International Monetary Fund

Republic of Kosovo
and the IMF

Press Release:
IMF Executive Board Completes First Review Under Stand-By Arrangement for the Republic of Kosovo; Approves €47.96 Million Disbursement
July 17, 2012

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Republic of Kosovo: Letter of Intent, and Technical Memorandum of Understanding

June 17, 2012

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REPUBLIC OF KOSOVO

Letter of Intent

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, D.C., 20431
U.S.A.

Pristina, June 27, 2012

Dear Ms. Lagarde:

1. Kosovo's economy has continued to perform well in a difficult international environment. Robust current and capital inflows and solid lending by a well-capitalized and liquid banking system have supported growth, while contagion from the financial crisis in the euro area has remained subdued, owing to a small export base and limited financial linkages. However, downside risks remain, as foreign direct investment and remittances from the Kosovar diaspora could be affected in case of a deterioration of labor market conditions in host countries. Steadfast commitment to disciplined fiscal management, the restoration of a sufficient level of government bank balances, the further strengthening of the legal and regulatory framework of Kosovo's financial system, vigilant financial supervision, and progress with structural reforms to boost competitiveness provide the best safeguard to steer Kosovo's economy through the period ahead, and to establish the fundaments for robust and balanced growth.

2. Implementation of our economic program has been broadly consistent with commitments under the Stand-By Arrangement (Tables 1 and 2):

- all *quantitative performance criteria* for end-April were met. The primary fiscal balance and government bank balances were stronger than programmed, despite a modest shortfall in revenue, as spending was under-executed and dividend payments from the state-owned telecommunications company (PTK) were advanced.
- most *structural benchmarks* were also met.

  (i) on May 10, we published the first 2013 budget circulars for municipalities. The circulars contain no limits on spending allocations from own-source revenues across nonwage categories, in line with the corresponding end-May structural benchmark;

  (ii) on June 14, the Assembly amended the Law on Public Financial Management and Accountability (LPFMA) with a provision specifying that only the central bank can authorize the withdrawal of funds from the special reserves fund (SRF) for emergency liquidity assistance (ELA), consistent with the corresponding structural benchmark;

(iii) also respected were the continuous structural benchmarks on monthly meetings of the Program Monitoring Committee, and on fiscal impact assessments evaluating the budgetary impact of all new benefit creating laws and amendments to such laws over a period of at least 5 years;

(iv) on June 22, we submitted a revised Deposit Insurance Fund Law to the Assembly in a form consistent with the new Banking and Microfinance Law. While the submission occurred somewhat later than originally specified under the structural benchmark (end-May), the delay was needed to complete discussions with stakeholders;

(v) on one occasion the continuous structural benchmark on including an article into all new benefit creating laws and amendment to such laws that allows for benefit cuts in case of insufficient budgetary funds was violated, as the law on pensions for the Kosovo Security Force was passed on May 3 without such a clause. The LPFMA contains a similar adjustment clause, however, for all budgetary allocations granted in the annual budget law. The amendment of the LPFMA passed on June 14 contains a provision emphasizing that the LPFMA's legal precedence over individual benefit creating laws extends to this adjustment clause (see also ¶14).

3. Based on this performance, we request completion of the first review under the Stand-By Arrangement. We also request a purchase of SDR 39.108 million following completion of the first review. We intend to deposit the purchase in the SRF designated for ELA.

4. We request two modifications of performance criteria:

- *increase the floors for the primary fiscal balance and the bank balance of the general government for end-August 2012* by €15 million, reflecting the early receipt of dividends from PTK in April that had originally been expected for October;
- *lower the ceiling on primary expenditures by the projected spending of the Kosovar Privatization Agency*, *and exclude PAK-related spending from the program definitions of primary expenditures and the primary balance.* Before 2012, PAK-related spending—both PAK's operational budget, and fees PAK pays to corporations charged with the liquidation of socially owned enterprises (SOEs)—were funded by donor grants. From this year, and in the context of Kosovo's transition from supervised to full independence, PAK pays for its expenditures from its own funds, consisting mostly of receipts from SOE privatization that will eventually be distributed among claimants, the residual claimant being the government. In the original 2012 budget, we recorded PAK's spending as primary expenditure and the use of PAK's funds as nontax revenue. We have now modified the recording and will register the use of PAK's funds as financing, in line with the definition in the Technical Memorandum of Understanding. The changes in program definitions avoid an unintended deterioration in the government's reported primary balance that would result otherwise from this recording change.

