

ANNEX



European Neighbourhood and Partnership Instrument

GEORGIA

NATIONAL INDICATIVE PROGRAMME

2011-2013

Abbreviations

BDD	Georgia Government ‘Basic Data and Directions 2007-10’
CIB	Comprehensive Institution Building
CPT	Committee for the Prevention of Torture
CSP	Country Strategy Paper
CSOs	Civil Society Organisations
DAC	OECD Development Assistance Committee
DCFTA	Deep and Comprehensive Free Trade Area
DFID	UK Department for International Development
EaP	Eastern Partnership
EC	European Commission
EDPRP	Economic Development and Poverty Reduction Programme
EIB	European Investment Bank
ENP	European Neighbourhood Policy
ENP AP	ENP Action Plan
ENPI	European Neighbourhood and Partnership Instrument
FSP	Food Security Programme
GDP	Gross Domestic Product
IDPs	Internally Displaced Persons
IFIs	International Financial Institutions
IMF	International Monetary Fund
MDGs	Millennium Development Goals
MTEF	Medium-Term Expenditure Framework
NIP	National Indicative Programme
PCA	Partnership and Cooperation Agreement
REC	Caucasus Regional Environmental Centre
SIDA	Swedish International Development Agency
SPS	sanitary and phyto-sanitary
TA	Technical Assistance
TACIS	Technical Assistance to the CIS
USAID	US Agency for International Development
VET	Vocational Education Training

WB	World Bank
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1. PART I: INTRODUCTION

This new National Indicative Programme (NIP) covering the period 2011-2013 was drafted by the Commission in consultation with the Georgian government, Member States and other international donors and civil society organisations following the Mid-Term Review of the Country Strategy Paper (CSP) for Georgia 2007-2013. The Mid-Term Review undertaken by the Commission concluded that the political, economic and social developments in Georgia between 2007 and 2009 (including the August 2008 war) and the development of new EU policies have changed the dimensions but not the substance of the main challenges identified in the CSP. Also, taking into account Georgia's progress in implementing the ENP Action Plan, the development of new EU policies, and the results and impact of EU assistance to Georgia, the CSP 2007-2013 for Georgia remains largely valid.

In addition to the developments in Georgia and EU-Georgia relations, and the validity of CSP priorities in view of these developments, it is important to note that general changes in EU policies and new key horizontal issues with policy effects were also explored during the CSP Mid-Term Review. These key issues included climate change, migration, aid for trade, rising food prices, drugs trafficking and the current global financial and economic crisis. This NIP was drafted with the aim of mainstreaming these global policy priorities into NIP priorities whenever possible, which should be reflected in the identification of specific actions and targeted groups and in the implementation of interventions.

Developments in Georgia

Since 2007, Georgia has made progress in implementing the ENP AP priorities, especially in democratic development and economic reforms. Progress has been achieved in justice sector reform, improving the business climate and the fight against corruption. Georgia has been and remains committed to European integration.

Nevertheless, during 2007-2009 Georgia was also confronted with grave internal and external crises. In mid-2007, Georgia entered a period of political turmoil, marked by anti-government mass demonstrations and a polarised atmosphere between the ruling majority and opposition parties. Early presidential and legislative elections in 2008 resulted in the re-election of President Saakashvili and gave a landslide victory to the ruling parliamentary majority. The elections were reported to be in line with international standards, by the OSCE/OIDHR, though the reports outlined several irregularities in the conduct of both elections. The opposition parties also criticised the ruling majority regarding the conduct of elections and contested the validity of the results. This resulted in the decision of some opposition parties not to take up their seats in Parliament.

In the course of 2008, Russia took a number of steps to strengthen its relations with the separatist regions of South Ossetia and Abkhazia, including the lifting of CIS economic sanctions and establishing closer political ties. A sequence of military incidents and provocations culminated in August 2008 in the outbreak of an armed conflict with Russia. The hostilities resulted in several hundred fatalities and the displacement of thousands of persons. A ceasefire agreement and a

more detailed implementation agreement were concluded with EU support in August and September 2008.

Following the war, and in the light of the internal political discontent, President Saakashvili acknowledged, in his speech to Parliament in September 2008, that the ‘rose revolution’ had not fully achieved its aim of democratic development. The President clearly stated the need to continue and accelerate democratic reforms and made a public commitment to give new momentum to the development of democracy and rule of law, as set out in an ambitious reform agenda called ‘second wave of democratic reforms’. In April 2009, the political opposition in Georgia started mass demonstrations, demanding the resignation of President Saakashvili. This development, and the criticisms made by the opposition parties, prompted the Georgian government to push forward even further with continuing democratic reforms, encouraging political pluralism, amending the election code and ensuring media freedom.

On the economic front, Georgia’s macro-economic performance was very strong until the conflict in August 2008. Real growth figures were above 9% in 2005 and 2006 and 12% in 2007. In the first half of 2008 the annual growth rate remained robust at 8.6%. Nonetheless, the conflict in August 2008 dented the strong growth performance of previous years. The global financial crisis developing since late 2008 further aggravated Georgia’s economic situation, where the severe contraction of external financing inflows, combined with the tightening of bank credits, depressed domestic demand. This translated into a sharp fall in both domestic output and imports.

However, thanks to the rapid response from the international community, which culminated in the Donors’ Conference of October 2008, Georgia received extra assistance to cover the unforeseen needs resulting from the conflict¹. At the conference, the EC pledged and immediately started delivering enhanced assistance of up to €500m for the period 2008-2010. This includes funds from different programmes and crisis instruments, including the Instrument for Stability (IfS). The main goal of this instrument is to provide an effective, timely, flexible and integrated response to situations of crisis, emerging crisis or continued political instability.

The EU assistance, in addition to the efforts of the other international donors since the donors’ conference in Brussels in October 2008, has helped significantly in alleviating the effects of the ‘double shock’ on Georgia’s economy. As the recent World Bank–UN Progress Report on Georgia ‘Donor Funding in Support of Post-Conflict Recovery and Reconstruction’ points out, the contraction of the Georgian economy has been ‘less severe than in some other CIS economies’. Consequently, the broad goals outlined in the CSP on sustainable development, to support the overarching goal of poverty reduction in Georgia, remain largely valid.

Overall, these exceptional events represented a setback for the ambitious process of reform and conflict resolution undertaken by Georgia since the 2003 ‘rose revolution’. However, rather than creating new challenges, these developments demonstrate the need to pursue the objectives on democracy, rule of law, media freedom, good governance, trade and economic integration, as already identified in the CSP 2007-13 and included in the EU-Georgia ENP Action Plan.

Developments in EU-Georgia relations

¹ A Joint Needs Assessment (JNA) document was jointly prepared for the donor conference by international institutions. The JNA identified extra needs amounting to \$3.25 billion over a three-year period. Donor pledges totalled \$3.7 billion, plus an additional \$800 million to support the private sector, including banks.

Until a new agreement is negotiated and enters into force, that EU-Georgia **Partnership and Cooperation Agreement (PCA)**, which has been in force since 1 July 1999, will remain as the legal basis for cooperation between Georgia and the EU. The **European Neighbourhood Policy Action Plan (ENP AP)**, adopted on 14 November 2006, sets out the mutually agreed political priorities for cooperation and is valid until 2011 with a possible extension until the conclusion of a successor document (if the ENP Action Plan is replaced by another document during the implementation period of this NIP, the successor document should be used to guide assistance). In general, Georgia has demonstrated a strong commitment towards implementation of the priorities outlined in the ENP Action Plan.

The principal objective of EU assistance to Georgia, as broadly outlined in the **CSP 2007-2013**, is to support the development of increasingly closer relations between Georgia and the EU, in the context of the PCA and ENP AP. While, as envisaged in the CSP, relations between Georgia and the EU have been intensifying during the past years, there have been no significant changes or shifts in the legal framework for bilateral relations or in the policy orientation of the Georgian government.

Following the war in Georgia, the European Council decided in its conclusions of 1 September 2008 to ‘step up relations with Georgia, including ... the possible establishment of a full and comprehensive free trade area as soon as the conditions are met’. In line with these conclusions, the Commission took several measures to step up relations with Georgia. This included the enhanced assistance package of up to €500 million for the 2008-2010 period and the organisation of an International Donors’ Conference for Georgia, together with the World Bank, in October 2008, which raised €3.44 billion for Georgia’s recovery from the conflict.

In October 2008, a trade mission of several Commission experts was carried out to Georgia in order to assess the country's preparedness for negotiating, implementing and sustaining a deep and comprehensive free trade area (DCFTA) with the EU, and on the basis of this assessment establish in particular a set of key recommendations that Georgia would need to implement before DCFTA negotiations could be launched. Enhancing trade relations is also an objective of the new Eastern Partnership as specified further in this section. Consequently, trade issues and related regulatory reforms are increasingly gaining importance in EU-Georgia relations and need special attention in the 2011-2013 period.

Moreover, negotiation mandates for visa facilitation and readmission agreements were prepared by the Commission and approved by the Council in November 2008. Negotiations started in April and were to be finalised in November 2009. Georgia signed a Joint Declaration for an EU-Georgia Mobility Partnership with the EC and interested EU Member States.

In addition to the measures taken following the conflict, it is important to note that the EC has also concluded negotiations on an enhanced aviation agreement with Georgia, and the negotiations on geographical indications for agricultural products are continuing

In May 2009, the **Eastern Partnership (EaP)** was launched in Prague to deepen relations between the EU and six neighbouring Eastern countries, including Georgia, as well as among themselves. Georgia has shown great interest in the Eastern Partnership, both in the prospect of deeper political cooperation and trade and economic integration with the EU and in deepening regional relations with other EaP partner countries.

The deepening of EU-Georgia relations implies an ambitious agenda for deeper bilateral engagement by upgrading contractual relations in the form of an enhanced agreement

(Association Agreement). This would include i.a. the objective of establishing a deep and comprehensive free trade area (DCFTA) between Georgia and the EU once the necessary conditions are met. In September 2009, the Commission was tasked by Member States to prepare draft negotiating directives for the enhanced agreement's negotiations with the three South Caucasus countries and these draft directives were subsequently adopted by the College on 30 October (2009). Both the political and trade/economic aspects of these negotiations will require continuing progress on reforms and the fulfilment of certain conditions. The EU should aim to help Georgia achieve these objectives under this NIP. Energy is also a core area of the Eastern Partnership, where the EU and Georgia have a mutual interest in developing a robust regulatory framework, in line with the EU *acquis*. As these priorities are already broadly contained within the policy priorities of the CSP, the deepening of relations in these areas does not call for rewriting or extensive revision of the CSP.

Georgia is also covered by the **Black Sea Synergy**, a regional cooperation initiative covering the five eastern ENP countries as well as the Russian Federation and Turkey. The Black Sea Synergy is an EU sea-basin inclusive initiative aiming to solve problems that require region-wide efforts. The implementation of the Black Sea Synergy involves, *inter alia*, the establishment of partnerships, like the one concerning environment to be launched soon. Other sectors and cooperative schemes are currently also being explored.

Therefore, this Indicative Programme supports not only the priorities for implementation of objectives under the PCA and ENP Action Plan but also the priorities of the Eastern Partnership and other regional cooperation initiatives.

As regards **technical and financial cooperation**, the current National Indicative Programme for Georgia (2007-2010), in line with the CSP 2007-2013, sets out four key priority areas for EU assistance to Georgia. These priority areas and the indicative budget for each are:

Priority areas	€m	%
(1) Support for democratic development, rule of law and governance	31.5	26%
(2) Support for economic development and ENP AP implementation	31.5	26%
(3) Poverty reduction and social reforms	38.4	32%
(4) Support for peaceful settlement of Georgia's internal conflicts	19.0	16%
Total indicative ENPI allocation 2007-10	120.4	100%

Due to the comparatively long lead times for the implementation of EU programmes, no programmes under the current NIP have been completed at this time. Hence, it is difficult to draw concrete lessons from current ENPI programmes. However, the wide range of consultations carried out with stakeholders indicate the need to ensure continuity in implementing the general priorities identified under the NIP 2007-2010 and consolidation of reforms supported by the EU.

