contracting authorities against whose actions the PPRB reviewed appeals, bidders could not be expected to believe that the PPRB's decisions in such cases were impartial.

### **3.1.3 Organization of Procurement in Contracting Authorities**

FAI 2/99 contained few provisions specifying how the procurement function were to be organized in contracting authorities, other than that the Approving Officer of the entity, usually the head of the entity or a director of a major department, had to appoint an evaluator or a committee of evaluators, with appropriate technical and procurement skills, to conduct the evaluation of bids.

The practice of contracting authorities interviewed for this assessment varies considerably. In some cases, each department within a procuring organization conducts its own procurement, while, in others, the conduct of procurement is concentrated into a dedicated Procurement Unit. The Ministry of Health, for example, has recently switched from an entirely decentralized

arrangement under which all departments conducted their own procurement to concentrating procurement into a Procurement Unit reporting to the Budget and Finance Director, who acts as the Approving Officer in approving all requisitions generated by line departments and authorizing the commencement of the procurement procedure by the Procurement Unit. The Unit has a staff of three and handles annual procurement expenditures of €2.0 million, mainly for medical equipment and pharmaceuticals.

### **3.1.4 Training of Public Officials in Procurement**

Provision of procurement training in Kosovo has been inadequate since FAI 2/99 was enacted in 1999. Until very recently, there has been no provision of procurement training in Kosovo itself and only a handful of civil servants have traveled outside Kosovo for training. In a recent development, the Kosovo Institute of Public Administration (KIPA) launched a series of short, mostly two-day courses, in which the trainers are usually international officers or consultants with expertise in areas related to procurement, such as law. The purpose of these short courses has been to explain the application of the new LPP. However, it must be realized that this is not technical training in procurement per se.

## **3.2 Institutional Framework under LPP 2004/3**

The new LPP proposes a different and very complex landscape for the oversight of public procurement in Kosovo, comprising three main organizations:

### **3.2.1 Public Procurement Agency**

The new LPP establishes the PPA as an executive agency within the Government, the Director and Board of which are nominated by the Government and appointed by the Assembly for a three-year term. The PPA's key duties and powers are to:

- review, approve and publish tender notices;
- review draft bidding documents prepared by contracting authorities;
- conduct a particular procurement procedure on behalf of a contracting authority if the PPA determines that such an action is necessary on the grounds of professional expertise, cost-effectiveness or efficiency;
- maintain a Public Procurement Register – a database containing current information on public procurement opportunities in Kosovo and electronic copies of all tender notices, bidding documents, reports, complaints, contract award notices and other procurement documents generated by contracting authorities governed by the LPP – and post these documents on a public-access website;
- publish statistical information on public procurement operations of all contracting authorities in Kosovo; and
- prepare reports on the activities of the PPA and of contracting authorities.

### **3.2.2 Public Procurement Regulatory Commission (PPRC)**

The PPRC is responsible for the overall development of the public procurement system, for ensuring that the public procurement system uses public funds rationally and effectively and that it promotes competition and non-discrimination. Its specific functions include:

- monitoring and inspection of public procurement by conducting both ad hoc and regular audits of procurement activities conducted by contracting authorities;
- monitoring and supervision of the implementation of the law;
- carrying out administrative review of bid protests (see 2.5 above);
- providing advice and interpretation of the law to contracting authorities and bidders;
- establishing qualification requirements, developing tests and designing and delivering training programs to meet the requirements of public procurement professionals;
- maintaining a list of all contracting authorities governed by the LPP;
- submitting an annual report on public procurement activities to the Government and the Assembly;
- making recommendations to the Government and the Assembly for improvement of public procurement legislation and operations.

The PPRC is comprised of five members who are nominated by the Government and appointed by the Assembly for a five-year term. The LPP stipulates the minimum qualifications of the members and that they should have the status of civil servants. The LPP also offers certain safeguard against the removal of PPRC members during their term. At least one of the five Commission members is required to have the same qualifications required for a judicial appointment and that member is designated by the Government to serve as Chairperson of the Review Panel, responsible for review of bid protests (see 2.5 above).

### **3.2.3 Public Procurement Rules Committee**

The Rules Committee comprises one member nominated by each of the following organizations:

- Public Procurement Regulatory Commission (Chairperson of the Rules Committee);
- Public Procurement Agency; and
- Ministry of Economy and Finance.

The main functions of the Rules Committee are to:

- develop and promulgate detailed implementing regulations, rules, instructions, guidelines, standard procurement documents and forms for the implementation of the LPP;
- ensure that the rules governing tender notices and bidding documents comply with EU legislation for large-value contracts (goods and services >€100,000; civil works >€250,000);
- develop precise procedures and forms to be used for each of the procurement procedures provided under the LPP (see Table 2 above); and

- develop a procurement code of ethics to be observed by public officials engaged in procurement, including a clear set of mandatory rules governing conflicts of interest.

The Chairperson of the Rules Committee, who is always the PPRC nominee, is responsible for managing the operations of the Committee. While the LPP places an onus on the Rules Committee to make its decisions by consensus, it allows for decisions to be made by simple majority voting in the absence of a consensus.

These arrangements seem excessively complex for a territory as small as Kosovo and look disproportionately complicated when compared with those of much larger and more populous countries, such as Poland, a nation of some 39 million people and an EU member, which has a single Public Procurement Office (PPO) ([www.uzp.gov.pl](http://www.uzp.gov.pl)) for policy, legislative and oversight functions and a panel of arbitrators, maintained by the PPO, who review appeals.

### **3.2.4 Organization of Procurement in Contracting Authorities under LPP 2004/3**

In contrast with FAI 2/99, the new LPP contains very detailed rules on organizational matters, requiring each contracting authority to establish a Procurement Department, headed by a designated Procurement Officer and staffed with specialists who must be qualified to undertake procurement in compliance with the LPP. The law holds Procurement Officers responsible for making sure that their entity's procurement transactions are conducted in compliance with the LPP and imposes an obligation on them to inform the PPRC of non-compliance with the LPP, failing which the PPRC make strip them of their procurement professional certificate (see below).

The LPP also foresees and requires a dramatic scaling-up of procurement training, as it requires the PPRC to develop and deliver at least three ten-day courses in procurement each year and to issue a "procurement professional certificate" to all delegates who satisfactorily complete such courses.

In this and many other respects, the LPP sets relatively high requirements for the qualifications of Procurement Officers and for their conduct. This rather utopian vision for Kosovo's procurement system is to be built on ground which is currently fairly unpromising, given the very low level of procurement capacity in government at the moment and the serious abuses and instances of non-compliance with FAI 2/99 identified in the most recent external audit. The ground is, however, being prepared by a €1.0 million Technical Assistance project for public procurement, funded by the European Agency for Reconstruction, the consultant contract for which has recently been awarded.