Quantitative performance criteria through end-2012 and indicative targets through end-June 2013 are set out in Table 2 and in the Technical Memorandum of Understanding, both attached to this letter.

5. We believe that the policies set forth in the letter of April 12, 2012 and in this letter are adequate for successful implementation of the program. However, the government stands ready to take additional measures as appropriate to ensure achievement of the program's objectives. As is standard under all IMF arrangements, we will consult with the IMF before modifying measures contained in this letter or before the adoption of new measures that would deviate from the goals of the program, in accordance with the Fund's policies on such consultations, and provide IMF staff with the necessary information for program monitoring. The second review is expected to be completed after December 20, 2012, the third review after February 28, 2013, and the program is expected to be monitored by quarterly reviews thereafter. The understandings between us and the IMF regarding performance criteria and structural measures described in this letter are further specified in the attached Technical Memorandum of Understanding. We authorize the IMF to publish this letter and the associated staff report.

I. Macroeconomic Outlook

6. The outlook remains broadly unchanged from the April Letter of Intent. The macroeconomic framework underpinning our program is based on purposely cautious assumptions, with a view to minimizing the risk of downward revisions during the program period.

a. We maintain a forecast for *real GDP growth* of 3.8 percent in 2012, driven primarily by robust private consumption and investment. The resilience of private sector demand is expected to continue in 2013.

b. Consumer price *inflation* is expected to remain subdued at around 1 percent, owing primarily to disinflation for import prices, notwithstanding prospective tariff increases in the context of a revamped electricity regulation.

c. The *external trade deficit* for goods and services is expected to narrow to 38 percent of GDP, from more than 40 percent in 2011. The deficit will continue to be financed by non debt-creating flows such as FDI, remittances, and other current transfers.

II. Fiscal Policy

A. Implementation of the 2012 budget

7. Fiscal policy remains anchored by the objectives of restoring a sustainable fiscal stance and maintaining an acceptable level of government bank balances. To this end, the 2012 budget contains structural adjustment measures of ¾ percent of GDP. In addition to these measures, we are in the process of introducing environmental taxes and fees that are expected to raise at least €10 million in 2012 (0.2 percent of GDP), with a full-year impact of 0.4 percent of GDP.

Further, we have also left €20 million in expenditures from the 2012 budget unallocated, and we have specified these across spending categories (€10.1 million in goods and services, €7.5 million in non-highway capital spending, and €2.4 million in subsidies).

8. In the first four months of 2012, budget implementation has been broadly in line with our program. Revenues excluding dividends were €36 million (0.7 percent of annual GDP) lower than expected, owing mostly to temporary factors such as unusually severe winter weather that depressed trade and border tax receipts. The shortfall in revenue collection was overcompensated by advancing dividend payments from PTK (€15 million, out of a total €45 million in PTK dividends for the year) and by exercising spending restraint—primary expenditure was €45 million below the program ceiling, owing in part to under-execution of capital spending by €27 million.

9. In the months ahead, we expect both revenue collection and expenditure execution to catch up with original program projections—we have already registered an improvement in revenue collection in May. As a result, we see no need to revise our projections for tax revenue or expenditures for end-August and end-December, and request to increase the program floor on the primary balance at end-August by €15 million, reflecting the PTK dividend received in April (instead of October as originally projected). Moreover, in the mid-year budget review we will keep the overall spending envelope for 2012 constant, notwithstanding a modest shift from capital spending to spending on goods and services that became necessary due to in part to higher maintenance needs caused by the severe weather in January and February. We stand ready, however, to take additional revenue or expenditure measures in case revenue collection fails to catch up with program projections going forward. We will decide on the need for such measures the latest on the basis of end-August data.

10. We have conducted five consecutive successful 3-month treasury-bill auctions this year, raising €30 million (net) at an average annual yield of between 3-4 percent. To lay the foundations for self-sustained budget financing we intend, as the next step, to issue bills with a maturity of 6 months in the second half of this year, and of 12 months in 2013, although variations to this schedule are possible depending on the absorptive capacity of the market.