Though the general priority lines do not change, interventions under this NIP will need to be better targeted. The identification and focusing of priorities under this NIP, compared to the NIP 2007-2010, thus reflects the following considerations:

- The scope of potential interventions in the area of ‘Support for the settlement of Georgia’s internal conflicts’ needs to be adjusted to the new status-quo after the August 2008 war. The focus of EU assistance has already started shifting towards mitigation of the human consequences of the internal conflicts and creating the necessary conditions for the settlement of the conflicts, in addition to the economic rehabilitation programmes and confidence building measures, which were previously the only focus.
- To be able to consolidate the reforms and assistance provided on good governance and in the development of a modern state, oriented towards the needs of its citizens, support for civil service reforms requires special attention.
- As outlined above, for strengthening democratic institutions and enhancing political pluralism, support for human rights and media freedom should be further encouraged. This point is supported by highlighting the need for civil society development, encouraging the systemic involvement of CSOs at all stages of programming and implementation.
- The environment protection aspect, in ensuring sustainable social, economic and regional development, should be more specifically outlined.
- The prospect of deepening relations and the ambitious bilateral and multi-lateral cooperation agendas under the Eastern Partnership should be mainstreamed in the priorities.

2. PART II: THE INDICATIVE PROGRAMME FOR 2011-13

2.1. Main priorities and goals

Assistance provided under this National Indicative Programme for Georgia will focus on four main priority areas and will cover a maximum of eight sub-priorities.

Priority area 1: Democratic development, rule of law, good governance

Sub-priority 1.1: Media freedom, political pluralism, human rights, civil society development

Sub-priority 1.2: Justice sector reform

Sub-priority 1.3: Public finance management and public administration reform

Priority area 2: Trade and investment, regulatory alignment and reform

Sub-priority 2.1: Export and investment promotion, in particular through market and regulatory reform; preparations for a future deep and comprehensive FTA with the EU

Sub-priority 2.2: Sector-specific regulatory alignment and reforms in line with PCA/ENP AP priorities

Priority area 3: Regional development, sustainable economic and social development, poverty reduction

Sub-priority 3.1: Social reforms and social protection

Sub-priority 3.2: Regional development and sustainable development, including environmental protection

Sub-priority 3.3: Education, skills development and mobility

Priority area 4: Support for peaceful settlement of conflicts

The extensive cooperation between the partner country and the EU based on the Eastern Partnership policy framework and existing and possible future contractual relations requires that the ENPI NIP for the period 2011-13 covers a relatively broad range of priority areas. The NIP priority areas in this programme should be covered during the programming period 2011-13. However, the indicative nature of the Programme provides certain flexibility regarding the implementation of sub-priorities. The identification process for Annual Action Programmes provides an opportunity to assess the suitability and timeliness of addressing the sub-priorities, in accordance with the evolution of EU policies and sector developments, to adapt the proposed measures and to better focus the expected achievements for specific measures. In this respect, in order to ensure the necessary flexibility, expected results and related indicators are indicative and should be adjusted according to the specific design of the Annual Action Programme. In this process, care should be taken to ensure implementation of those sub-priorities of key importance for deepening the relationship with the EU in the context of the Eastern Partnership and supporting reforms.

2.2. Indicative budget

Under the NIP 2011-2013 Georgia will receive €180.29m from the European Neighbourhood and Partnership Instrument (ENPI). This includes the additional allocations from the Eastern Partnership of €30.86m for the Comprehensive Institution Building programme (CIB) and €7.43m for regional development programmes. If the CIB cannot be agreed or its implementation is delayed, these funds will be fully or partly reallocated to other programmes.

Priority areas	€m	%
(1) Democratic development, rule of law, good governance	45-63	25 – 35 %
(2) Trade and investment, regulatory alignment and reform	27-45	15 – 25 %
(3) Regional development, sustainable economic and social development, poverty reduction	63-81	35 – 45 %
(4) Support for peaceful settlement of conflicts	9-18	5 – 10 %
Total indicative ENPI allocations 2011-2013	€180.29	100 %

2.3. Priority areas

2.3.1. Priority area 1: Democratic development, rule of law, good governance

Support for democratic reforms, the rule of law and good governance is a key priority at the heart of EU-Georgia bilateral relations. This priority is directly linked to the first general priority area, chapter 4.1.1, in the EU-Georgia ENP Action Plan. Since the start of implementation of the ENP

Action Plan priorities, and with the EU assistance under the NIP 2007-2010, some progress has already been achieved in this field. However, internal political developments, unrest and demonstrations by the opposition and criticisms of the conduct of the Presidential elections in January and the legislative elections in May 2008 show the need for continuing democratic reform efforts, with the long-term aim of democratic consolidation.

Consequently, the European Commission should remain fully engaged in monitoring and supporting developments in this area. Specifically, the Commission should support progress in developing fundamental freedoms, civil society, reform of the justice sector, public administration and public finance management.

EU support in this area will be able to build on ongoing interventions, such as the ongoing sector budget support programmes for public finance management and criminal justice sector reform, as well as targeted projects, technical assistance and twinning programmes. In the current Sector Policy Support programme (started in 2008) for criminal justice reform, the basis for sustainable sector management has been established by updating the Criminal Justice Reform Strategy and its related Action Plan and by establishing a sector management system, via the introduction of strategic planning tools, statistical instruments and monitoring structures.

The EU Sector Policy Support Programme in the public finance management area (started in 2007) has contributed to the successful implementation of various reforms, including the introduction of risk-based taxation and customs control procedures and the development of a government-wide system of internal financial control. These reforms will need to be further deepened through continuous EU assistance.

There are already several donors active in this field, with smaller-scale projects and interventions. However, due to the broad scope of this priority and the wide range of projects required, there are opportunities for several donors to work together, though effective donor coordination is essential. EU assistance in this area, as in the case of the above-mentioned sector support programmes, would be particularly important in helping Georgia develop longer-term strategies and action plans, to complement the relatively smaller-scale assistance provided by other donors.

2.3.1.1. Sub-priority 1.1: Media freedom, political pluralism, human rights, civil society development

Long-term impact

The expected long-term impact is the strengthening of democratic institutions and greater political pluralism, widespread acceptance of democratic values, and lasting results in democratisation of the country.

Specific objectives

Improved division of powers, checks and balances, media freedom and respect for human rights and fundamental freedoms, in line with international and European standards. Ensured sustainability and success of democratic reforms with the cooperation and involvement of civil society actors in policy making and monitoring processes.

Expected results

- Strengthened capacity of democratic institutions, including the Ombudsman and the Parliament.

- Enhanced respect for human rights (in particular women’s and children’s rights), including increased awareness within law enforcement bodies.
- Increased involvement of civil society in policy-making structures.
- Secured freedom of expression and freedom of the media.
- Improved quality of the electoral process and administration in line with international standards.

Indicators of achievement²

- Ombudsman and Parliament fulfil their constitutional and legal functions.
- Improved and enforced legal administrative framework to secure freedom of expression and freedom of the media, also with regard to ownership and journalists’ rights.
- Improved electoral administration in line with international standards and better informed electorate.
- Implementation of recommendations made in the Universal Periodic Review of Georgia by the UN Human Rights Council.
- Functioning of the National Preventive Mechanism (NPM) under the Optional Protocol of the UN Convention Against Torture (OP-CAT).

2.3.1.2. Sub priority 1.2: Justice sector reform

Long-term impact

The expected long-term impact is the development of a modern state oriented towards the needs of its citizens and increased public confidence in the justice system.

Specific objectives

The objective is to strengthen the rule of law and ensure more effective functioning of the judiciary, increasing public confidence in the judiciary in Georgia.

Expected results

- Increased public confidence in the judiciary and law enforcement authorities.
- Improved access to justice and guaranteed access to representation for all, including women and vulnerable groups, and continued involvement of specialised civil society organisations.
- Establishment of a comprehensive juvenile justice system in compliance with international standards.

² All general indicators set out in this NIP will need to be further aligned (and specified) in the Annual Action Programmes.

- Improved detention conditions in line with the recommendations of the Council of Europe Committee for the Prevention of Torture (CPT).
- Strengthened capacity of justice institutions and other relevant Georgian services to apply / approximate / adhere to EU Standards in Justice and to cooperate fully with European partners in the area of justice, freedom and security.

Indicators of achievement

- Regular updating and publication of relevant policy and planning documents, supported by enhanced monitoring capability and improved collection and analysis of data for assessment of the status and impact of reforms.
- Broadening of outreach activities, to facilitate access to justice, and expansion of the responsibilities and capacity of the Public Lawyer's Service (legal aid).
- Significant increase in the investigation of alleged politically motivated crimes and abuses by the law enforcement system indicating effective independence of the judiciary.
- Reduction in the numbers in prison (or at least in the growth of the prison population), in line with Council of Europe recommendations.
- Increased use of non-custodial sentences, community orders, probation and early release through parole, development of policies to address the causes of crime (poverty, social exclusion, lack of education and employment opportunities, drug dependency and so forth).

2.3.1.3. Sub priority 1.3: Public finance management and public administration reform

Long-term impact

The expected long-term impact is the development of a sound and transparent public finance management system and a stronger, stable, citizen-oriented public administration.

Specific objectives

Sound management of public finances, with internal and external control systems and public procurement rules in place. Strengthening of administrative capacity and increasing public accountability of government. Effective decentralisation of power.

Expected results

- Implementation of national administrative reform plans, including the strengthening of local government in line with the European Charter of Local Self-Government.
- Improved management of public finances, in particular improvements in budget formulation, implementation and internal/external control.
- Increased transparency of government expenditure, including public procurement.

- Improved public trust in the management of public finances (as demonstrated by improved ranking in the Transparency International corruption perceptions index and WB PEFA Assessments).
- Strengthened government capacity to lead and monitor the implementation of a cross-cutting reform agenda in the public sector.

Indicators of achievement

- State budget preparation and MTEF processes are enhanced through expansion of the sectoral planning and costing capacities of line ministries and local self-governance units.
- Internal control and external audit functions are gradually developed and harmonised with internationally agreed standards (IIA, INTOSAI, IFAC) and methodologies.
- Improved public trust in the management of public finances (demonstrated by improved ranking in the Transparency International corruption perceptions index and PEFA Assessments).
- The legal and regulatory framework for public procurement is in line with the OECD-DAC 4 pillars.
- An operational internal audit function and a risk-based taxpayers' audit system are established within the revenue services.
- Improved access and quality of public services, including at local level

2.3.2. Priority area 2: Trade and investment, regulatory alignment and reform

This priority is directly linked to general priority area 4.5, sub-chapters 4.5.1 to 4.5.5, in the EU-Georgia ENP Action Plan, which covers all trade-related issues and market and regulatory reform.

In order to stimulate sustainable economic growth and address some structural challenges, efforts need to be made to promote exports, improve regulatory approximation with the relevant international and EU laws and standards, including as regards quality infrastructure systems and diversify export capacity. Also, the planned accession of Georgia to the Energy Community requires substantial work on the alignment of legislation with the EU energy and environmental *acquis*. To support this work, emphasis should be placed on strengthening institutional and administrative capacity in all relevant areas to ensure effective implementation and enforcement of the aligned laws and standards.

In June 2009, the Council tasked the EC to negotiate a Common Aviation Agreement with Georgia, and negotiations started in September. The gradual integration of Georgia within the European aviation market may need particular technical support under this priority.

In line with the EaP, this priority would include a support to Georgia's efforts to become ready for negotiating and subsequently implementing a deep and comprehensive FTA with the EU in a sustainable manner. The areas where further reform efforts would be necessary include, in

particular, technical regulation and standards, sanitary and phytosanitary measures, competition policy, protection of intellectual propriety rights, statistics, customs, and taxation.

Trade and related regulatory issues have not been a focal sector for any donor support in Georgia so far. The EU would have a comparative advantage as a donor in this area, thanks to its long experience with the economic integration of third countries.

2.3.2.1. Sub-priority 2.1: Export and investment promotion, in particular through market and regulatory reform; preparations for a future deep and comprehensive FTA with the EU

Long-term impact

The expected long-term impact is positive economic development and prosperity in Georgia, in particular through a better regulated market and enhanced trade and investment between Georgia and the EU.

Specific objectives

The objectives are to facilitate trade and investment between Georgia and the EU, to assist Georgia in preparations to negotiate and implement a future deep and comprehensive FTA with the EU, to support regulatory alignment with, and implementation of relevant EU internal market and international laws and standards, and to ensure institutional and administrative capacity building.