The EAR-financed consultants will assist the Government to:

- develop secondary legislation and regulations;
- develop procurement manuals;
- develop a training plan;
- develop and deliver a training of trainers program and hand over the training materials to the Kosovo Institute of Public Administration (KIPA); and

- deliver procurement training, at basic and advanced levels, for up to 200 Procurement Officers.

The success of this TA is clearly essential if the high standards set by the LPP are to become reality.

## **Section 4: Control Environment**

### **4.1 Audit**

Given the absence of a Supreme Audit Institution in Kosovo itself, external audits of the Kosovo Consolidated Budget for 1999 and 2000 were conducted by the Netherlands Court of Audit (NCA); the audit report was issued in September 2003. The NCA report recognized that the difficult post-conflict conditions which existed in Kosovo in late 1999, when UNMIK began its operations, seriously affected the financial management of the Kosovo Consolidated Budget; essential institutions, infrastructure and systems had to be established or re-established quickly, and this contributed to the significant control weaknesses which characterized budget operations in 1999 and 2000. Equally, the NCA audit report recognizes that gradual but considerable progress has been made in establishing an orderly financial management system and budget control.

The NCA audit report identified the following weaknesses in UNMIK's systems:

- inadequate audit evidence led to significant uncertainty about financial statements;
- fragile accounting systems;
- the absence of an asset management and valuation system;
- severe weaknesses in the financial reporting of municipalities and public enterprises;
- revenues and expenditures were not soundly based on the applicable regulations;
- manual transaction processing resulted in inefficiency and a high risk of error; and
- the absence of internal audit units in most public-sector institutions.

With particular reference to the procurement of goods and services, NCA's audit report found that:

- there were shortcomings in compliance with instructions, internal controls and the retention of supporting documentation for procurement transactions;
- procurement procedures or commitments were entered into without the required authorizations;
- purchase orders were authorized without adequate documentation on the evaluation of bids submitted;
- there was use of single source procurement for contracts where the regulations required competitive tendering;

- there was splitting of procurement requirements in order to bring them under the applicable financial thresholds stipulated in the regulations, above which competitive tendering is mandated; and
- contracts were awarded in a manner inconsistent with the bid evaluation criteria specified in the bidding documents.

One egregious example which the NCA identified in its audit involved a purchase order placed by UNMIK on the United Nations Office for Project Services (UNOPS) for the procurement of eight bulldozers, financed by a Dutch grant. NCA found a major discrepancy between the price information on the purchase order and the price information on the Customs invoice contained in UNMIK's files. While the total value of the purchase order was US\$2,666,836, the Customs invoice showed a total value of only \$1,798,874, undervaluing the purchase order by \$867,961 or 33 percent. NCA's repeated requests to UNMIK's Central Fiscal Authority for an explanation of the discrepancy went unanswered. While the NCA audit report records that it is uncertain whether the value of the delivered bulldozers is in accordance with the purchase order, this looks like either a case of over-stating the contract price or understating the Customs invoice, possibly to avoid import duties. Details of the NCA's findings are presented in Table 4 below.

**Table 4: Example of Procurement Transaction in NCA Audit Report 1999-2000**

	<b>Per Bulldozer</b>	<b>for 8 Bulldozers</b>
<b>Purchase Order</b>		
Bulldozer	\$ 310,248.50	\$ 2,481,988.00
Spare Parts	\$ 23,106.00	\$ 184,848.00
<b>Total:</b>	<b>\$ 333,354.50</b>	<b>\$ 2,666,836.00</b>
<b>Customs Invoice</b>		
Bulldozer	\$ 147,559.35	\$ 1,180,474.80
Dismounted Elements	\$ 77,300.00	\$ 618,400.00
<b>Total:</b>	<b>\$ 224,859.35</b>	<b>\$ 1,798,874.80</b>
<b>Difference:</b>	<b>\$ 108,495.15</b>	<b>\$ 867,961.20</b>

On the topic of asset tracking and management, Kosovo is awash with stories of equipment and supplies which have been bought with public funds "leaking" into private hands. These stories have some credibility, as there is a sufficient number of documented reports, including some contained in the Management Systems International (MSI) corruption report (cited in 4.2 below), about equipment and pharmaceuticals which have gone unaccounted for in the health sector, where there is "little visible improvement" despite the considerable investments that have been made in the sector (30 percent of the health budget goes on purchasing pharmaceuticals).

In order to address the problems identified in its report, the NCA recommended that:

- the Central Procurement Executive (CPE), the forerunner to the PPA, should strengthen its oversight of public procurement and enforce compliance with procurement regulations;
- the PPRB should issue reports on compliance with procurement regulations in accordance with FAI 2/99, a recommendation which appears not to have been heeded;
- the establishment of an asset management system to track publicly-owned assets, including those acquired as a result of public procurement transactions; and
- authorizing, approving, certifying officers and the Central Financial Authority Treasury should check the completeness and correctness of all mandatory documentation to provide evidence about the regularity of expenditures on goods and services.

With regard to the implementation of these recommendations, the new institutions, with clearer responsibilities and powers, set up under the new LPP will be essential to the establishment of an effective and comprehensive operational framework within which public procurement can take place in Kosovo. On compliance monitoring, the PPRB does prepare an annual report on its activities but this report focuses more on the PPRB's activities (e.g., that it conducted 29 monitoring and inspection exercises in 2003) than on reporting the degree of compliance of the contracting authorities with the applicable legislation. Asset management remains a weakness of the system and there are no immediate plans to set up an effective system for tracking and managing physical assets owned by public institutions. Finally, it is understood that Treasury has now put in place measures to check the authenticity of signatures on purchase orders and that full, original purchase order documentation is provided.

### **Development of External and Internal Audit Functions in Kosovo**

Within the framework of the four "pillars" or areas of responsibility which UNMIK has established for the involvement of international institutions in Kosovo, under Pillar 4: Economic Development and Reconstruction, which is led by the European Union, the EU has responsibility for setting up a supreme audit institution in Kosovo, called the Office of the Auditor General (OAG). The legal basis for the establishment of OAG is provided by UNMIK Regulation 2002/18<sup>5</sup> dated October 4, 2002; the OAG was established and an Auditor General appointed in November 2003. A new project has also been launched to expand and enhance the existing internal audit functions, which have grown out of the Internal Audit Unit of the old Central Financial Authority, which has since been transformed into the Ministry of Economy and Finance, a PISG institution. However, the operational capacity of both internal and external audit units remains limited and will take time to develop.