A. Medium-Term Fiscal Issues and Structural Fiscal Reforms

11. For our 2013 budget, we will target a primary deficit of no more than €155 million (excluding possible budget support grants; structural benchmark for end-October). Structural fiscal adjustment of at least €31 million (0.6 percent of GDP) will be needed to achieve this objective. Part of the adjustment will come from an increase in lignite royalties that the Assembly approved in early June. The remaining adjustment measures will be specified in full during the budget preparation process; options include restraint on current spending, notably wages and salaries, and growth friendly revenue measures, consistent with the recommendations of the IMF technical assistance mission on tax policy from November 2011. A technical

assistance mission analyzing Kosovo's mining tax regime, scheduled for September of this year, may also identify options for adjustment.

12. Restoring an adequate level of bank balances in 2013 as envisaged will in part depend on the successful privatization of the telecommunications operator PTK. The privatization process has made significant progress in recent months. A new transaction advisor was hired in April, and road shows in London and Istanbul in May generated substantial investor interest. We began with the prequalification of bidders in June, and by July will present separate balance sheets for PTK and the postal service that has been split from PTK earlier this year. Thereafter we will launch the tender offer (new structural benchmark for end-August). The winner of the bidding process is expected to be announced toward the end of this year.

13. We are preparing the introduction of a legally binding, rules based fiscal framework. An IMF technical assistance mission is visiting Kosovo in late June. We will discuss the TA mission's recommendations changes with the IMF mission for the 2nd review under the SBA, scheduled for early October. We intend to enact the necessary legislation in early 2013, i.e., during the early stages of the 2014 budget preparations. The technical assistance mission in June will also develop proposals to improve the recording and monitoring of payment obligations, with a view to preventing the accumulation of domestic payments arrears.

14. We intend to maintain a flexible structure of our budget to preserve options for adjustment, should the need arise. To this end, the Assembly passed on June 14 an amendment to the Law on Public Financial Management and Accountability (LPFMA) that emphasizes that the LPFMA's legal precedence over individual benefit creating laws extends to an adjustment clause allowing the government to reduce budgetary allocations in case of (i) a macroeconomic shock reducing fiscal revenue or financing, (ii) natural disasters, or (iii) the suspension or cancellation of a program or project to which the allocation relates. This provision renders redundant the continuous structural benchmark of including a corresponding adjustment clause into any new benefit creating or amending law. We therefore request to drop that benchmark. Further, with a view to upholding principles of sound fiscal management and costing, we will maintain the requirements that (i) new laws, amendments to laws or regulations that create benefits will grant only cash benefits, with no link to the minimum wage; and (ii) any such law, amendment to a law or regulation will be preceded by a thorough fiscal impact assessment covering a period of at least 5 years (continuous structural benchmark).

15. Careful planning of spending initiatives remains at the core of efforts to improve public financial management.

a. *Highway R7 to Albania.* The ongoing construction of highway R7 to Albania requires close cost control as the project nears completion in 2013, especially with regard to variation cost.

b. *Highway R6 to Macedonia.* The analysis of design and financing options for R6 is ongoing. We will move beyond the preparation stage only once (i) R6 can be integrated into a sustainable budgetary framework, and (ii) World Bank staff confirms that the highway's design is economically viable. Bidding for the highway project will be competitive and transparent, and we will consult with IMF staff prior to entering into any contractual obligations. In case we were to decide to finance R6 fully out of the budget, prerequisites for entering into contractual obligations are the completion of the privatization of PTK and the near-completion of highway R7, to have sufficient clarity about the available budgetary space.

c. *Health care reform*. We submitted a proposal of a new Health Law to the Assembly that will allow the Ministry of Health to contract services from hospitals based on the services' quantity and quality. The contracting of services will only start after the costs have been assessed and budgeted.

d. *Civil Service Reform.* We are in the process of finalizing the terms of reference for the activities of a company that will assist the Ministry of Public Administration in establishing a grading system and a unified pay structure for civil servants. Thereafter we will, with assistance from the World Bank, re-assess the civil service reform's fiscal impact, and include cost control measures into secondary legislation as needed to keep the budgetary impact manageable. We will move forward with implementation of the reform only once its medium-term fiscal implications are fully understood.

e. *Pension reform*. A revised Pillar I Pension Law is in preparation. Legislation for the pensions for workers forcibly removed from their workplace in the 1990s will only be developed after a fiscal impact assessment has been conducted.

f. *War veteran pensions.* A working group under the supervision of the Prime Minister's Office is preparing a fiscal impact assessment for a possible war veteran pension, starting with an assessment of eligible beneficiaries. To move the work forward, we are considering hiring an international consultant to assist the working group.