Expected results

- Improved trade environment and increased and diversified trade and foreign direct investment (FDI) in Georgia.
- Implementation of reforms to promote trade and investment, including gradual removal of existing barriers.
- Enhanced institutional and administrative capacity in all relevant areas to ensure effective implementation and enforcement of aligned laws and standards.
- Increased preparedness for a future deep and comprehensive FTA with the EU.
- Strengthened quality infrastructure system, aligned with the EU and international standards.
- Market and regulatory reform measures in the form of gradual alignment of legislation and procedures with EU and international norms, particularly in the areas of technical regulations and standards, sanitary and phytosanitary measures, competition policy, protection of intellectual property rights, statistical standards, customs and taxation

Indicators of achievement

- Improved economic and social development indicators.
- Increased alignment with the EU's internal market and international legislation and procedures, particularly in the areas of technical regulations and standards, sanitary and

phytosanitary measures, and animal welfare, conformity assessment procedures and standards, competition policy, protection of intellectual property rights, statistical standards, customs, and taxation, based on the ENP Action Plan and agreed priorities.

- Strengthened institutional and administrative capacities in all relevant areas.
- Increased levels of trade and more diversified trade commodity structure.
- Improved investment climate demonstrated by increased and more diversified FDI.
- Increased level of preparedness for a future deep and comprehensive FTA with the EU.

2.3.2.2. Sub-priority 2.2: Sector-specific regulatory alignment and reforms in line with PCA/ENP AP priorities

Long-term impact

The expected long-term impact is regulatory convergence with the EU, in key sectors to be agreed on a bilateral basis, and progress with economic and social reform, in line with PCA and ENP AP priorities and the objectives of the EaP.

Specific objectives

Increased regulatory convergence of Georgia's legislation and procedures with the EU in selected key sectors, increased competitiveness and improved environment for businesses in Georgia, alignment and reforms in the area of technical regulations and standards in selected sectors, including transport, energy and the environment.

Approximation and reforms in the area of technical regulations and standards in selected sectors including transport, energy, Information Society and environment.

Expected results

- Implementation of sector-specific regulatory reform and development, with detailed sector strategies, to support broad-based economic growth.
- Improved institutional framework, in particular in transport, energy and the environment.
- Enhanced competitiveness of the economy and better protection of consumers' rights, in line with EU requirements and international standards.
- Enhanced capacities in relevant ministries or state structures to ensure effective enforcement.
- Implementation of legislative and policy reforms in the employment and social areas to align with EU standards.

Indicators of achievement

- Increased level of regulatory convergence with the EU's laws and standards in selected sectors.
- Enhanced energy security through further progress in energy sector reform and regulatory development, as well as progress in the development of energy efficiency and renewable energy.
- Strengthening the Transport Corridor Europe-Caucasus-Asia (TRACECA), through development of transport regulations and standards.
- Integration within European aviation structures and harmonisation with EU aviation (transport) standards to realise the objective of a Common Aviation Area.
- Improvement in aviation safety and security
- Improved employment and social situation, demonstrated by data on job creation and provision of social services.

2.3.3. *Priority area 3: Regional development, sustainable economic and social development, poverty reduction*

This priority is directly linked to general priority area 4.4 'Economic and social reform, poverty reduction and sustainable development', together with sub-chapters 4.5.4 'Movement of persons including movement of workers' and 4.7.1 'Education, training and youth', in the EU-Georgia ENP Action Plan.

Under the EaP, Georgia will receive assistance to address economic and social disparities between regions within the country and increase its internal cohesion by supporting economic and social development. This assistance can take the form of regional development programmes modelled on EU cohesion policy and designed to target local needs. These programmes should be agreed between the Commission and Georgia by mid-2012. To assist Georgia in setting up such programmes, assistance will be provided, as appropriate, in the form of twinning or technical assistance to design the programmes and prepare the implementation structures. These interventions should be based on Georgia's real needs.

Poverty still remains one of the main concerns in Georgia, with 23.6%³ of the Georgian population living under the poverty line. This number is expected to increase to 25.9% due to the consequences of the August 2008 conflict⁴. In 2008, Georgia adopted a new programme called 'Georgia without poverty' for the years 2008-2012, aiming to reduce poverty by developing more efficient social safety nets. Efforts to combat poverty are also one of the key priorities of the country-specific Millennium Development Goals to be achieved by 2015.

Sustainable regional development programmes and support for the development of the agricultural sector would contribute greatly to poverty reduction efforts in Georgia, given that a large part of the poorest social groups live in Georgia's rural areas. The Georgian government has identified regional development as a political priority and in 2008 established a 'Task Force on

³ World Bank Poverty Assessment available on <http://www.statistics.ge/main.php?pform=49&plang=1>.

⁴ Georgia — Joint Needs Assessment, 9 October 2008.

Regional Development’, which is working on a national strategy and action plan for regional development. Under the NIP 2007-2010, the Commission envisages supporting regional development under a sector budget support programme, as of 2010. Consultations with Georgian authorities and civil society organisations have indicated that the national strategy should be supported over the medium to long term. Hence, regional development should remain a key priority for Georgia for continued and possibly increased assistance under the NIP 2011-2013.

In 2007, Georgian government also amended the law on environmental protection adopted in 1996. The government is putting more emphasis on environmental protection and giving more attention to environmental problems⁵. These efforts should also be supported, in line with the sustainable development priority.

To ensure that poverty reduction efforts are successful, social reforms and social protection also need closer attention. Child protection, for which the EC has provided some assistance through the TACIS project, Support for Child Welfare Reform, and the Food Security Programme, should be an integral part of the more general priority of social protection. Gaps in terms of wages and pensions between men and women and the increased burden on women following the deterioration of the social infrastructure will also need to be taken into account. Moreover, in supporting economic development in the regions, it is crucial to consider a number of cross-cutting issues, especially environmental protection⁶ and the civic integration of minorities, given the presence of ethnic minorities in Georgia’s regions.

Currently, the EU is providing assistance in the vocational education and training (VET) sector under a sector budget support programme. However, ensuring the long-term success of this VET programme and strengthening the links between assistance and the needs of the labour market requires continuing attention to skills development for employment, lifelong learning, training and mobility. The adaptability of the education system needs to be improved to meet labour market demands. These issues are also identified as priorities under the forthcoming Mobility Partnership between the EU and Georgia. Hence, education (including science and people-to-people contacts), skills development and mobility should be established as new priorities.

2.3.3.1. Sub-priority 3.1: Social reforms and social protection

Long-term impact

The expected long-term impact is a reduction in poverty levels, a reduction in social inequalities and disparities, improved living standards and a better social environment in terms of social protection, employment and social dialogue.

Specific objectives

Improved social protection system and employment opportunities based on decent work, and social protection, including the protection of women and children. Progress towards achieving the country-specific Millennium Development Goals (MDG)⁷.

Expected results

- Progress towards achieving MDG indicators for Georgia.

⁵ See Annex 6: Country environment profile.

⁶ See Annex 6: Country environment profile.

⁷ See Annex 2: Millennium Development Goals for Georgia.

- Increased child protection standards safeguarded by relevant regulations and effective implementation of legislation.
- Improved social safety nets and protection, as outlined in the ‘Georgia without poverty’ programme and continued pension reform.
- Improved access to social services for all vulnerable groups, in particular women and those living in poverty-line.
- Improved coherence and efficiency of different social protection and social assistance schemes

Indicators of achievement

- Lower/decreased proportion of population living under the poverty line.
- Higher net enrolment ratio in school education and improved pupil performance indicators.
- Lower child and maternal mortality rates.
- Improved performance of the social protection system and existence of adequate safety nets.
- Modern social protection system and adequate safety nets, continued pension reform.
- Continued social reforms and implementation of priorities under the ‘Georgia without poverty’ programme.
- Public expenditure in social protection
- Ratio of the population entitled to access to social protection schemes/programmes
- Range of/level of access to social assistance services provided for vulnerable groups. Continued social reforms and implementation of priorities under ‘Georgia without poverty’ programme

2.3.3.2. Sub-priority 3.2: Regional development and sustainable development, including environmental protection

Long-term impact

The expected long-term impact is reduced regional disparities, broader economic development through sustainable policies, mainly in rural and poor urban areas, and an improved social, economic and environmental situation in Georgia’s regions.

Specific objectives

To foster economic and social development in the regions and reduce regional and social disparities, with a focus on the integration of vulnerable groups. To integrate environmental and climate change considerations within development programmes. To stimulate economic opportunities and cooperation between regions in Georgia and the EU.

Expected results

- Enhanced economic growth, reduced income disparities and social approximation of Georgian Regions
- Implementation of reforms and establishment of necessary structures with regard to environmental issues.
- Development of policies for environment protection and sustainable use of resources.
- Integration of local and regional development and environmental policy within the national development plan.
- Enhanced capacities of local authorities to develop local and regional plans (including issues such as: decentralisation of functions and powers of central government, financial autonomy, etc.) and to implement development projects.
- Enhanced agricultural production and market access (both internal and external) for Georgian agricultural output. Increased quality of Georgian products and increased opportunities for sustainable farming and for agro-processing industries with emphasis on innovation and new technologies.
- Increased economic and social integration of Georgia's minorities living in rural and mountainous areas (including IDPs).

Indicators of achievement

- Reduction of people living below poverty line in regions; or/and Reduction of income disparities among regions (Gini Coefficient can be used at this purpose)
- Increase in agricultural productivity and trade in agricultural export and non-export commodities and in the volume of alternative economic activities.
- Improvements in local, municipal and regional infrastructure, including transport and communication.
- Improved institutional setup for protection and preservation of the environment.
- Increased planning and administrative implementation capacity at local and regional levels, with improved provision of, and access to, quality services.
- Increased access to basic services and infrastructures and employment opportunities in rural and poor urban communities.

2.3.3.3. Sub-priority 3.3: Education, skills development and mobility

Long-term impact

The expected long-term impact is development of the economy and social stability, along with improved economic competitiveness in Georgia.

Specific objectives

Support human resource development; strengthen links between education, training, skills development and the needs of the labour market, facilitating access to jobs and mobility. Support further modernisation of education and training systems, including vocation education and training, in order to enhance socio-economic development, to facilitate integration into the European Higher Education Area and the European Research Area.

Expected results

- Improved quality, capacity and relevance of the education and training systems and their convergence with EU standards and practices, including greater participation of both male and female students at all levels as well as in relevant exchange programmes.
- Improved employment policies and labour market information systems, governance, services and institutions.
- Greater capacity of research structures (human and material resources) with a focus on scientific excellence.
- Decreased barriers to mobility, supported by the relevant regulatory framework and implementation.
- More efficient employment programmes, improved job opportunities and greater labour market participation of women and men.
- Support for the development of education and training programmes targeting specific needs in the labour market.

Indicators of achievement

- Improved education and training systems demonstrated by studies assessing the performance of the systems;
- Further implementation and assessment of the implementation of reforms in higher education according to the Bologna principles and guidelines as measured by the Bologna scorecard.
- Increased participation in EU programmes in the field of education such as Tempus and Erasmus Mundus as measured by the number of applications submitted and proposals selected and increased student mobility.
- Further integration / closer involvement of Georgia into the European Research Area, as measured by an increased number of applications submitted and proposals selected in the 7th EU Research Framework programme, and increased research activity and capacity within universities.
- Closer integration of Georgia within the European Research Area, measured by increased number of (successful) proposals/applications.

- Enhanced employability and reduced inequalities between men and women (including access to social services, employment and incomes). Increased mobility of labour, improved labour market system/management
- Existence of labour market information system
- Number or percentage of jobs mediated by labour market services
- Number of new public programmes in favour of job-seekers, job-matching etc.
- Percentage of public expenditure for labour market measures
- Range of services offered by public labour market institutions or services.

2.3.4. Priority area 4: Support for peaceful settlement of conflicts

This priority is directly linked to general priority area 4.2 ‘Cooperation for the settlement of Georgia’s internal conflicts’ in the EU-Georgia ENP Action Plan.

The European Commission has been one of the biggest contributors to efforts for the peaceful resolution of internal conflicts in Georgia since 1997, supporting confidence building measures and economic rehabilitation projects in both the Abkhazia and South Ossetia conflict zones and also through projects to improve the living conditions of internally displaced persons (IDPs). The overall objective is to support the process of conflict resolution and confidence building and to facilitate progress in constructive dialogue across the conflict divide. Including this priority in the NIP is in line with the Commission’s policy ‘Link Relief to Rehabilitation and Development’ (LRRD).