#### **4.2 Corruption and Anti-Corruption Measures**

Measuring corruption is difficult under any circumstances. Given that parties to corrupt transactions have little incentive to talk about them, most surveys of corruption tend to limit themselves to measuring perceptions of corruption, rather than corruption itself. However, measuring corruption in Kosovo is particularly difficult given that, due to its uncertain status, Kosovo is usually omitted from most international surveys of corruption such as the Business

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<sup>5</sup> available on the UNMIK website at: [http://www.unmikonline.org/regulations/2002/RE2002\\_18.pdf](http://www.unmikonline.org/regulations/2002/RE2002_18.pdf)

Environment and Enterprise Performance Survey (BEEPS).<sup>6</sup> Also, while Serbia and Montenegro is generally included in such surveys, data on Serbia and Montenegro are generally not accepted as being representative of Kosovo, again due to the province's unique circumstances. A further factor inhibiting empirical observation of corruption is the deeply adversarial nature of political debate in Kosovo, which creates an environment in which allegations of corruption are habitually hurled by leaders of one ethnic group at another with the intent of gaining political advantage, but such allegations tend to be based on little more than hearsay or ill will. While conducting this procurement assessment, the Bank team was besieged with reports of corruption related to public procurement. However, none of their originators was able to back up the reports with hard facts.

Perhaps the most exhaustive study of corruption in Kosovo is one conducted by Management Systems International (MSI) for the United States Agency for International Development (USAID) entitled "Corruption in Kosovo: Observations and Implications for USAID."<sup>7</sup> This report is based on a representative public opinion survey, conducted in May 2003, as well as on focus groups and interviews with individuals and representatives of major stakeholder organizations, including UNMIK, PISG, civil society, mass media, the private sector and international organizations.

This survey concluded that:

"while corruption exists in Kosovo...it does not appear that corruption is a pervasive force in the governance process and it does not appear to significantly undermine the capacity of government to perform its duties and deliver services in a fundamental way."

Another encouraging finding of the survey was that:

"In comparison to other countries in the region...corruption does not appear to be as widespread among public officials, the demands of corrupt officials are lower and the extent of citizen involvement in corrupt transactions is lower in Kosovo than in other countries in Southeast Europe."

While the survey also repeats the threat – often cited in Kosovo – that corruption may increase as UNMIK's international civil servants are progressively withdrawn and as powers are transferred to PISG organizations, nevertheless it points out, fairly, that "the UNMIK administration has been a poor role model for the Kosovars when it comes to transparency and accountability."

In terms of the prevalence of corruption, respondents to the MSI survey, when asked the question "What are the top three problems facing Kosovo?" identified corruption as the second most pressing problem (38.9 percent), a long way behind unemployment (85.8) but ahead of poverty (32.9), low incomes (30.9) and high prices (30.3). In another survey conducted by the Kosovo Institute for Democratic Society in 2003 only among respondents in Pristina, 66 percent of respondents described corruption as a major problem in their daily lives, while 85 percent described it as a major problem in Kosovo in general.

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<sup>6</sup> available online at <http://info.worldbank.org/governance/beeps2002/>

<sup>7</sup> available online at [http://www.usaid.gov/missions/kosovo/pdf/kosovo\\_corruption.pdf](http://www.usaid.gov/missions/kosovo/pdf/kosovo_corruption.pdf)

The MSI survey also asked respondents to identify the most corrupt institutions in Kosovo; the top five are listed in Table 5, below:

**Table 5: Institutions Perceived to be the Most Corrupt in MSI Survey, 2003.**

<b>Institution</b>	<b>Percent of respondents who believe that corruption is high or very high</b>
KEK	78.2%
Businesspeople	57.0%
PTK (Telecommunications Company)	55.2%
Customs	54.9%
Hospitals	45.6%

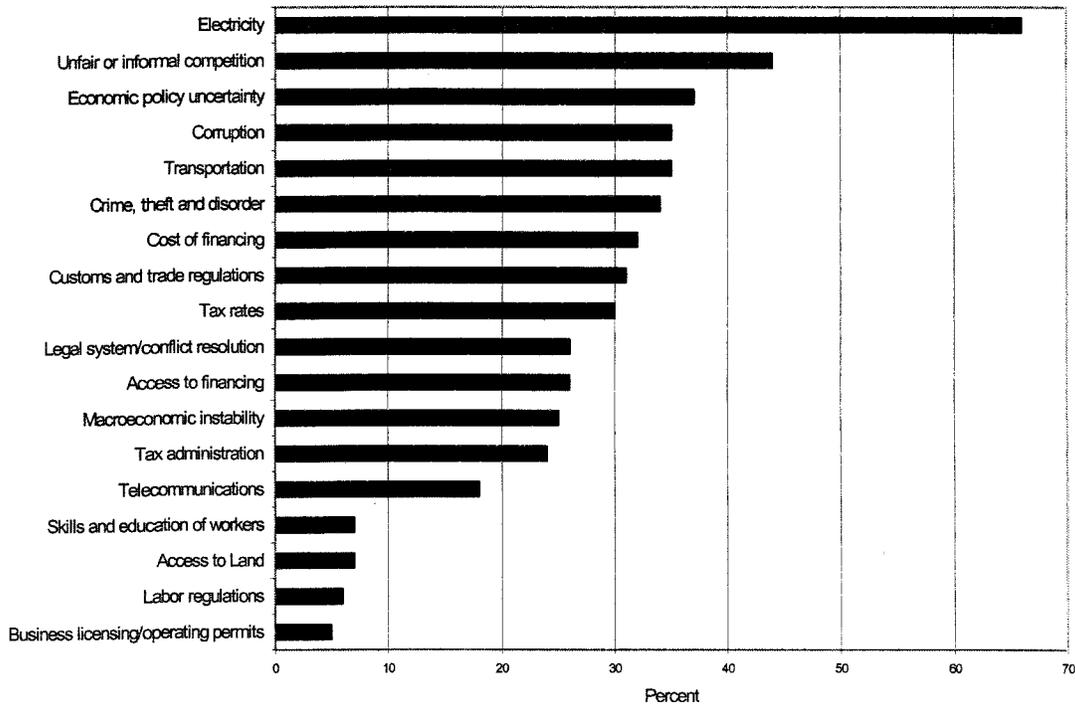
In the section of its report which surveyed six focus groups drawn from NGOs, business groups and the media, four of the six focus groups identified public procurement as being among the most corrupt functions. All six of the focus groups rated UNMIK's procurement operations as being corrupt. The focus group that comprised businessmen admitted to having been extorted by public officials in procurement procedures. Members of the government perceived "pervasive corruption" in public procurement, as well as in the border police, customs, publicly-owned enterprises and large reconstruction grants from international donors. A section of MSI's report dedicated to public procurement, also recounts several allegations of corrupt practices related to public procurement, but few of these can be substantiated in fact.