16. We have enhanced the budgetary autonomy of municipalities by refraining from specifying municipal spending limits for all expenditure categories except wages from own-source revenues in the first budget circular for 2013, in line the end-May structural benchmark. In early 2013, we intend to revise the Law on Local Government Finance to (i) implement in a gradual manner the revised grant allocation in line with the 2011 census results (scheduled to be published in September); (ii) reduce gradually the size of the general grant. Going forward, we intend to allow municipalities to shift expenditures across all spending categories except wages for both own sources revenues and revenues from the general grant.

III. Financial Sector Policies

17. The financial system has remained well-capitalized, liquid, and profitable. Capital adequacy stood at 17.4 percent at end-April, while the share of nonperforming loans in total loans has continued to hover around 6 percent. Credit to private sector grew by about 11 percent in the 12 months to April. A domestic bank whose capital adequacy ratio fell below the

regulatory minimum of 12 percent last year has been recapitalized by its owners, and its board and senior management have been replaced.

18. We have submitted a revised Deposit Insurance Law (DIL) consistent with the new Banking and Microfinance Law (BML) to the Assembly on June 22, i.e., with a small delay compared to the corresponding structural benchmark of end-May. The extra time was needed to complete discussions with stakeholders, including KfW of Germany and the IMF. The revised DIL streamlines procedures to deal with troubled banks, including by allowing the use of resources from the deposit insurance fund for purchase and assumption transactions. Further, the revised law limits the deposit insurance fund's mandate to administrating payments of insured depositors, while issues related to bank resolution remain primarily the responsibility of the central bank.

19. The completion of the framework for deposit insurance is part of a larger effort to upgrade our prudential policies, with a view to safeguarding the stability and health of the banking sector in an uncertain external environment.

- The SRF for ELA establishes the central bank's capacity to combat liquidity strains in the banking sector if needed.
- The revised BML (passed in April) contains tight prudential requirements, such as limits on banks' exposures to their foreign controlling institutions of 20 percent of Tier 1 capital—containing the risk that liquidity strains in controlling institutions would spread to their Kosovar affiliates—and exposure limits to single borrowers of 15 percent of Tier 1 capital.
- Other rules and regulations, including on liquidity requirements and consolidated supervision, are currently being revised to bring them in line with the BML and Basel core principles, with an expected completion date of end-October.
- The central bank is committed to maintaining prudent loan-to-deposit ratios of around 80 percent, and to maintain high standards of corporate governance within the banking system.
- We cooperate closely with the home supervisors of Kosovar banking subsidiaries and have signed MoUs with all but one home supervisors (the remaining MoU is expected to be completed in due course).

We are confident that these measures provide strong support for our financial system to withstand strains, but are prepared to take additional measures as needed, such as requesting banks to temporarily suspend dividends payments to increase capital buffers. Further priorities may emerge from our discussions with the joint IMF/World Bank mission under the Financial Sector Assessment Program (FSAP), scheduled for September.

20. In line with the recommendation from the IMF's safeguard assessment, the CBK will continue to act as the sole investment manager for the government, and the government will continue holding all its deposits at the central bank.

IV. Competitiveness and Private Sector Development

21. To further strengthen the business climate and promote competitiveness of the economy, we have prepared a package of twelve laws to reduce costs of setting up business, unify business registries and simplify the licensing system. Eleven laws have been passed (including on business organization, cadastre, reporting and auditing, establishment of immovable property right registers, external trade, management and control of state borders, construction, and the customs code). The remaining law (on execution procedure) has been drafted and sent to the Assembly for approval, enactment is expected before end-year. To foster the development of telecommunication and mining sectors, we are preparing two additional laws that remove entry barriers and ensure equal treatment among investors. While the law regulating the mining sector is still being drafted, the law concerning the telecommunication sector is expected to be approved in the coming months. Further, we are planning to launch a joint project on promoting the development of SMEs with Austrian Development Agency and the Swiss Cooperation Office.

22. We are finalizing the analysis on the implementation of the Labor Law with an emphasis on maternity leave provisions, notably whether the length of maternity leave provokes employment discrimination against women. The final report will be ready by the end-June 2012. Thereafter we will initiate preparatory work for the amendment of the Labor Law if necessary.