The hostilities of August 2008 have significantly changed the parameters for EU assistance towards the peaceful settlement of territorial conflicts in Georgia. The self-declared independence of the two breakaway regions has been recognised by Russia, which maintains a strong military presence there. The mandates of the UNOMIG and OSCE missions in Georgia, which played a crucial role in implementing EU-funded conflict-related projects, were discontinued because of opposition by Russia. The Geneva discussions following the August 2008 ceasefire remain ongoing for the time being, as the only forum where security, humanitarian and IDP issues are discussed among all parties involved.

Given the present lack of trust among all sides and the importance of status issues after Russia’s recognition, it is difficult to predict how EU support for conflict resolution will evolve during the period covered by this NIP. However, because of geographic proximity and traditional links, confidence building will remain a major component of EU-supported conflict resolution efforts. It is necessary to provide financial support for the Geneva discussions, which are co-chaired by the EU and where the EU is involved particularly in IDP and rehabilitation issues. It should be also noted that the mandate of the EU Monitoring Mission in Georgia has been extended until mid-September 2010 as part of a coherent EU approach to the region. The Mission’s tasks will concentrate on stabilisation and normalisation efforts on the ground, complementing confidence building measures

As regards IDPs, the EU has been supporting the resettlement of persons displaced from the 2008 war as well as continuously encouraging and supporting the reintegration of people displaced

since 1992. During the period covered by this NIP, the Commission aims to continue its support to improve the living standards of all IDPs while creating the conditions for their safe and dignified return, taking into account the IDP strategy and related action plan established by the Georgian authorities in cooperation with UNHCR and other agencies. Also, the people living in the conflict zones should benefit from infrastructure rehabilitation and projects supporting their livelihoods. The gender dimension of the situation of IDPs will have to be taken into account, such as the needs of female victims of violence as a result of the conflict, women's empowerment in communities around 'collective centres', women's peace activism, initiatives for peace resolution, and participation in reconstruction processes, etc.

Long-term impact

The expected long-term impact is stimulation and support for all efforts towards confidence building and the peaceful settlement of conflicts, to mitigate the consequences of conflicts.

Specific objectives

To contribute to confidence building between communities and address the needs of IDPs and returnees, mainly through resettlement and reintegration efforts, livelihood projects and support for creating conditions to ensure their safe and dignified return. To contribute to the development of conflict settlement mechanisms and peace plans.

Expected results

- Lowered tensions and mistrust between all parties and improved living standards for all people displaced or otherwise affected by the conflict.
- Continuation and success of the Geneva discussions; prevention of new outbreaks of violence.

Indicators of achievement

- Creation of an environment conducive to the final settlement of conflicts.
- Implementation of rehabilitation and reconstruction projects, creating conditions for the safe and dignified return of IDPs.
- Contribution to the development of conflict settlement mechanisms and peace plans.
- The contribution of women to peace processes as enshrined in UN Security Council resolutions 1325 and 1820.

2.4. Implementation

Sector budget support programmes seek to enhance policy dialogue and increase government ownership in the reform process. Their design should be coherent with the priorities of the ENP APs (and/or equivalent documents) and their implementation should be linked with the ongoing policy dialogue. The identification of these programmes should be based on a Sector Readiness Assessment. The existence of a well-defined sector strategy, a sound macro-economic framework, and a sound public finance management system are necessary preconditions for sector budget support operations.

Initial analysis of the use of sector budget support in Georgia shows that it requires a long preparatory phase in order to address all the relevant areas important for sector support. In many sectors, no long-term strategy documents or systems for monitoring and evaluation and for sector coordination exist. However, since budget support programmes have only recently started and it is difficult to draw far-reaching lessons from their early phases, their further implementation should be monitored closely during the period of the NIP 2011-2013 to ensure their effectiveness in achieving ENPI objectives. Lessons learnt to date point to the need to ensure the readiness of sectors before embarking on budget support, to work in close partnership with other donors in preparing and implementing programmes, and to carefully identify, communicate and monitor disbursement criteria, including in public financial management. The experience of NIP 2007-2010 implementation also shows the need for strong dialogue with the Georgian government throughout the process. Reforms currently supported through budget support operations will in many cases require further support under the NIP 2011-2013 to become sustainable.

It is also important to underline that too many small, stand-alone measures would result in administrative overload that could hamper implementation in general. Instead, annual Action Programmes based on this NIP should contain a limited number of components with inbuilt flexibility. General Budget Support could be considered provided it is demonstrated that this aid delivery mechanism can effectively support the priorities of the NIP. If a priority area is not sufficiently mature for sector budget support, the use of other forms of support and capacity-building is encouraged, especially in the form of technical assistance and twinning programmes.

Where relevant, stakeholders (including civil society organisations) should be consulted on the design of the specific measures to be implemented under this programme, and might be involved in the monitoring process. As appropriate, civil society organisations should be supported in their role of promoting reform and increasing public accountability in the sectors supported by the NIP. The European Commission already supports civil society development through the European Instrument for Democracy and Human Rights and the Non-State Actor and Local Authorities programmes. Consultations with civil society actors and the Georgian government have shown that there is scope for formalising their ongoing informal policy dialogue in identifying specific actions and monitoring progress on the implementation of priorities. Consequently, the establishment of a tripartite dialogue to allow regular exchanges between the EU delegation, CSOs and the Georgian government would be a good step forward.

Support for infrastructure rehabilitation and development as part of a programme addressing a NIP priority area should, as a general rule, be designed in close cooperation with the EIB, the EBRD and other International Finance Institutions. If such support can be financed through the Neighbourhood Investment Facility (NIF), this should normally be considered as the first option. Whenever interest rate subsidies are considered, their relevance will be assessed on a case-by-case basis, and care should be taken to avoid significant market distortions.

Georgia may receive support to co-finance participation in EU programmes, insofar as these are open to the country⁸. Resources for enhanced sector cooperation between relevant EU agencies and interested public bodies and authorities in Georgia will be provided as appropriate under the ENPI Inter-Regional Programme 2011-13.

⁸ This support must not exceed 10% of the programme budget, should be phased out degressively over time and, as a general rule, cannot cover more than 50% of the costs of participation.

Climate change is a key challenge affecting the global community across a wide range of policy areas (including air, water, waste, nature protection, industrial pollution, agriculture, forestry, fisheries, energy, transport, infrastructure and urban planning, tourism, human, animal and plant health, education, research). In implementing this indicative programme, considerations regarding climate change causes (mitigation) and effects (adaptation) will be integrated (if possible) within relevant areas of intervention. Available climate risk screening methodologies will be used in the different stages of the implementation process to improve the climate resilience of activities in the chosen area of cooperation.

The priorities set out in the NIP will be underpinned and supported by the results of research and development. In this regard, Georgia is encouraged to increase investment and capacity in research and development, in particular through an increased level of involvement of Georgian research entities in the 7th Framework Programmes (FP7)⁹.

Also, concerns stemming from the internal situation in Georgia, such as the integration of minorities, internally displaced people and environmental matters, need to be generally covered in a comprehensive and horizontal manner under the programmes identified under this NIP. For example, continued social reforms and poverty reduction assistance should also address the needs of all vulnerable groups (including minorities, IDPs, etc.) and economic development assistance should focus on sustainable development, taking into account environmental concerns. Gender as a cross-cutting issue will be mainstreamed in all assistance measures.

In 2005 the Commission identified eleven priority areas¹⁰ where attaining ‘policy coherence for development’, i.e. synergies with development policy objectives, is considered particularly relevant. As a policy-driven instrument, the ENPI is particularly well-placed to accommodate this. As a result, the programmes and activities described in this NIP will — where possible — be designed in such a way as to create these synergies with Georgia’s national development and reform policy objectives.

The Eastern Partnership Comprehensive Institution Building Programmes

More intense bilateral cooperation under the Eastern Partnership provides the foundation for Association Agreements (AA) which would include i.a. the objective of establishing Deep and Comprehensive Free Trade Areas (DCFTAs) once the necessary conditions for it have been met. These Association Agreements will deepen political association and foster trade and economic integration by, among other things, promoting further convergence towards EU legislation and standards.

The Comprehensive Institution Building programme (CIB) is a medium-term planning and implementation framework developed jointly by the Commission and Georgia. It is intended to assist Georgia with institution building for a limited number of core institutions that are central in preparing the ground for and implementing future Association Agreements, which would include i.a. the establishment or objective of establishing, and a deep and comprehensive free trade area (agreement-driven). It will focus on a few selected core institutions (or clusters of institutions)

⁹ See http://cordis.europa.eu/fp7/home_en.html for full information on FP7.

¹⁰ Trade; environment; security; agriculture; fisheries; social dimension of globalisation, promotion of employment and decent work; migration; research and innovation; information society; transport; energy.

that will have a central role in implementing the new Association Agreements. Through a comprehensive approach it will seek to enable the institutions at the end of the programme to assume the obligations stemming from these new agreements. It will be based on clear commitments from the partner country and be co-financed in cash and or kind.

The CIB will be agreed by the Commission and the Georgian government. A Framework Document will identify the CIB core institutions. Based on the Framework Document, institutional reform plans will be designed for selected institutions during 2010 in partnership with government representatives and EU Member States interested in contributing to the CIB. Preparatory and initial CIB measures may start in 2010 with full CIB financing to implement the institutional reform plans, provided through Action Programmes drawn up on the basis of this NIP 2011-2013. The CIBs will be implemented through, for example, the provision of advice and training to the selected public institutions as well the provision and delivery of EU-standard equipment and the specialised infrastructure needed for its operation. Support will be provided using existing instruments such as twinning and TAIEX as well as high-level advice and new innovative mechanisms. In order to ensure coherence, the CIB will build upon relevant aspects of ongoing cooperation activities.

A minimum of €30.86m from the indicative allocation is earmarked for the CIB. Additional ENPI resources may be added as appropriate to strengthen the CIB and finance accompanying measures. If the CIB programme cannot be agreed or its implementation is delayed, these funds will be fully or partly reallocated to other programmes.

2.5. Risks and assumptions

The key assumption underpinning this Programme is Georgia's continued commitment to the reform agenda and policy objectives in the jointly agreed EU–Georgia Action Plan and the underlying Partnership and Cooperation Agreement (PCA). Should this assumption no longer hold true, as a result of major policy changes on the Georgian side, the priorities under this Indicative Programme and the underlying Country Strategy Paper might have to be subject to an early review. However, given the strong commitment expressed by the Georgian government, and the majority of the opposition parties, in support of the policies pursuing integration with the EU, a major change of policy on the Georgian side can be considered a low risk.

As regards the aid delivery mechanisms and financing methods, such as budget support, the assumption is that the current approach of the Georgian government towards developing effective planning and budgeting instruments will be further extended to all relevant policy areas. The continued improvement of public finance management, with donor support as appropriate, and a stable macroeconomic framework will also be necessary. In adapting to new aid delivery mechanisms for assistance delivered under the NIP 2007-2010, one of the main challenges faced was the lack of a common understanding between the EU and the government of Georgia on principles of good governance and sustainable cooperation. There was a clear need to base assistance on sector policies developed in consultative and transparent processes, which is the key to ensuring the sustainability of government programmes. Cooperation with the Georgian authorities in developing common approaches and in ensuring transparent consultative processes in policy making should continue.

Moreover, it is important to further strengthen the transparency and effectiveness of sector reform policies, which can be done by including costed action plans in the government budget and Mid-Term Expenditure Framework. Additionally, in all bilateral contacts, the Commission

consistently encourages Georgia to sign the Paris Declaration, explaining that the discussion leading to this signature could also provide a useful opportunity for debate on basic principles of cooperation.

2.6. Alignment, harmonisation and consultation

The Georgian authorities were widely consulted during the preparation of this NIP in the course of two programming missions in February and April 2009¹¹. In addition to the programming missions, the EU delegation in Tbilisi ensured continued communication with the Georgian authorities, who submitted written comments. It was agreed that the future assistance strategy and priorities outlined in this indicative programme should be jointly established and be based on the policy objectives of the EU–Georgia Action Plan and the priorities of the Eastern Partnership. Therefore, reflecting the ambitious agenda for deepening bilateral relations between the EU and Georgia, a high number of priority areas were selected in order to allow for flexibility in Commission assistance and intervention as needed. Although the broad priority areas are broad, the sub-priorities and objectives focus on aspects where needs are significant and can be meaningfully addressed through the EU assistance modalities. In preparing this NIP, the Commission paid specific attention to the comments received from stakeholders during the consultation process.