With regard to the impact of corruption on the operations of private-sector businesses in Kosovo, a recent survey of enterprises (see Figure 3) indicates that 35 percent of surveyed firms identified corruption as a "major" or "severe" constraint to their operations, ranking corruption fourth among the eighteen constraints identified.

In its efforts to combat corruption, the Government has established an Office of Good Governance under the Prime Minister. In 2002, this Office prepared the Government's first Anti-Corruption Plan, which includes public awareness, legislative and administrative initiatives.

UNMIK's main response to corruption has been the establishment, in November 2003, of an Investigation Task Force (ITF), a special unit to fight corruption within its own ranks as well as in Kosovo's institutions, including publicly-owned enterprises and other entities funded by the consolidated budget. The ITF's role is to initiate, conduct and coordinate administrative investigations to identify fraud and corruption. In one of the most high-profile corruption cases to be successfully prosecuted, German authorities sentenced a UN official in 2003 to three and a half years in prison for the embezzlement of some €4.5 million (US\$5.2 million) of international aid donated to KEK. There is some evidence, therefore, that anti-corruption measures are working. However, the separation of the justice and law enforcement functions, which are reserved for UNMIK, and administrative governmental functions, vested in the PISG bodies, creates a continuing vulnerability to corruption.

**Figure 3: Evaluation of General Constraints to Operations**  
 (percent of firms ranking constraint as "major" or "very severe")



Source: Investment Climate Assessment, World Bank 2003.

Another important element of anti-corruption measures relates to the procedures for appointing civil servants. An essential component of these measures is the Senior Public Appointments Committee (SPAC), which appoints senior public officials through a competitive selection process. The recently-appointed Executive Director of the Public Procurement Agency was appointed by the SPAC. A gap in the system, however, exists with respect to senior public officials who were appointed before the SPAC came into existence. According to Regulation No. 2001/36 "On The Kosovo Civil Service," such appointments should be retroactively reviewed by the Independent Oversight Board. However, that Board has yet to be created and, in its absence, appointments of senior civil service positions, such as heads of departments, have been left prone to the vagaries of political patronage. As UNMIK's International Officers (IOs) increasingly pull out of Kosovo, there is a real risk that many senior civil service positions may be politicized, resulting in the large-scale capture of the top ranks of the civil service by Kosovo's political parties and raising the specter of political pressure being brought to bear on public procurement, as well as on many other areas of public sector decision-making. If this grave situation is to be averted, it is clear that the Civil Service Oversight Board must be established and that it retroactively review senior appointments that have not gone through the SPAC process.

The same Civil Service Regulation contains a Civil Service Code of Conduct, which imposes on civil servants an obligation to perform their duties honestly, not to misuse their official positions for personal gain and to use public resources efficiently, among other duties.

## Section 5. Public-Sector Performance

Information on recurrent and capital expenditure, based on International Monetary Fund (IMF) estimates, indicate that, as a percentage of total budgetary expenditure, procurement expenditure has increased significantly in the five years from 2000 to 2004, when it reached 28.1 percent of budget expenditure.

**Table 6: Recurrent and Capital Expenditures as % of Consolidated Budget, 2000-2004**

	2000	2001	2002	2003	2004
Goods and Services	10.1	7.9	11.6	14.7	13.6
Capital Expenditure	2.3	1.8	3.3	7.8	14.5
<b>Total</b>	<b>12.4</b>	<b>9.7</b>	<b>14.9</b>	<b>22.5</b>	<b>28.1</b>

The same information examined in monetary terms indicates that expenditure on procurement from the Kosovo Consolidated Budget rose from €90.2 million in 2000 to €295.5 million in 2003, with a further increase to €388.6 million budgeted for 2004.

Given an estimated GDP in 2003 of €1,317, this suggests that public procurement expenditure was 22.4 percent of GDP, which is substantially in excess of the EU average of 16.7 percent.

**Table 7: Recurrent and Capital Expenditures, 2000-2004 (Euro millions)**

	2000	2001	2002	2003	2004
Goods and Services	75.2	90.9	148.4	193	188.6
Capital Expenditure	17	20.6	41.9	102.5	200
<b>Total</b>	<b>92.2</b>	<b>111.5</b>	<b>190.3</b>	<b>295.5</b>	<b>388.6</b>

This increase can be explained by the establishment of the PISG and by including expenditures, which had previously been carried out by the donor community, in the budget. Recurrent costs have increased in line with capital costs, which likely reflect increased investments in post-conflict infrastructure rehabilitation.

Based on data provided by the PPA for this assessment, there were a total of 464 procurement procedures undertaken in 2003, which resulted in the award of 886 contracts. Of those 464 procedures, PPA figures indicate that 402 (87 percent) were by the Competitive Tendering procurement method, the most open and competitive method available under FAI 2/99. While this is encouraging as an indicator of the extent to which expenditures on procurement are exposed to competition, it is at variance with the anecdotal information collected by the

assessment mission, including from senior officials of UNMIK, which suggests that Direct Single-Source Procurement is heavily over-used.

## Section 6: Procurement Performance on World Bank-financed Projects

This section reviews the quality of the performance of Bank-financed procurement in terms of its compliance with Bank procurement and consultant guidelines. It also identifies major problems from past implementation and recommends measures to be introduced to strengthen procurement capacity in World Bank financed-projects. In addition, it provides a basis for decisions on the level of intensity of procurement supervision over Bank operations.

### 6.1. Development of World Bank Portfolio

The Bank's first Transitional Support Strategy (TSS) for Kosovo, dating from September 1999, defined the Bank's strategy as helping to ensure the overall sustainability of the reconstruction and recovery effort by using the Bank's comparative advantage in aid coordination and policy advice and through selective financial support. A Trust Fund for Kosovo of US\$60 million was made available by the Bank and was committed by August 2001 to twelve projects, in addition to two post-conflict grants of US\$2 million. The Bank's resources have been complemented by co-financing of projects in the amount of US\$62 million.

Currently, the Bank's portfolio in Kosovo comprises nine active projects totaling US\$31.5 million (see Table 8). Eleven projects have closed. The current pipeline contains three IDA grants totaling approximately US\$15 million. The Human Development sector accounts for approximately 50 percent of the total portfolio, with four ongoing projects out of nine.