23. The reform of the energy sector is advancing. In May, the bids for the privatization of the distribution and supply division of the electricity company (KEK) were received, and the winner was announced in June. This result comes on the back of important gains in KEK's revenue collection capacity and the revision of electricity price regulation, to enhance the sector's attractiveness for private investors.

Sincerely yours,

/sgd/

Hashim Thaçi
Prime Minister

/sgd/

Bedri Hamza
Minister of Finance

/sgd/

Gani Gërguri
Governor Central Bank of the Republic of Kosovo

Table 1. Kosovo: Program Monitoring

	April 2012
Performance criteria	
Floor on the bank balance of the general government	Met
Floor on the primary fiscal balance of the general government	Met
Ceiling on primary expenditures of the general government	Met
Ceiling on the net contracting of nonconcessional debt by the general government	Met
Indicative targets	
Ceiling on the stock of domestic payment arrears of the central government	Not met
Ceiling on the stock of domestic payment arrears of the general government	Not met
Prior actions for SBA approval	
Passage of the Pension Fund Law in a version that limits (i) exposure of the pillar II pension fund to the government to 30 percent of the fund's assets and (ii) annual investments of the fund in government paper to 50 percent of inflows into the fund in the previous calendar year	Met
Passage of the revised Banking and Microfinance Law in a version consistent with the recommendations of IMF technical assistance	Met
Issuance of a government decision that specifies spending cuts of €20 million across expenditure categories relative to the approved 2012 budget	Met
Structural benchmarks	
Publication of budget circulars for municipalities that contain no limits on spending allocations across non-wage categories (by end-May, 2012)	Met
Submission of a revised Deposit Insurance Fund Las to the Assembly that is consistent with the new Banking and Microfinance Law (by end-May, 2012)	Met with delay
Amendment of the Law on Public Financial Management and Accountability by a provision that specifies that only the central bank can dispose over the funds in the Special Reserves Fund designated for Emergency Liquidity Assistance (by June 15, 2012)	Met
Continuous structural benchmarks	
Monthly meetings of the Program Monitoring Committee and transmission of meetings' minutes to the IMF	Met
Inclusion of a paragraph into all new benefit creating laws, amendment to laws or regulations that allows cutting benefits if budgetary funds are unavailable	Not met
Fiscal impact assessments evaluating the budgetary impact of all new benefit creating laws, amendments to such laws or regulations over a period of at least 5 years	Met

Table 2. Kosovo: Quantitative Performance Criteria and Indicative Targets, SBA 2012-2013
(Millions of euros; flows cumulative from beginning of the year)

	2012						2013	
	End-Apr.		End-Aug.		End-Dec.		End-Mar.	End-Jun.
	Prog.	Actual	Prog.	Rev. Progr.	Prog.	Rev. Progr.	Proj.	Proj.
Performance Criteria 1/								
Floor on the bank balance of the general government	166	180	215	230	187	187	164	173
Floor on the primary fiscal balance of the general government 2/	-21	4	-41	-26	-119	-119	-7	-26
Ceiling on primary expenditures of the general government 2/	399	353	914	911	1,499	1,494	288	655
Ceiling on the net contracting of nonconcessional debt by the general government 2/	150	30	150	150	150	150	250	250
Ceiling on guaranteeing nonconcessional debt by the general government 2/	0	0	0	0	0	0	0	0
Ceiling on the accumulation of external payments arrears of the general government 3/	0	0	0	0	0	0	0	0
Indicative Targets								
Ceiling on the stock of domestic payment arrears of the central government	0	2	0	0	0	0	0	0
Ceiling on the stock of domestic payment arrears of the general government	0	2	0	0	0	0	0	0
Memorandum items:								
Program assumptions								
Repayment of policy loans extended to public corporations	…	4	…	4	4	4	0	0
Non-project grants	4	1	30	30	30	30	0	0
Budget support loans	0	0	0	0	0	0	0	0
Project grants	1	0	3	3	4	4	1	2
Project loans	0	0	6	6	7	7	1	3
PAK-related spending	…	…	3	5	5	8	1	4

Sources: Kosovo authorities; and IMF staff estimates and projections.
1/ Adjusted according to the Technical Memorandum of Understanding. Numbers are indicative targets for 2013.
2/ Excluding PAK related spending from August 2012.
3/ Continuous ceiling on the gross flow of new accumulation.