Donor coordination and aid effectiveness as enshrined in the Paris declaration on aid effectiveness and the Accra Agenda for Action are important principles for the Commission, and have been taken into account in developing this NIP. In the consultation process that led to the preparation of the programme, all major donors, CSOs, IFIs and Member States active in Georgia, in addition to the Georgian authorities as mentioned above, were consulted both in writing and through round-table discussions during the programming missions. The concept note for the NIP 2011-2013 was also put on the website of the European Commission for public consultation. A number of international organisations, Member States and CSOs submitted their comments in writing. Also, during the programming process, extensive work was done to analyse donor activities by compiling donor matrices¹² on support for the chapters of the ENP Action Plan.

As a general principle, in programming this NIP the Commission refrained from prioritising areas where other donors are deeply involved with long-running sector support programmes. It did this only where other donors' activities are in the form of smaller or pilot projects, and where the EU can bring in added value by stimulating wider policy development. This is to ensure complementarity between donors, and to have a maximum combined impact given each donor's own comparative advantage. The Commission considers its comparative advantages in delivering assistance are in areas such as sector reform, public administration reform, policy development, alignment with EU standards, and institution building. Many donors in Georgia are currently providing short-term support in the form of pilot projects or technical assistance. Donor activity in Georgia increased significantly after the August 2008 conflict and the donors' conference pledges in October 2008. However, these activities normally cover only the period 2008-2011, and it is difficult to foresee if the extent and scope of donor activity will remain the same as today, during the period covered by this NIP (2011-2013).

¹¹ See Annex 5: CSP MTR consultations and NIP 2011-2013 drafting process.

¹² See Annex 4: Donor Matrix.

On donor coordination in specific priority areas, the Commission believes the main responsibility for and ownership of a donor coordination system should be with the Georgian government, in close cooperation with the local donor organisations. So far, in view of the current programming and the significant volumes of additional post-conflict assistance that Georgia is receiving, donor coordination efforts by the government have not been fully satisfactory. As close donor coordination is important in preparing and implementing assistance programmes, while ensuring that efforts remain complementary and do not overlap, the EU has been encouraging the Georgian authorities to take steps to improve such coordination. Consequently, new structures, reforms and information channels are being introduced by the government, in dialogue with all donors and the CSOs in order to address the concerns raised.

Meanwhile, the EU delegation in Tbilisi is taking the initiative to organise regular meetings with other donors and Member State representatives on the ground. More concretely, the Delegation is setting up sectoral working groups for different areas of assistance and is developing information management systems. These meetings aim to improve structural donor cooperation and coordination. While EU support is provided in a number of sectors where some Member States are also active with smaller-scale projects, the regular exchanges ensure that there are no overlaps or duplication between the two.

2.7. ANNEXES

2.7.1. Annex 1: Country at a Glance

Georgia - Main economic indicators

	2005	2006	2007	2008	2009
				prel.	proj.
Real sector					
Real GDP growth (domestic currency, % change)	9,6	9,4	12,3	2,1	-4,0
GDP nominal (EUR, billion)	5,2	6,2	7,4	8,7	7,8
GDP nominal (USD, billion)	6,4	7,7	10,2	12,9	10,6
GDP per capita (EUR)	1201	1415	1679	1987	1781
GDP per capita (USD)	1491	1760	2313	2924	2445
GDP per capita (PPP current prices USD)	3644	4038	4694	4851	
Inflation (period average)	8,3	9,2	9,2	10,0	1,8
Social indicators					
Population (million)	4,3	4,4	4,4	4,4	4,4
Unemployment rate (ILO definition)	13,8	13,6	13,3	16,5	
Poverty rate (% population) ¹	24,1	24,3	24,3		
Inequality (Gini index consumption/ income)			40,4		
Fiscal sector					
Total revenue (incl. grants) (% GDP)	23,4	26,7	29,2	30,7	29,4
Total expenditure (% GDP)	24,9	29,8	25,0	28,5	30,0
General government balance (% GDP, cash basis)	-2,4	-3,0	-4,7	-6,3	-9,6
Public debt (% GDP)		27,6	22,1	25,0	35,7
Monetary sector					
Domestic credit to private sector (% GDP)	14,8	19,7	27,1	30,5	
Broad money (M3) (% change)	26,5	39,7	49,7	6,9	
Degree of monetisation (M3/GDP, %)	14,8	19,5	23,7	23,2	
Dollarisation in bank deposits (%)	71,8	69,4	65,6	75,8	

External sector

Current account balance (% GDP)	-10,9	-15,1	-19,6	-22,6	-15,1
Trade balance (% GDP)	-18,9	-23,9	-28,3	-29,8	-24,7
Foreign direct investment (net, % GDP)	7,1	13,7	17,1	12,2	6,5
Import cover of reserves (months)	1,8	1,8	2,1	2,4	

External vulnerability

External public debt (% GDP)	27,1	22,0	17,5	20,9	31,5
Debt service ratio ²	7,4	7,2	3,5	3,4	6,2
Gross reserves (excl. gold, USD million)	479	881	1361	1480	2005
Reserves/M3	0,45	0,58	0,56	0,51	

Financial sector

Money market rate	7,7	9,5	7,4	10,0	
Lending rate (3-month)	21,6	18,8	20,4	10,2	
Exchange rate (lari per EUR, average)	2,3	2,2	2,3	2,2	2,3
Exchange rate (lari per USD, average)	1,8	1,8	1,7	1,5	1,7
Real effective exchange rate (% change)	3,7	3,7	1,3	8,4	

¹ Poverty incidence with respect to 60% of median consumption

² Public external debt service as % of exports of goods and services

Sources: IMF, WB, Georgian authorities and Commission.

2.7.2. *Annex 2: Millennium Development Goals for Georgia*

Millennium Development Goals
<p>Goal 1: Eradicate extreme poverty and hunger</p> <p>Target 1: Halve, between 1990 and 2015, the proportion of people whose income is less than one dollar a day</p> <p>Target 2: Halve, between 1990 and 2015, the proportion of people who suffer from hunger</p> <p>Target 3: Ensure socio-economic rehabilitation and civil integration of population affected and displaced as a result of conflicts and natural calamities</p>
<p>Goal 2: Achieve universal primary education</p> <p>Target 4: By 2015 maintain universal primary education; ensure the transformation of school education into 12 year cycle; inclusion into the International Systems of School Education Quality Assessment; achievement of institutional coherence with modern school systems</p> <p>Target 5: By 2015 ensure establishment of accreditation system for tertiary education institutions; achievement of institutional coherence with modern tertiary education systems</p> <p>Target 6: By 2015 ensure the transformation of vocational education into the one focused on labour market needs; facilitate the establishment of institutional support to private sector development in vocational education</p> <p>Target 7: By 2015 ensure the function of inclusive educational programmes; incorporate the principles of inclusive education into national study programmes</p>
<p>Goal 3: Promote gender equality and empower women</p> <p>Target 8: Ensure gender equality in employment</p> <p>Target 9: Ensure equal access to activity in the political domain and all levels of management</p>
<p>Goal 4: Reduce child mortality</p> <p>Target 10: reduce by two-thirds, between 2000 and 2015, the under-five mortality rate</p>
<p>Goal 5: Improve maternal health</p> <p>Target 11: Reduce by three-quarters, between 2000 and 2015, the maternal mortality ratio</p>
<p>Goal 6: Combat HIV/AIDS, malaria, and other diseases</p> <p>Target 12: Have halted by 2015, and begun to reverse, the spread of HIV / AIDS</p> <p>Target 13: Have halted by 2015, and begin to reverse, the incidence of malaria and other major diseases</p>
<p>Goal 7: Ensure environmental sustainability</p> <p>Target 14: Integrate the principles of sustainable development into country policies and programmes and reverse the loss of environmental resources</p>

Target 15: Halve, by 2015, the proportion of people without sustainable access to safe drinking water

Target 16: Harmonise housing with international standards, including the development of a municipal (social) tenure component

Goal 8: Develop a global partnership for development

Target 17: Develop further an open, rule-based, predictable, and non-discriminatory trading and financial system

Target 18: Deal comprehensively with the debt problems of developing countries through national and international measures in order to make debt sustainable in the long term

Target 19: Ensure improved accessibility to communication systems countrywide, minimising digital inequality between urban and rural areas

2.7.3. Annex 3: Summary table of focal areas and indicative budget

Assistance provided under this National Indicative Programme 2011-2013 for Georgia will focus on four main priority areas and eight sub-priorities.

Priority area 1: Democratic development, rule of law, good governance

Sub-priority 1.1: Media freedom, political pluralism, human rights, civil society development

Sub-priority 1.2: Justice sector reform

Sub-priority 1.3: Public finance management and public administration reform

Priority area 2: Trade and investment, regulatory alignment and reform

Sub-priority 2.1: Export and investment promotion, in particular through market and regulatory reform; preparations for a possible future deep and comprehensive FTA with the EU

Sub-priority 2.2: Sector-specific regulatory alignment and reforms in line with PCA/ENP AP priorities

Priority area 3: Regional development, sustainable economic and social development, poverty reduction

Sub-priority 3.1: Social reforms and social protection

Sub-priority 3.2: Regional development and sustainable development, including environmental protection

Sub-priority 3.3: Education, skills development and mobility

Priority Area 4: Support for peaceful settlement of conflicts

Indicative budget

Under the NIP 2011-2013 Georgia will receive €180.29m from the European Neighbourhood and Partnership Instrument (ENPI). This includes the additional allocations from the new Eastern Partnership of €30.86m for the Comprehensive Institution Building programme (CIB) and €7.43m for regional development programmes.

Priority areas	€m	%
Democratic development, rule of law, good governance	45-63	25 – 35 %
Trade and investment, regulatory alignment and reform	27-45	15 – 25 %
Regional development, sustainable economic and social development, poverty reduction	63-81	35 – 45 %
Support for peaceful settlement of conflicts	9-18	5 – 10 %
Total indicative ENPI allocations 2011-2013	€180.29	100 %

2.7.4. Annex 4: Donor Matrix¹³

Action Plan area / sector identified for reform	EUROPEAN UNION														Other (non-EU) Donors	
	EC	AT	FI	FR	D	EL	IE	IT	LV	LT	PL	SL	SE	UK	Norway	USA
Political dialogue and reform																
Governance and democracy																
Rule of law (incl. judicial reforms)																
Human rights																
Cooperation with civil society																
Peace and security																
Conflict prevention																
Crises management																
Cooperation on justice and home affairs																
Border management																
Migration and readmission																
Refugees and IDPs																
Organised crime																
Police and judicial cooperation																
Economic and social reform																
Macro-economic reforms																
Employment, poverty reduction and social policy																
Agriculture, forestry and fisheries																

¹³ This matrix is based on the data provided at the EU-US donor conference in December 2007, supplemented with the input provided by the Member States for the Mid-Term Review in the summer of 2009. Donors have supplied the Commission with descriptions of their main programmes and activities, to ensure an optimal division of labour. The matrix forms the basis for the coordination of assistance activities from 2009 onwards with the various donors active in Georgia and will be continuously updated.

2.7.5. *Annex 5: CSP MTR consultations and NIP 2011-2013 drafting process*

Georgian authorities and all relevant stakeholders were widely consulted during the preparation of this NIP in the course of two programming missions in February and April 2009 and through bilateral contacts, wide circulation of the concept paper on the NIP 2011-2013, and its publication on the Commission website. During the programming missions, there were visits to and discussions with the Georgian government, IFIs and other donors, local NGOs and EU Member State Development Counsellors in local representation offices. In the period between and following the programming missions, the EU delegation in Tbilisi ensured continued communication with all local stakeholder representatives, who also submitted written comments on the concept paper.