**Table 8: World Bank Portfolio in Kosovo as of January 31, 2004**

No.	Project ID	Financier <sup>8</sup>	Project Name	Currency	Principal	Effective Date	Closing Date
23626	P069516	WBTF	Education and Health	USD	4,435,000	10-May-00	30-Jun-04
24832	P072814	WBTF	Community Development Fund II	USD	4,000,000	31-Dec-03	31-Dec-06
28929	P072405	UK+WB	Social Protection	USD	4,200,000	16-Jul-01	28-Feb-05
H0360	P079260	IDA	Education Participation Improvement Project	USD	4,600,000	23-Jul-03	31-Dec-06
24792	P070365	WBTF	Pilot Water Supply	USD	4,600,000	18-Apr-01	15-Jan-05
H0480	P079019	IDA	Energy Sector TA 2	USD	1,500,000	17-Nov-03	30-Jun-05
H0470	P078380	IDA	Economic Assistance IV	USD	5,000,000	20-Nov-03	31-Jan-04
27806	P071265	WBTF	Private Sector Development TA	USD	3,000,000	21-Jun-01	30-Jun-04
	P083575	IDF	Public Expenditure Management TA	USD	197,000		
<b>TOTAL</b>				<b>USD</b>	<b>31,530,000</b>		

<sup>8</sup> WBTF = World Bank Trust Fund; IDA = International Development Association; IDF = Institutional Development Fund.

The Kosovo portfolio consists of small grants with relatively short implementation periods of up to four years. While a considerable number of projects are implemented by PIUs, two are handled by “continuing” entities such as KEK and Kosovo Trust Agency, and in one case by the Community Development Fund (CDF) – a local non-governmental organization. While in the Community Development Fund I Project, the CDF was the Grant Recipient, in the Community Development Fund II Project, with the trend of transferring functions from UNMIK to the PISG, the CDF PIU is the Grant Recipient. It was established and will operate under UNMIK supervision. In discussions with PIUs on the preparation of OPR, several common procurement problems were found.

A widespread problem is the weak procurement capacity of staff in PIUs. Although some have received training in international organizations, such as ILO Turin, there is a need for further strengthening of their capacity to conduct procurement in accordance with the Bank’s guidelines. Recent experience indicates that most projects failed to keep up-to-date procurement plans, to use appropriate bidding documents for NCB (National Competitive Bidding), or to apply the recommended procedures for the evaluation of bids for civil works contracts awarded by NCB. Often bid evaluation reports lack detailed information, such as the justification for contract award recommendation, grounds for rejecting a bid as non-responsive or the verification of bidders’ qualifications, all issues which require detailed treatment in bid evaluation reports in order to obtain prompt clearance by the Bank.

Some newly established implementing agencies do not have a clear understanding of how to start and finalize a simple shopping procedure, in terms of drafting technical specifications, opening and evaluation of quotations. Quite often it is noted that PIUs cannot correctly adhere to the pre- and post-qualification processes. Post-qualification is conducted for the three lowest bids, while according to Bank guidelines, it should be applied only to the lowest evaluated bidder. In some projects, it was found that PIUs have established consultant rosters for engineering assignments, but these are not updated regularly and cannot be used as a reliable source for establishing long list, given their tendency to exclude unregistered consultants.

Deficiencies in contract monitoring systems are another common problem. Given that many of the projects are jointly financed by other agencies, PIUs keep a summary list of contracts financed by each donor but fail to pay adequate attention to the aggregate thresholds within Bank grant agreements, which are frequently exceeded.

While the process of handing over implementation functions from UNMIK to PISG is ongoing, it has resulted in limited ownership of the projects by either UNMIK or PISG. Avoidable problems and delays are created, since both of them have limited capacity in World Bank procurement, and time-sensitive decisions on procurement sometime get lost in transition between the two.

To date, the World Bank has conducted a limited number of procurement post reviews. This is due, in part, to the fact that contracts which are, according to the grant agreement, subject to post review are frequently submitted to the Bank for prior review. This is yet another indicator of weak capacity in implementing agencies, which lack the confidence to take procurement

decisions which they are authorized to take without the comfort of a “no objection” from the Bank.

## 6.2 Decentralized Projects

Procurement arrangements for most of the projects are handled by headquarters-based procurement staff, except for one project, Education and Health, which is decentralized to the Procurement Unit in the Bosnia and Herzegovina Country Office.

## 6.3 Recommended Actions

The following actions are recommended to improve the quality of implementation and supervision of procurement of Bank-financed projects in Kosovo:

- The PIUs should use the appropriate standard bidding documents for the procurement of goods, works or services, which should contain a draft contract, all acceptable to the Bank.
- Bank task teams should ensure that the level of post reviews conducted is kept at the level stipulated in the applicable grant agreement.
- The implementing agency should prepare a detailed procurement plan at the stage of project appraisal and keep it up-to-date throughout the period of implementation, with revisions being made at least once a quarter. Bank procurement staff should follow up assiduously to make sure that plans are kept up-to-date and implemented without slippage.
- Thresholds for International Competitive Bidding for goods and works should be kept relatively low at >US\$100,000 for goods and >US\$300,000 for works. Below US\$300,000 the procurement of works may be conducted by NCB while, below US\$100,000, Shopping may be used for goods and works. Prior review thresholds should be set at the same level as ICB thresholds for goods and works, so that all ICB contracts are subject to prior review. For NCB for works, all contracts should also be subject to prior review.
- The Bank should place an obligation on all implementing agencies, through post review reports and supervision missions, to establish and maintain a contracts register for goods, works and services financed by World Bank.
- Task teams should strongly recommend that PIUs attend procurement seminars organized by the Bank in the region, as, to date, attendance by delegates from Kosovo has been low.

The following thresholds are recommended for application to Bank-financed contracts in Kosovo:

**Table 9: Recommended Thresholds by Procurement Method**

<b>Procurement Method</b>	<b>Threshold</b>
International Competitive Bidding: Works	>US\$300,000
NCB: Works	<US\$300,000
International Competitive Bidding: Goods	>US\$100,000
Shopping: Goods and Works	<US\$100,000

The Bank should conduct Prior Review for every project on:

- all contracts for Goods and Works procured through ICB and NCB;
- the first two Shopping contracts for goods and the first two Shopping contracts for works;
- contracts with consulting firms >US\$50,000; and
- contracts with individual consultants >US\$25,000.

In the selection of consultants, shortlists of firms may comprise only firms from Kosovo provided that the assignment is estimated to cost less than US\$100,000 and there is a sufficient number of qualified local consultants to generate competition.

#### **6.4 Unacceptable Practices on World Bank-financed Projects**

When National Competitive Bidding (NCB) is used on Bank-financed projects in Kosovo, the following procedural waivers should apply to the Law on Public Procurement (LPP) in Kosovo (UNMIK/REG/2004/3 dated February 9, 2004).

##### **Eligibility**

No restrictions should be imposed on employment of specific persons or origin of the goods or services to be supplied or provided.

##### **Procedures**

The Open Procedure, as defined in Section 30 and related sections of the LPP, shall be followed in all cases.

##### **Advertising**

Invitations to bid shall be advertised in at least one widely circulated Albanian-language daily newspaper in Kosovo and in at least one widely circulated Serbian-language daily newspaper in Kosovo, allowing a minimum of 30 days for the preparation and submission of bids.

##### **Assessment of Bidders' Qualifications**

When pre-qualification shall be required for large or complex works, invitations to pre-qualify for bidding shall be advertised in at least one widely circulated Albanian-language daily newspaper in Kosovo and in at least one widely circulated Serbian-language daily newspaper in Kosovo a minimum of 30 days prior to the deadline for the submission of pre-qualification applications.

Minimum experience, technical and financial requirements shall be explicitly stated in the pre-qualification documents, which shall be determined by a "pass/fail" method, not through the use of a merit point system. Where pre-qualification is not used, the qualifications of the bidder who

is recommended for award of contract shall be assessed by post-qualification, applying minimum experience, technical and financial requirements, which shall be explicitly stated in the bidding documents.

### **Participation by Publicly-Owned Enterprises**

Publicly-owned enterprises in Kosovo shall be eligible to participate in bidding only if they can establish that they are legally and financially autonomous, operate under commercial law and are not a dependent agency of the Government. Furthermore, they will be subject to the same bid and performance security requirements as other bidders.

### **Bidding Documents**

Procuring entities shall use the appropriate standard bidding documents for the procurement of goods, works or services, which shall contain draft contract and conditions of contract acceptable to the Bank.

### **Bid Submission, Opening and Evaluation**

- a) Bids shall be submitted in a single envelope containing the bidder's qualification information, technical and price bids, which shall be opened simultaneously at the public bid opening.
- b) Bids shall be opened in public, immediately after the deadline for submission of bids. The name of the bidder, the total amount of each bid and any discounts offered shall be read aloud and recorded in the minutes of the public bid opening.
- c) The evaluation of bids shall be done in strict adherence to the monetarily quantifiable criteria specified in the bidding documents, and a merit point system shall not be used.
- d) Extension of bid validity shall be allowed once only for not more than 30 days. No further extensions should be requested without the prior approval of the Bank.
- e) Contracts shall be awarded to qualified bidders having submitted the lowest evaluated substantially responsive bid.

### **Price Adjustment**

Civil works contracts of long duration (e.g. more than 18 months) shall contain an appropriate price adjustment clause.

### **Rejection of All Bids**

All bids shall not be rejected and new bids solicited without the Bank's prior written concurrence. When the number of bids received is less than three, re-bidding shall not be carried out without the Bank's prior concurrence.

## Securities

Bid securities should not exceed 3 percent of the estimated cost of the contract; performance Securities, not more than 10 percent. No advance payments shall be made to contractors without a suitable advance payment security. The wording of all such securities shall be included in the bidding documents and shall be acceptable to the Bank.

## Section 7: Risk Assessment

While, because of the promulgation of the new procurement law, Kosovo's **legal framework** for public procurement promises to be much sounder and more comprehensive than it has been to date, the new LPP is an entirely untested document. Much will depend on whether the many good ideas and controls inserted into the LPP are carried out in practice. Only the passage of two or three years from June 9, 2004, when the new law came into effect, will tell whether it has had its intended effect.

The **regulatory framework** for public procurement in Kosovo has been weak to date, with both the PPA and the PPRB embedded within PISG ministries and lacking both the capacity and the independence to do their jobs to full effect. The public institutions that conduct procurement are generally very weak in terms of their procurement capacity and the level of knowledge and technical skills in procurement among public officials is as yet very low.

The **control environment** has been similarly weak to date, with external auditing taking place only by the intervention of a supreme audit institution from another country and internal auditing totally undeveloped. Control systems within contracting authorities either do not exist or do not work. As the NCA audit found, procurement transactions frequently occur without proper authorization and financial commitments are entered into without appropriate linkages to budgetary allocations. **Corruption** is significant and, to date, no convincing programs to tackle it have been implemented.

Measured against all of these parameters, the environment for conducting public procurement in Kosovo is one of **high risk**. In this respect, Kosovo rates comparably with other countries in Europe and Central Asia Region that have recently embarked along the road of public procurement reform and whose procurement environments have also been rated as high risk in recent assessments undertaken by the World Bank, including Serbia and Montenegro, Albania, Macedonia, Turkey, the Russian Federation and Ukraine.

## **Section 8: Recommendations**

### **8.1 Recommendations for Legislative Reform**

The World Bank indicated as recently as May 2003 that the then draft LPP of Kosovo was acceptable to the Bank. However, changes to the law have been made in the interim which are likely to undermine its efficacy in implementation, particularly regarding the institutions which will be responsible for ensuring its enforcement. Recommendations relating to institutional reform are presented under 8.2 below. Recommendations relating to legislation are aimed mainly at completing the legislative framework for public procurement:

- 1. As a matter of urgency, UNMIK should enact a transitional legal instrument, perhaps in the form of an executive order, to provide a legal basis for the continued functioning of the existing Public Procurement Agency and the Public Procurement Regulatory Body and to authorize them to carry out the functions of new PPA and PPRC on a transitional basis until such time as those new institutions are formally established.*
- 2. Enact a complete set of implementing regulations to underpin the procurement law, to clarify its correct application and provide detailed instructions on its application in key areas. Specific regulations should be enacted on procurement planning, selection of procurement methods, pre-qualification and post-qualification, bid evaluation and contract administration.*
- 3. Promulgate a comprehensive set of standard bidding and contract documents, whose use should be mandatory for all contracting authorities, covering prequalification, procurement of goods, civil works and consulting services, including standard forms of contracts for each application.*
- 4. Promulgate a set of procurement manuals detailing the correct application of the LPP, implementing regulations and SBDs.*

Assuming adoption of the recommendations on institutional reform (see below), the above recommendations would be for the Public Procurement Regulatory Commission to implement.

### **8.2 Recommendations for Institutional Reform**

With regard to the institutions which oversee the implementation of the LPP and the division of powers and responsibilities between them, in every country there are four main groups of tasks which need to be performed to ensure the efficient operation of a public procurement system. These are:

- procurement policy and legislative development;
- supervision;
- monitoring and enforcement;
- administrative review of bid protests.