Local and international stakeholders, institutions, state bodies and Member State representatives who took part in the consultation process and submitted comments were:

Ministries:

Foreign affairs;
Reintegration;
Euro-Atlantic integration;
Economic development;
Regional development and infrastructure;
Finance;
Labour, health and social affairs;
Refugees and accommodation;
Education;
Justice and corrections;
Probation
Office of the Deputy Prime Minister

IFIs and other donors:

World Bank
IMF
USAID
Millennium Challenge Corporation
UNDP

Local and international NGO representatives:

Anti-Violence Network of Georgia
Association of Caucasus Lawyers
Civic Integration Foundation
Eurasia Partnership Foundation
European Choice for Georgia

Georgian Young Lawyers Association
Georgian-European Policy and Legal Advice Centre (GEPLAC)
Green Alternative
Heinrich Böll Stiftung
Inclusive Foundation
International Centre for Migration Policy Development
International Crisis Group
International Society for Fair Elections and Democracy
Open Society Georgia Foundation
UK-Georgia Professional Network
World Vision

Member State Development Counsellors at local representation offices of: BG, CZ, DE, EE, FR, HU, IT, NL, RO, SE, UK

11-13 February 2009: First programming mission — Tbilisi.

Presentation of the MTR process and initial ideas on NIP 2011-2013 to the Georgian government, IFIs and other donors, local NGOs and EU Member State Development Counsellors at local representation offices.

1 April 2009: Country team meeting — Brussels

Consultation with the EC services and line DGs as well as with the EIB on the first version of the concept paper on the NIP 2011-2013.

6 April 2009

Distribution of the concept paper to the Georgian government, IFIs and other donors, local NGOs and EU Member States for comments. Some comments were received in writing in the period that followed.

13-14 April 2009: ENP Workshop — Tbilisi

Workshop on the ENP AP priorities, including a discussion on the MTR and NIP 2011-2013 with NGOs, Georgian government and EU delegation in Tbilisi. Some written comments by NGOs on the concept paper were compiled and submitted to the EC for consideration.

21-23 April 2009: Second programming mission — Tbilisi

Presentation of the draft concept paper on the NIP 2011-2013 to the same interlocutors as in the first programming mission.

30 April 2009

Publication of the concept paper on the EC website for consultation on new indicative programmes 2011-13¹⁴, with a deadline of 20 May 2009 for comments.

5 May 2009

¹⁴ http://ec.europa.eu/world/enp/mid_term_review/index_en.htm.

Georgia submitted extensive comments from all state ministries on the priorities outlined in the concept paper.

30 April – 15 June 2009

Several comments received in writing on the concept paper from other donors, local NGOs and EU Member State local representation offices.

23 June – 14 July 2009

Distribution of and comments on the first draft NIP 2011-2013 by Commission services and line DGs, Georgian government, NGOs, other stakeholders, other donors and Member States.

15 July 2009

Informal consultation by the Commission on revised NIP priorities, sub-priorities (with expected long-term impact, specific objectives, expected results and indicators for achievement) with the Georgian authorities.

23 July 2009

Mid-Term Review discussion with Brussels-based CSO platforms.

5 August 2009

Further submission of comments by Georgia on revised NIP.

The main outcome of the consultation process can be summarised as follows:

- The government is concentrating its efforts on trying to ensure the political and economic stability of the country since the August 2008 armed conflict and in view of the current global economic and financial crisis. Hence, their identified priorities concentrate on actions that will have an immediate impact in 2009-2010. Similarly, most donors on the ground are making efforts to meet current needs and deliver on the pledges of the October 2008 donors' conference, which covers the period up to 2011. This also means that there has not yet been any thorough reflection on priorities beyond this date.
- Due to the comparatively long lead-in times for the implementation of EU programmes, no projects under the current NIP have been completed at this time. For this reason, it is difficult to draw concrete lessons from current ENPI programmes.
- The priorities identified under the NIP 2007-2010 are still valid, and should continue to be supported as priorities until 2013. This would ensure not only continuity in implementing general priorities but also consolidation of reforms supported by the EU through the ENPI. Additionally, these priorities correspond to areas where the EU has the appropriate tools and comparative advantages (right aid delivery mechanisms, know-how and established norms).
- The participation of civil society organisations (CSOs) is important, not only at the programming stage, but also in identifying actions and monitoring progress. CSOs are keen to play a more active role, which should be mainstreamed within EU assistance. The establishment of a tripartite dialogue between the EU delegation, CSOs and the Georgian government could be a good step forward.
- Concerns regarding the integration of minorities, internally displaced people and environment matters should be addressed in a comprehensive manner in the programming of new assistance. For example, continued social reforms and poverty reduction assistance

should address the needs of all vulnerable groups (including minorities, IDPs, etc.), and economic development assistance should focus on sustainable development, taking into account environment concerns. Hence, these areas would not necessarily need to be separate priority areas.

2.7.6. Annex 6: Georgia — Country environment profile

1) State of the environment

The key environment issues in Georgia are air quality, water quality, waste management, land use, coastal and marine pollution, chemicals, and nature protection.

Air pollution, in particular from road traffic, followed by the energy sector and industry, is becoming an important issue. Georgia has about 3 000 stationary sources of air pollution, not many of which work at full capacity. The annual inventory of national emissions of air pollutants is limited to three sectors: energy, industry and transport.

With regard to **water quality**, infrastructure is mostly not sufficient and also outdated. Georgia has nevertheless considerable water resources, but their distribution is uneven due to varying geographic conditions. Data on surface and ground waters is limited. Drinking water quality is of concern, as shortages in infrastructure and contamination from waste water cause problems.

Waste management is a serious challenge, including with regard to prevention, collection, treatment, recovery and final disposal. Stocks of obsolete pesticides constitute an important challenge. There is no overall government strategy on waste management.

As regards **nature protection**, land degradation and desertification are becoming serious issues. Due to falling living standards and reduced controls, illegal logging has increased.

With regard to **coastal and marine pollution**, sources include a number of industrial hotspots, pipelines and oil spills from oil transport.

With regard to **land use**, administrative structures to ensure an effective spatial planning system and management of the environment require particular attention.

Industrial pollution is mainly caused by metallurgy, oil refining, coal mining and the chemical industry, entailing severe pollution.

Current **trans-boundary environment issues** include the use and protection of shared waters — in particular the Kura-Araks river basin and the Black Sea. The Kura-Araks river basin is an essential source of fresh water for the region. Existing problems in the Kura river basin are related to both the quantity and quality of water. Water quality is affected by discharges of municipal and industrial wastewaters and return flow from agriculture. The Black Sea is subject to similar problems, the most serious of which are discharges of wastewater, oil pollution in coastal areas, and loss of biodiversity, including fish stocks.

As regards **global environment issues** and climate change in particular, Georgia acceded to the Kyoto Protocol in 1999, and therefore needs to implement the relevant provisions and, where appropriate, implement concrete policies and measures to reduce greenhouse gas emissions, in particular in the energy and heavy industry sectors.

Georgia's water and waste infrastructure as well as biodiversity were seriously affected by the August 2008 armed conflict.

2) Environment policy

The First National Environmental Action Plan (NEAP) was adopted in 2000 with a 5-year time span. Its six priorities were: rehabilitation and improvement of water supply and sewage systems; increase in the share of municipal transport and monitoring of fuel quality; prevention of pollution by encouraging the introduction of best available techniques (BAT) and cleaner production methods; improvement of waste management through the application of economic instruments; introduction of integrated coastal zone management to address the environmental problems of the Black Sea; and preservation of biodiversity, including that of forest ecosystems. However, only a few of the first NEAP recommendations were implemented, mainly due to shortage of resources.

Updating and finalisation of the draft second national environment protection programme for 2009-2012 is planned. Local environmental action plans are also under development in selected municipalities.

In the field of climate change, Georgia has prepared its climate strategy, adaptation policies and a second national communication on climate change, including vulnerability and adaptation studies. An inventory of greenhouse gas emissions of 2000 – 2006 has been completed, and a first report published in September 2008 has taken steps to prepare and approve further Clean Development Mechanism (CDM) projects. Only one Georgian CDM project has however been registered at the UN level. The European Commission has continued to support Georgia to implement the Kyoto Protocol.

3) Environment legislation and implementation

The Constitution of Georgia establishes basic rules for environmental protection and natural resource use. It also grants all citizens the right to have access to complete, objective and timely information on their working and living conditions.

The law on environmental protection was adopted in 1996, and amended in 2007. It establishes the general legal framework and covers a wide range of issues, including environmental standard setting, licensing of activities connected with natural resource use, issuing environmental permits, keeping state registers of environmental information, and monitoring. Provision is also made for granting tax privileges to those who use best available techniques and low-waste technologies or produce environmentally sound products. The law also lists citizens' environmental rights, outlines general environmental requirements for the production of goods and the generation of waste, and establishes the basis for state ecological appraisal of projects, on which another piece of legislation was adopted in 1996.

A law on environmental permits was adopted in 1996, covering the issue of environmental impact assessments. Georgia adopted legislation on ambient air protection in 1999 (amended in 2007) which incorporates several EU requirements. The law on water has been in force since 1997 and was last amended in 2000. In the field of nature protection, a number of acts have been adopted, such as the law on soil protection (1994), the law on the protected area system (1996), the law on wildlife (1996), the forest code (1999), and the law on endangered species (2003). Other legislation includes the law on mineral resources (1996), the law on nuclear and radiation safety (1998), the law on hazardous chemical substances (1998), the law on the sea (1998), the law on fees for natural resources (2004), and the law on licences and permits (2005).

In the period 2007–2008, new legislation was prepared on water, waste and nature protection and on rules for the conduct of state ecological examinations and the granting of environment

impact permits. A policy document on forestry is under preparation. Some steps have been taken to address obsolete pesticides. Georgia has taken steps to enhance its environmental monitoring system and environmental inspectorates. Water governance reform is on hold.

Georgia has taken steps to prepare a state-of-the-environment report for 2006. Access to information and public participation require particular attention, although the Aarhus Centre continues to be operational. Lately, there have been no developments concerning environmental impact assessment (EIA), as public projects continue to be exempted from such assessments. Some steps have been undertaken to promote strategic environmental assessment.

Overall, environment legislation is therefore in place in several areas, but still needs further development, in particular with regard to implementing legislation. Georgia faces difficulties with the implementation and enforcement of environment legislation due to limited administrative capacities and financial resources, especially at regional and local levels.

4) Administrative capacity

The Ministry of the Environment and Natural Resources was established in 1991. As a result of an institutional reform in 2004 the Ministry was reorganised and is now called the Ministry of Environmental Protection and Natural Resources. It is the national body responsible for establishing, promoting and implementing policies and strategies for environmental protection, including nature protection and forest management.

In 2005, following recommendations by domestic and international experts, the Environmental Inspectorate was created under the Ministry to improve the enforcement of environmental laws and regulations. In 2008, the former Environmental and Prognostic Centre became the National Environmental Agency. An Agency of Protected Areas was created from a former department under the Ministry of the Environment and Natural Resources.

However, the further strengthening of administrative capacity at all levels of the country is still a major challenge in order to enhance strategic planning and the implementation and enforcement of environment legislation. Coordination between authorities requires further attention.

5) Participation in regional and international processes

Georgia has ratified the relevant **international and regional conventions** to which it is signatory, with the exception of the Strategic Environmental Assessment Protocol of the UNECE Convention on Environmental Impact Assessment in a Transboundary Context. Georgia has not signed the UNECE Convention on the Protection and Use of Transboundary Watercourses and International Lakes. Georgia is not a party to the UNECE Convention on the Transboundary Effects of Industrial Accidents or to the UNECE Convention on Environmental Impact Assessment in a Transboundary Context. The implementation of several already ratified agreements requires particular attention.

Georgia is a member of the Commission **on the Protection of the Black Sea against Pollution** (the Black Sea Commission), which is the body implementing the Convention on the Protection of the Black Sea against Pollution and the Black Sea Strategic Action Plan. The Commission aims to combat pollution from land-based sources, maritime transport, rivers,

etc. so as to ensure the sustainable management of marine living resources and sustainable human development.

Georgia participates in environmental and climate cooperation under the **Black Sea Synergy** and the **Eastern Partnership**. As these initiatives were launched fairly recently, it is expected that regional and multilateral cooperation will significantly increase.

Georgia is a member of the **Danube-Black (DABLAS) Sea Task Force**, which provides a platform for cooperation between IFIs, donors and beneficiaries on water protection and water-related issues in the Danube and the Black Sea. The main aim is to encourage a strategic focus on the use of financing, and to ensure coordinated action between all financial instruments operating in this region.

Georgia is participating in the **Eastern Europe, Caucasus and Central Asia component of the EU Water Initiative, a regional component of the EU Water Initiative** as announced at the 2002 World Summit on Sustainable Development. The initiative aims to promote better water governance and coordination between stakeholders. A national policy dialogue with Georgia has been launched under the initiative.