It is essential, for the transparent and effective operation of these functions, that the bodies which exercise them should be independent from the executive branch of government, which is the branch which conducts procurement.

In Kosovo, because of the institutional legacy which the PISG has inherited from UNMIK and because of the weakness of procurement implementation capacity in the contracting authorities, a decision has been taken to add a fifth function, namely:

- an executive procurement function which is to be performed by the PPA.

However, it is essential that the PPA's responsibilities should not include any functions which are regulatory in nature – such as granting waivers for the use of procurement procedures other than the Open Procedure – because the PPA is an executive agency within Government and, therefore, does not have the independence which is essential to the credible performance of regulatory functions. ***For that reason, this report recommends that all regulatory functions should be removed from the PPA and that it should be responsible solely for the exercise of executive procurement functions –that is to say, for doing procurement.***

By the same logic, it is also essential that the executive branch of government should not be involved in setting the rules which will apply to it when it performs executive procurement functions. ***Therefore, this report recommends that the PPA and the Ministry of Economy and Finance should be removed from the Public Procurement Rules Committee.*** Indeed, there is little justification for having a Rules Committee at all, given that its functions can be credibly performed by the Public Procurement Regulatory Commission. ***To that end, it is recommended that the Public Procurement Rules Committee should be disbanded and that its rule-making functions should be subsumed into the PPRC.***

The one remaining change necessitated by these reforms would be to ***remove the review function from the PPRC***, as it cannot be expected, on the one hand, to define procurement procedures and write rules and, on the other hand, to review appeals against procedures conducted under those rules. ***To that end, this report recommends the establishment of a new, independent Public Procurement Review Commission, which should be independent from government and which should meet the requirements of the EU Public Remedies Directive 89/665/EEC.***

Table 10 summarizes the proposed institutional arrangements recommended by this report. Implementation of these recommendations would clearly require an amendment to the LPP. It is understood that, when the LPP was enacted, UNMIK and the PISG recognized that there were certain compromises made within the law, particularly in respect of its institutions. Therefore, it is expected that there will already be acceptance on the part of UNMIK and the PISG that these reforms are necessary.

**Table 10: Recommended Public Procurement Institutions and Functions**

<b>Institutions</b>	<b>Public Procurement Agency</b>	<b>Public Procurement Regulatory Commission</b>	<b>Public Procurement Review Commission</b>
Functions	Executive procurement functions on behalf of government	Procurement policy and legislative development Supervision Monitoring and enforcement	Administrative review of procurement procedures

To summarize the recommendations in the institutional area:

- 1. Limit the duties and powers of the PPA to executive procurement functions and remove from it functions which are regulatory in nature, such as granting approvals to the use of procurement procedures other than the Open Procedure.*
- 2. Concentrate all regulatory duties and powers in the Public Procurement Regulatory Commission.*
- 3. Abolish the Public Procurement Rules Committee.*
- 4. Establish a new Public Procurement Review Commission as an independent second-instance body to undertake administrative review of bid protests.*

### **8.3 Recommendations for Improving Procurement Procedures, Increasing Transparency and Combating Corruption**

Many of the deficiencies identified in this report have already been addressed by the new LPP, which has much more comprehensive provisions than did FAI 2/99 relating to the manner in which public procurement procedures are to be conducted. Therefore, the key to making sure that the planned improvement actually takes place will be to maximize transparency and public scrutiny over procurement operations, thereby holding public officials accountable for applying the law. The following recommendations are designed to promote this objective.

- 1. Launch a public-access Internet website carrying full details of public procurement in Kosovo, including relevant laws, implementing regulations, standard procurement documents, invitations to bid and contract award notices.*
- 2. Publish all applications from contacting authorities to use procurement procedures other than the Open Procedure, as well as the decision made by the regulatory authority on each application.*
- 3. Publish the annual report of the PPA, PPRC and the Review Commission on the public procurement website.*

#### **8.4 Recommendations for Building Public Procurement Capacity**

The LPP already contains quite comprehensive requirements for the training and certification of Procurement Officers and for the establishment of a Procurement Department in each contracting authority. It will be essential that the Public Procurement Regulatory Commission sees that these important steps are taken. Therefore, the recommendations in this section are intended not to repeat those measures but to complement them.

- 1. Establish a public procurement training program at the Kosovo Institute of Public Administration (KIPA), with a cadre of procurement professionals trained as trainers and qualified to deliver courses resulting in the award of the “procurement professional certificate” foreseen in the LPP (this measure is planned to be financed under the EAR Technical Assistance for public procurement).*
- 2. Once the program has been established for 2-3 years, KIPA should seek to develop an internationally-recognized professional procurement qualification, for example by association with and accreditation from an international procurement body.*

The recommendations of this report are summarized in an Action Plan, contained in Table 11 below.

**Table 11: Action Plan for Public Procurement Reform in Kosovo**

AREA	ACTION	RESPONSIBLE ORGANIZATION	TIMING		
			SHORT-TERM < 6 MONTHS	MEDIUM TERM <12 MONTHS	LONG TERM < 24 MONTHS
1. Legislative Reform	a. <i>Enact a transitional legal instrument, to provide a legal basis for the continued functioning of the existing PPA and PPRB</i>	UNMIK to draft  SRSG to promulgate	X		
	b. Enact a complete set of implementing regulations to underpin the procurement law.	PPRC to draft and promulgate		X	
	c. Promulgate a comprehensive set of standard procurement documents, and make their use mandatory for all contracting authorities.	PPRC to draft and promulgate		X	X
	d. Promulgate a set of procurement manuals detailing the correct application of the LPP..	PPRC to draft and promulgate		X	X
2. Institutional Reform	a) Limit the duties and powers of the PPA to executive procurement functions; remove its regulatory functions. (to be achieved by an amendment to the LPP)	UNMIK/PISG to draft Government to adopt Assembly to pass SRSG to promulgate			X
	b) Concentrate all regulatory duties and powers in the Public Procurement Regulatory Commission. (to be achieved by an amendment to the LPP)	UNMIK/PISG to draft Government to adopt Assembly to pass SRSG to promulgate			X
	c) Abolish the Public Procurement Rules Committee. (to be achieved by an amendment to the LPP)	UNMIK/PISG to draft Government to adopt Assembly to pass SRSG to promulgate			X
	d) Establish an independent Public Procurement Review Commission (to be achieved by an amendment to the LPP)	UNMIK/PISG to draft Government to adopt Assembly to pass SRSG to promulgate			X

**Table 11: Action Plan for Public Procurement Reform in Kosovo**

AREA	ACTION	RESPONSIBLE ORGANIZATION	TIMING		
			SHORT-TERM < 6 MONTHS	MEDIUM TERM <12 MONTHS	LONG TERM < 24 MONTHS
Improve transparency and accountability	a) Launch a public-access Internet website carrying full details of public procurement	PPA PPRC		X	
	b) Publish all applications from contacting authorities to use procurement procedures other than the Open Procedure, as well as the decision of the regulatory authority in each case.	PPRC		X	
	c) Publish the annual report of the PPA, PPRC and the Review Commission on the public procurement website.	PPA PPRC Review Commission		X	
Capacity Building	a) Establish a public procurement training program at the Kosovo Institute of Public Administration (KIPA),	KIPA			X

## Section 9: Private Sector

### 9.1 Competitiveness and Participation in Public Procurement

The enterprise sector in Kosovo comprises some 30,000 formal businesses, with many more operating in the informal sector. Most firms are micro-enterprises, registered as sole proprietorships or partnerships and employing fewer than four employees. Very few firms are involved in value-adding activities: 60 percent of firms are engaged in wholesale or retail trade or service activities. The other major sectors, measured by the number of firms active in them, are manufacturing (15 percent), construction (10 percent) and transportation, storage and communications (5 percent).<sup>9</sup>

The privatization of socially-owned enterprises (SOEs) has proven highly political. While three rounds of privatization, involving some 30 SOEs have been completed, the privatization process was suspended in October 2003. Of the more than 500 SOEs in Kosovo, only some 75 to 100 have the potential to be sold as ongoing businesses.

Private sector firms interviewed for this assessment expressed a low level of confidence in the fairness of public procurement processes in which they had participated. They generally had more confidence in the fairness of tenders conducted under rules imposed by external donors (World Bank, DFID) and subject to their scrutiny, than in those under FAI 2/99.

Several bidders complained about unfair competition. This finding was upheld by the results of a recent survey on Kosovo's investment climate undertaken by the World Bank, where 45 percent of respondent firms rated unfair competition as a major or very severe constraint on their business, second only behind electricity supply. Typical of the complaints expressed by private-sector firms is being forced to compete against Non-Governmental Organizations (NGOs) for public contracts, the inference being that, because many NGOs receive charitable contributions, they do not bear their full costs and can feed this advantage into the prices they submit in public tenders. Because of Kosovo's unique circumstances, NGOs implement certain contracts there that they may not be interested in in other countries. For example, the Bank has approved the award of a civil works contract to a foreign NGO, given the difficulty of getting any other entity to execute the works.

Most firms expressed the opinion that the level of detail contained in technical specifications and scope of works included in bidding documents is considerably lower in tenders conducted by UNMIK/PISG than in tenders issued under IFI procurement rules and supervision.

Several private-sector firms also complained about unqualified firms winning public contracts and failing to execute them, generally ascribing this to the contracting authorities' failure to check on the experience and qualifications of bidders before awarding contracts. Some also complained that one of the reasons unqualified firms win contracts is that contracting authorities introduce into the evaluation process criteria which were not cited in the bidding documents, including paying personal visits to bidding firms, ostensibly to check that the bidders actually have the resources claimed in their bids.

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<sup>9</sup> Data reproduced from the World Bank "Investment Climate Assessment" on Kosovo, March 2004.

## **9.2 Performance on Public Procurement Contracts**

While there are no hard data available, the assessment heard many reports of problems experienced in the execution of contracts. Bidders and contractors most frequently ascribed these problems to poor or inaccurate definition of the technical specification or scope of work in the bidding documents or to the contracting authority's failure to assess the qualifications of the winning bidder before awarding the contract. For works contracts, bidders complained that the works are not properly designed, engineered or costed before the bidding documents are issued to the bidders. One contractor, active in road rehabilitation works, reported that it is common for executed contracts to exceed the original price by more than 100 percent.

Given that there is no formal mechanism in Kosovo for reviewing contract performance and performance audits are not conducted as part of internal or external auditing, poor contract execution currently goes unchecked.

## **Annex: List of Contracting authorities Governed by FAI 2/99**

1. Ministry of Public Services
  - a. Central Processing Center
  - b. Department of Local Administration
  - c. Kosovo Cadastral Agency
  - d. Statistical Office of Kosovo
  - e. Department of Engineering and Building Management
  - f. Department of Administration and Support
  - g. Department of Emergency Management
  - h. Department of Information and Technology
  - i. Central Procurement Entity
  - j. Kosovo Institute of Public Administration
  
2. Ministry of Health
  - a. University Clinical Center
  - b. Pharmaceutical Procurement Unit
  
3. Ministry of Economy and Finance
  - a. Central Fiscal Authority
  - b. Tax Administration
  
4. Ministry of Culture, Youth and Sports
  - a. Department of Non Resident Affairs
  
5. Ministry of Education, Science and Technology
  - a. Student's Center
  - b. University of Pristina
  
6. Ministry of Transport and Tele Communications
7. Ministry of Agriculture and Forestry
8. Ministry of Trade and Industry
9. Ministry of Environment and Spatial Planning
10. Ministry of Labor and Social Welfare

Office of the President  
Office of the Prime Minister  
Office of the Kosovo Assembly  
Office of the Community Affairs  
Office of the Missing Persons  
Office of the General Revision  
Office of the KPC Coordinator  
Office of Ombudsperson

## **Municipalities:**

1. Municipality of Pristina
2. Municipality of Prizren
3. Municipality of Gjilan
4. Municipality of Mitrovica
5. Municipality of Istog
6. Municipality of Deçan
7. Municipality of Podujevë
8. Municipality of Fushë Kosovë
9. Municipality of Kamenicë
10. Municipality of Klinë
11. Municipality of Drenas
12. Municipality of Pejë
13. Municipality of Lipjan
14. Municipality of Obiliq
15. Municipality of Vushtrri
16. Municipality of Novo Bërd
17. Municipality of Dragash
18. Municipality of Kaçanik
19. Municipality of Shtërpc
20. Municipality of Ferizaj
21. Municipality of Shtime
22. Municipality of Suharekë
23. Municipality of Viti
24. Municipality of Malishevë
25. Municipality of Rahovec
26. Municipality of Zubin Potok
27. Municipality of Gjakovë
28. Municipality of Skënderaj
29. Municipality of Leposaviq
30. Municipality of Zveçan

Kosovo Police Services

Kosovo Protection Troops

Kosovo Trust Agency

Customs

Banking and Payment Authority

Department of Justice

Housing and Property Directorate

KEK

Trepça