Georgia also participates in the **Europe and the North Asia Forest Law Enforcement Governance (FLEG) process** concerning forest governance and the protection and sustainable management of forests in the region.

Georgia is a co-founder (together with Armenia, Azerbaijan and the European Commission), as well as host country, of the **Caucasus Regional Environmental Centre (REC)**, which has been operational under a revised Charter as of 2007. The REC Caucasus, with headquarters in Tbilisi, addresses environment issues in the Southern Caucasus by promoting regional cooperation between various stakeholders at all levels, involving civil society, governmental bodies, local communities and the business sector. The REC Caucasus also aims to foster public participation in environmental decision-making.

6) Key areas where action is required

Georgia faces significant challenges in promoting environment protection. Key areas include air quality, water quality, waste management, land use, coastal and marine pollution, chemicals and nature protection.

As regards climate change, Georgia needs to implement the relevant provisions of the Kyoto Protocol to the UN Framework Convention on Climate Change, and to prepare for the implementation of a new agreement to succeed the Protocol. Particular attention needs to be devoted to mitigation and adaptation issues, and to ensuring the inclusion of relevant actions in all national plans and budgetary processes. Georgia has significant possibilities to use flexible mechanisms under this Protocol.

Institutional and administrative capacity needs strengthening, in particular as regards strategic planning, implementation and enforcement. Further national support for the Regional Environmental Centre (REC) could assist Georgia in promoting environmental awareness and protection by providing a forum for cooperation between various stakeholders.

Key environment areas where action is required are identified in the environment section of the EU–Georgia Action Plan. It defines a set of priorities for action with regard to environmental governance, issue-specific activities, and international and regional

cooperation on environment issues. Progress towards implementing the Action Plan will also contribute to achieving the objectives of the Partnership and Cooperation Agreement.

2.7.7. Annex 7: Georgia: Public Finance Management (PFM) Report

Evolution of the PFM system

Global evolution of the PFM performance and reform process

Until 2002, Georgia was one of the poorest performing economies with one of the weakest governance frameworks in the Europe and Central Asia region. This was typified by the pervasive corruption, with its negative repercussions for government revenues. On taking office in January 2004, the new government responded decisively to its mandate to improve overall performance and governance. In the area of economic liberalisation, the results achieved have been encouraging: in the last 4 years Georgia has enjoyed rapid GDP growth. However, this was interrupted by the global financial crisis and the 2008 August war with Russia. In 2009, GDP is forecast to fall by 4.5-6 percent.

A new tax code, introduced in 2005, reduced the number of taxes collected and their percentage rates, simplified the process for registering a business, and eliminated close to 90% of previous licensing requirements. These changes have enabled the government to curb economic corruption and increase the state budget several times over. As a result of the improvement in the state's revenue-collecting capacity and the sustained economic growth, the state budget has indeed tripled, increasing to 1.5 billion dollars in the period 2003-2006 and reaching 4.2 billion dollars in 2008.

In the area of public finance management, the government has outlined a strategic vision for public finance management reform with ambitious goals. This strategic vision is an expression of the government's ownership of the reform agenda, and acts as an anchor for the overall reform process in public finance. The focus of the reforms has been on the following main areas: budget system, treasury system, financial policy, tax and customs department and financial police, and external audit. The main achievements since 2004 have been the adoption and enactment of the new law on budget systems and the introduction of the Single Treasury Account. In 2005 a start was made on improving the link between 'strategic planning' and 'budget preparation' over a medium-term perspective with the introduction of the Medium Term Expenditure Framework (MTEF).

In 2006 a new law on state procurement became effective. The new law extends its coverage to state-owned enterprises and streamlines procurement procedures, which have been amended several times. For the last few years the government has produced annual consolidated financial statements in accordance with internationally accepted accounting and reporting standards. It has also introduced a GFS 2001-compliant budget classification.

While acknowledging what has been achieved in an often difficult environment and with limited resources and experience, it is also accepted that significant further reforms are required to ensure an efficient, effective and transparent public finance system (PFS), one that all stakeholders can have confidence in.

This is recognised by the government, which is addressing the shortcomings on a number of fronts. In March 2007 the Ministry of Finance produced a document '*Strategy 2007-2011 and priorities for cooperation with development partners*'. This document summarises the reforms already undertaken, the plans for further reforms, and the roles that donors will play in the reform process. It also identifies areas where external assistance is still required. It thus presents an overall framework for reform of the PFM system.

In 2008, the Ministry of Finance revised the Public Finance Management Reform Strategy and issued a new Policy Vision paper, which complements the 2007 PFM strategy reform. The Vision includes an action plan, to be implemented from 2009 to 2013, and a more detailed list of activities for 2009.

While there may be some discussion as to the appropriateness of the Vision's level of detail, the government considers it a realistic reflection of what can be done with existing capacities.

The Policy Vision addresses most of the findings of the PEFA assessment, which was finalised in October 2008. There are, however, elements in the PFM reform agenda that are missing from the Vision: public procurement and external oversight. These are elements over which Ministry of Finance considers it has limited or no control and, therefore, thinks inappropriate to include in a document that is essentially the Ministry of Finance's strategy and plan of action.

However, the Chamber of Control has developed its own strategy to implement the new law approved in January 2009. This was presented to donors in April, to seek technical assistance. The strategy addresses several of the main elements that can contribute to making this institution a genuinely independent supreme audit body: establishment of a sustainable training system for auditors; development of a methodology for all kinds of audits according to INTOSAI standards; improvement in relations/communication with the Parliament, Ministry of Finance and the broader public.

Following the WB Country Procurement Assessment (CPA), finalised in October 2008, the State Procurement Agency has made a major effort to revise the legislative framework for public procurement. The amendments are based on the WB CPA recommendations.

In addition, the Ministry of Finance has developed a policy paper and action plan for Public Internal Financial Control (PIFC) (approved in March 2009). As a first result, a draft law has been prepared for the introduction of a standardised internal audit system throughout the Georgian government.

The EC, jointly with the WB, SIDA, DFID and Dutch Government, has supported the Ministry of Finance in implementing the strategy and pushing forward the PFM reforms since 2007. Under the ENPI, the AAP 2007 included 'support for the public finance management reform in Georgia' (2007-2009). A new programme is under discussion with the Ministry of Finance for 2010-11. The programme is intended to address the following challenges:

- To further improve the budget preparation process, primarily focusing on strategic planning and budgeting;
- To strengthen the internal and external audit functions so as to enhance the accountability and transparency of the budget process;

To improve the effectiveness, transparency and efficiency of public procurement and revenue collection.

Structured analysis of the PFM system vis-à-vis the 2008 PEFA

Topics	Situation at the time of the PEFA 2008 Report	Evolution since and key concerns to address during the next period
Legal and institutional framework	<p>The legal framework specifying the function, roles and responsibilities of the government of Georgia in PFM is provided by the Constitution, the Organic Budget Law, the Law on the Chamber of Control, and the Organic Law on Self-Government Units.</p> <p>The Ministry of Finance is responsible for the preparation of the draft state budget and the execution and reporting of the approved budget. The state budget covers recurrent and capital expenditure, and transfers to local governments.</p>	<p>Although efforts are being made to improve the capacity for macro-economic forecasting, it still needs to be strengthened.</p> <p>Although a link was made between strategic planning and budget preparation in 2005 by introducing an MTEF, it still needs to be improved by enhancing understanding and capacity in the Ministry of Finance and in all</p>

	<p>The Ministry of Finance starts the budget process on 1 March of each year with the preparation of the Medium-Term Macroeconomic Forecast, Medium-Term Fiscal Forecast, and the Basic Data and Directions (BDD) for the budget, in collaboration with the Ministry of Economic Development and other ministries, and in collaboration with the National Bank of Georgia.</p> <p>In 2007, local self-government units started implementing new rules for budget planning and execution. However, capacity to implement the rules varies considerably across the self-government units.</p>	<p>spending units.</p> <p>A new budget law is under preparation to include performance budgeting for some of the spending units on a pilot basis.</p> <p>The Ministry of Finance has also drafted a draft law for the introduction of a standardised internal audit system throughout the Georgian government.</p> <p>A new Law on the Chamber of Control (CoC) was enacted in January 2009, which provides for transforming the CoC into an independent supreme audit institution.</p> <p>The implementation of the CoC and Internal Audit laws is a challenge for the next period, which is addressed in the new programme.</p> <p>Enhanced capacity to plan and execute budgets in the self-government units needs to be addressed.</p>
<p>Comprehensiveness, transparency of the budget and oversight of aggregate fiscal risk.</p>	<p>The comprehensiveness and transparency of the budget is guaranteed. The administrative, economic and functional classification of the budget has gradually (since 2007) been adopting the 2001 GFS methodology.</p> <p>The level of unreported extra-budgetary expenditure is insignificant.</p> <p>Fiscal relations between central government and local self-government units are transparent, rule-based and fully integrated within the annual budget, and approved by the Parliament.</p> <p>The Ministry of Finance is responsible for oversight of the aggregate fiscal risk for the government. Audited annual financial statements are provided by the major state-owned enterprises to the State Enterprise Management Agency.</p> <p>The aggregate annual fiscal risk posed by state-owned enterprises is not reported in a consolidated fiscal report.</p> <p>Public access to fiscal information is satisfactory.</p>	<p>Extra-budgetary funds that were still active have all been closed.</p> <p>The privatisation process has left a very small number of state-owned enterprises still under state control, reducing the concern as to the aggregate risk that this can generate.</p> <p>Public access to fiscal information has been challenged by some NGOs monitoring the budget process.</p> <p>No major issues.</p>
<p>Budget formulation and preparation</p>	<p>A clear budget calendar exists and allows sufficient time for it to be respected.</p>	<p>Strategy formulation in Georgia remains weak and incomplete. The MTEF process has been regrettably</p>

	<p>Parliament approves the annual budget before the start of the fiscal year.</p> <p>There are sector strategy statements for 54 per cent of primary expenditure, but these are not fully costed and the links between investment decisions, sector strategies and recurrent costs remain weak</p>	<p>watered down and there is no clear link between strategy and planned expenditure.</p> <p>There is room for improving capacity for budget preparation, especially forecasting and strategic planning and budgeting, both in the Ministry of Finance and in all spending units.</p> <p>The EDPRP (Economic Development and Poverty Reduction Programme) was abandoned as a reference document in 2008. The BDD is meant to be the overarching document of reference for the government, with the aim of translating the government's programme 'Georgia without Poverty' into figures.</p> <p>In 2010, the Georgian government plans to introduce performance-based budgeting on a pilot basis.</p>
<p>Revenue management</p>	<p>Georgia has implemented a major tax policy reform, and further moves are under way.</p> <p>Tax legislation and procedures are relatively clear, taxpayer registration procedures are simple and quick, and penalties are adequate and act as a deterrent. Audit selection is based on a continuous programme, but risk assessment criteria are still in the process of being implemented.</p> <p>Customs legislation has also been extremely simplified.</p> <p>The initial phase in the introduction of a customs control system based on risk analysis and simplified procedures has been completed.</p>	<p>Modernisation of tax administration to have a system that provides a reliable and credible appeal and arbitration mechanism for taxpayers.</p> <p>Old tax arrears, which are not recoverable.</p> <p>In 2007, the Tax Department introduced a risk profiling system for profit tax audits. Software was designed to identify risk factors to produce a list of taxpayers ranked in risk order. Such a list was produced in mid-2007 and submitted for approval as a basis for an audit plan. The list was rejected by senior management, however. Audit managers found the list to be unsatisfactory as known high-risk taxpayers were ranked very low, casting doubt as to the list's credibility. There were also question marks over the calculations performed by the software, and the use of only one year's data to produce the list.</p> <p>During 2008, the risk criteria were revised and in 2009 the system should become fully operational.</p>

		With respect to customs, the Revenue Service reports that the initial phase in the introduction of a customs control system based on risk analysis and simplified procedures for Authorised Economic Operators (AEOs), as in the EU, was completed at the end of 2007. To facilitate this, an automated system was introduced for management and analysis of the Customs Database (ASYCUDA World) with technical assistance from UNCTAD. The system is partially operational.
Budget execution	The use of PEFA performance indicators to assess the credibility of the federal budget indicates that the overall execution of expenditure and actual amounts spent differs from the budgeted amounts. These deviation is explained by over-performance in revenue collection. However, all supplementary budgets are reviewed, discussed and approved by Parliament	Limited forecasting capacity is still an issue.
<i>Public procurement</i>	While the legislative framework is partially aligned with international practices, weaknesses remain in several areas. Current procurement practices show weaknesses in over-reliance on single sourcing and the complaint mechanism is poorly designed and implemented.	Despite these efforts, procurement practices have weaknesses as exhibited by heavy reliance on single sourcing. The procurement system is decentralised but lacks a systematic approach to procurement monitoring and reporting. While in principle procurement is part of budget planning and execution, the lack of integrated monitoring and reporting systems means that the system is fragmented. Georgia faces important challenges if it is to bring current procurement practices into line with international practices.
<i>Cash management and treasury function</i>	Regarding cash management, Georgia relies on the Treasury Single Account, which provides real-time information on cash balances. The Treasury publishes daily cash balances and a consolidated monthly report (ex ante and ex post) on the execution of the cash plan. All cash balances are calculated daily and consolidated monthly.	The cash flow management system (and forecasting) needs to be fully established and further developed in order to comply with best practices in the area. This system should be based on cash availability. This also includes training activities (for the cash flow management and commitment systems).
<i>Personnel expenditures</i>	The process is decentralised and personnel and payroll functions are carried out by the accounting and human resources departments of the spending units. This has allowed adjustments to staff composition and salary levels within the approved annual ceilings, which result in the lack of effective control. During the PEFA it	Unchanged, it remains an issue.

	was not possible to fully assess the issues due to the lack of overall information.	
<i>Debt management</i>	Debt management is currently centralised by the Ministry of Finance and strictly regulated. Specifically, chapter 4 of the Budget System Law, ‘Government Borrowing and Debt’, and the Law on Public Debt No 1429/1998, as amended in 2004, 2005 and 2006, provide the rules governing public debt management. Local Self-Governments (LSGs) may only borrow from central government or with the permission of the Ministry of Finance. Information on debt is readily available in English on the websites of the Ministry of Finance, the National Bank of Georgia, and the Department of Statistics. The central government’s contracting of loans and issuance of guarantees are against transparent criteria and fiscal targets, and are always approved by the Ministry of Finance and promulgated by Parliament. Georgia’s debt profile has improved markedly over the past few years.	Performance remains strong
<i>Accounting and reporting</i>	The operationalisation of the Treasury Single Account in 2005 was a key first step in strengthening Georgia’s financial management system. The technical accounts used by the Treasury are reconciled daily In-year reports on budget execution are produced on a regular and timely basis. However, they do not include a breakdown of the expenditure and revenue of LEPLs whose liabilities are not the government’s responsibility. There are no material concerns regarding data accuracy	Unchanged.
<i>Internal audit</i>	Internal audit systems and procedures in accordance with international standards are not in place (nor supported by any legal framework) for checking that the internal control systems are countering the perceived risk and are evaluating and improving the effectiveness of risk management, control, and governance processes.	The Ministry of Finance has developed a Public Internal Financial Control (PIFC) policy paper and action plan (approved in March 2009). A draft law has been prepared for the introduction of a standardised internal audit system throughout the Georgian government. Implementation of the law.
External audit		
<i>Supreme Audit Institution</i>	The external audit system does not follow recognised international standards and is characterised by capacity limitations due to weaknesses in its structure, staff skills, and the technical quality of reports.	Although a new law has been adopted, external audit does not yet operate according to recognised standards. A strategy to strengthen auditing practice over the period 2009-11 has been drafted and is to be

		implemented
<i>Parliament</i>	The annual budget law review process is clear and has been adhered to; examination covers both the medium-term framework and annual details; an adequate timeframe is available for legislative review. Clear rules exist for in-year amendments, but there are no limits on their extent or nature.	Legislative scrutiny of the budget is weak. Parliament's <i>Budget and Finance Standing Committee</i> therefore needs to be strengthened.

PFM Policy dialogue and institutional support

Policy dialogue during the period under review

Despite the efforts made during most of 2008, the EU delegation, and the other donors (Dutch government, SIDA and World Bank) supporting the PFM reforms in Georgia, could not establish a constructive policy dialogue with the Ministry of Finance to monitor and discuss the status of advancement of the reforms.

The difficulty of establishing a policy dialogue with the Ministry of Finance and the donor communities can be explained by two factors: a new Prime Minister and Minister of Finance, who had new priorities and did not focus attention on PFM reforms; the political instability per se, internal and external, which characterised most of 2008, ending in the August war and followed by the financial crisis.

Policy dialogue is critically needed for driving the reform programme of the PFM system. However, no institutionalised mechanism is yet in place under the leadership of the Georgian government. Donors are systematically meeting with the government, using the respective Steering Committees for implementation of the assistance they provide to move forward the PFM reforms.

Discussions and consultations are ongoing with the Georgian government and other donors (WB, Dutch Embassy, SIDA and GTZ) on the possibility of creating a joint mechanism to improve policy dialogue between the Georgian government and at least the donors closely supporting these reforms.

The Ministry of Finance seems rather keen to start on a different footing, since the 2008 August war, and has demonstrated renewed interest and commitment to the PFM reforms and to the establishment of policy dialogue with donors and civil society.

Institutional support

The absence of adequate capacity remains a significant problem in Georgia, both in the Ministry of Finance and in line ministries. The public finance reform agenda is very substantial and its successful implementation will require adequate numbers of well-trained and motivated staff. This is especially true in relation to the development of external and internal audit, where current numbers of qualified auditors are low.

Problems of capacity are not helped by an inappropriate recruitment and retention policy throughout the public service. Changes at ministerial level are often accompanied by major staff changes at senior and middle level. This often results in the loss of capacity and institutional memory. System development will not be sufficient for successful PFM reform, if not accompanied by strengthening of capacity at all levels.

Conclusion:

The outcome of the 2008 PEFA exercise demonstrates that, in general, the PFM system in Georgia is functioning fairly well. PFM reform programmes were strongly owned by the government, which ensured the necessary commitment across the government to bringing the existing PFM system into line with international principles.

However, the government's commitment to PFM reform had been compromised during 2008 by more urgent political issues. During 2009, with the changes brought about by the August war, and the financial crisis that followed, the Ministry of Finance has engaged in a more constructive dialogue allowing for a better understanding of and progress with PFM reform.

Adequate capacity remains a significant problem in Georgia, both in the Ministry of Finance and in line ministries, which needs to be addressed possibly by entering into a dialogue to support a comprehensive civil service reform.

In addition, internal control and external control are two areas of Georgian public finance management which deserve attention, to bring practices into line with internationally recognised standards and best practices.

The EU delegation is designing a new programme with the Ministry of Finance for 2010-11 to continue supporting PFM reform in areas considered of paramount importance for ensuring a transparent and credible PFM system.

2.7.8. ANNEX I

Georgia: Macro-Economic Assessment (August 2009)

In July 2009, the IMF undertook the third review under the Stand-By Arrangement and requests for augmentation, extension of the arrangement, rephrasing of purchases, and modification of performance criteria.

Georgia will suffer a deeper contraction than previously expected, with real GDP falling by 4 per cent in 2009. The contraction in output seems to be led by falling exports and remittances and a fall in bank lending of 10 per cent since the end of 2008. Deposits, remittances, and trade indicators stabilised in May-June 2009, so with the economy possibly bottomed out recovery is expected to begin in the second half of 2009, led in part by public spending.

CPI inflation stabilised at 2.3 per cent in June, reflecting weakened economic activity and a fall in world commodity prices. Significant lay-offs were reported in the construction, financial, and retail sectors and the unemployment rate reached 16.5 percent in late 2008. Poverty remains widespread (23.7 percent in 2007) and is likely to have increased due to the conflict and the economic downturn.

The Georgian government's response to the downturn has mostly relied on a fiscal stimulus and on the inflow of resources from donors. The reduced interest rates and ample liquidity injections have not yet led to a resumption in bank lending. The government has decided to accommodate tax revenue losses with a higher deficit in 2009. It intends to make a fiscal adjustment at the beginning of 2010 to preserve investor confidence and restore access to international capital markets ahead of the large repayment obligations due in 2013.

The financial sector has been resilient so far, but remains vulnerable to deterioration in asset quality and continued uncertainty about the deposit base. The Georgian government is strengthening supervision and developing a contingency plan for managing potential financial sector stress.

The mission concluded that macroeconomic stability is now challenged not so much by foreign exchange market pressures but by the worsening state of the economy. The deterioration in economic activity depends on trading partners, but domestic political uncertainties have also dampened confidence, while the deteriorating quality of the loan portfolios held by the banks has set in motion adverse financial macroeconomic interactions. There are signs that the output contraction could be bottoming out, but the recovery in 2010 is expected to be slow. With imports contracting, pressures in the foreign exchange market have disappeared, but could re-emerge depending on current account trends, private capital inflows, donor financing, and confidence in the currency.

However, the policy response of the government so far has been good, containing the fiscal deficit despite significant tax revenue shortfalls, maintaining a prudent monetary policy, and successfully completing the introduction of foreign exchange auctions. Macroeconomic stability should be maintained in 2009 and 2010 thanks to a moderate recovery in activity (real GDP growth is projected to be 2 per cent in 2010). After the expansion of government spending in the second half of 2009, the government is expected to withdraw the fiscal stimulus in 2010 as FDI gradually returns to Georgia and banks return to lending. Inflationary pressure is of course expected to increase as growth resumes.

2.7.9. ANNEX II

Georgia: Highlights of the PSFMSP and PFM Programmes

The Public Sector Financial Management Reform Support Project (PSFMRSP)

The Public Sector Financial Management Reform Support Project (PSFMRSP) supports the government's strategy for public finance management and is supported by four development partners (DPs): the UK Department for International Development (DFID), the Netherlands Ministry for Development Cooperation, the Swedish International Development Cooperation Agency (SIDA) and the International Development Association (IDA), referred to below as the World Bank. The development objective of the PSFMRSP is:

To enhance governance, particularly in the public financial management domain, through:

- i) Strengthening the institutional capacity of key agencies to use public resources more effectively and efficiently; and*
- ii) Improving accountability in the use of public resources.*

This development objective is broad in order to be able accommodate the plans being further developed by the government. In addition, it provides for flexible funding arrangements to be set up for the PSFMRSP that will enable the Government to attract additional resources from various development partners.

This project will focus on strengthening the agencies directly responsible for achieving the four outcomes described above: the Ministry of Finance for MTEF, Treasury and HRMIS, and the Chamber of Control of Georgia (CCG) for external oversight of public financial management.

EU-Georgia ENP AAP2007: SPSP — Support for PFM Reform

The EU-Georgia Action Plan under the European Neighbourhood Policy (ENP AP) came into force on 14 November 2006. Within this context, the first Annual Action Plan for 2007 (ENP AAP 2007) incorporates the Sector Policy Support Programme (SPSP), Support for Public Finance Management (PFM) Reform in Georgia, as a major component. The Financing Agreement (FA) for this PFM Reform Programme was signed by the European Commission (EC) on 30 November 2007 and by the Government of Georgia on 17th December 2007.

Under the FA, a total grant of up to €16 is to be provided to support PFM reform over the three years from 2007 to 2009. Of this, up to €15 m is for direct budgetary support for the Georgian state budget and €1 m for technical assistance (TA) to support the reform process and effective execution of the Programme. The budget support is to be provided in three annual payments of up to €5 m. The initial instalment is a fixed amount of €5 m to be paid on signature of the FA, assuming compliance with specific reform preconditions and continuing fulfilment of the general policy conditions detailed in the FA. The second and third instalments, each €5 m, are to be paid after reviews of compliance with the conditions for instalment release in July 2008 and 2009, respectively. In each case, the instalment includes a fixed component (equivalent to 60% of the total possible instalment, or €3 m) and a variable component (of up to €2 m).

The disbursement decision is based on two general conditions — macro-economic stability and positive progress with the PFM reforms — as well as specific (pre)conditions. The latter are linked to: constructive monitoring of the overall reforms; development of effective external and internal audit systems; improvement of the public procurement system; and strengthening the Revenue Service.

The value of the variable component released will depend on the degree to the specific conditions have been fulfilled. Throughout, continuing compliance with the general policy conditions will be a precondition for release.