Table 3: Structural Conditionality

Actions	Type	Timing
Launch of the tender offer for PTK	Structural benchmark	End-August 2012
Submission of a 2013 budget consistent with the objectives of the program to the Assembly	Structural benchmark	End-October 2012
Monthly meetings of the Program Monitoring Committee and transmission of the meetings' minutes to the IMF Resident Representative	Structural benchmark	Continuous
Fiscal impact assessments evaluating the budgetary impact of all new benefit creating laws, amendments to such laws or regulations over a period of at least 5 years	Structural benchmark	Continuous

Technical Memorandum of Understanding

Definitions and Data Reporting Requirements under the 2012–13 Stand-By Arrangement

1. This Technical Memorandum of Understanding (TMU) sets out the understandings between the Kosovo authorities and the IMF staff regarding the definition of quantitative performance criteria and indicative targets, and reporting requirements for the Stand-By Arrangement ("SBA") requested in April 2012.

I. Performance Criteria and Indicative Targets

A. Coverage

2. For the purpose of this memorandum, the **central government** is composed of the Executive, the Legislative, and Judiciary branches of the Government, and any other public authorities except municipalities that receive direct budgetary appropriations. The **general government** includes the central government and municipalities. Both the central and the general government exclude publicly owned enterprises and socially owned enterprises.

3. **Performance Criteria and Indicative Targets.** The performance criteria, indicative targets, and their respective test dates are set in Table 2 of the Letter of Intent (LOI).

B. Bank Balances of the General Government

4. **Bank balances** are funds usable and readily available (i.e., liquid or marketable, and free of any pledges or encumbrances), held and controlled by the general government for the purposes of making payments and transfers. Bank balances include Undistributed Funds of the Government of Kosovo plus funds specifically reserved for policy purposes including emergency liquidity assistance but do not include the balance of unspent Own Source Revenues (OSR) carried forward, or funds encumbered or pledged as Donor Designated Funds and funds relative to on lending operations. Bank balances do not include investments made and managed by an outside Investment Manager assigned by the Minister pursuant to Kosovo's Law on Public Financial Management Article 7.1.(iii). Bank balances may be held in the form of gold, holdings of foreign exchange and traveler's checks, demand and short-term deposits at the Central Bank of the Republic of Kosovo (CBK), long-term deposits abroad that can be liquidated without penalty, and any holdings of investment-grade securities held directly by the general government. Bank balances at December 31, 2011, were € 159.986 million.

- The floor on the bank balance set in Table 2 will be raised by
    - the excess of budget grants and loans relative to program assumptions

5. **Reporting requirements.** A table on bank balances will be transmitted by the Treasury with a maximum delay of five weeks after the end of each month. In addition, the CBK will

submit twice a month, with a delay of 1 day, the Report of Positions of Treasury Accounts. Within 45 days after each test date, the CBK will submit to the IMF the independent audit of the reconciliation of government accounts.

C. Primary Expenditures of the General Government

6. **Primary expenditures** are measured on a cash basis cumulatively from the beginning of the calendar year. Expenditures of the Privatization Agency of Kosovo (PAK) are excluded. Primary expenditures include current expenditures (wages and salaries, goods and services, subsidies and transfers, reserves), capital expenditures, and net lending. They do not include interest payments or receipts or expenditures designated by donors financed with grants ("donor designated grants"). Net lending comprises loans granted by the general government except that it does not include onlending such as funds borrowed from KfW, which is instead included as a domestic financing item ("below the line"). All expenditures and net lending financed with loans to be serviced by the general government are in the program's concept of expenditures and net lending, even if the cash did not transit through the Treasury.

- The ceiling on primary expenditures set in Table 2 will be raised by the excess of project grants and loans relative to program assumptions.

- The ceiling on primary expenditures set in Table 2 will be lowered by

  - the shortfall of project grants and loans relative to program assumptions.
  - the repayment of loans extended to public corporations in excess of program assumptions.

7. For the purposes of this memorandum, **proceeds of privatizations** will be understood to mean all monies received by the government from the sale of a publicly owned company, organization, or facility to a private company or companies, organization(s), or individual(s), as well as any proceeds generated from the sale of government nonfinancial assets and from the liquidation of the assets of the Privatization Agency of Kosovo (PAK). Proceeds of privatizations are not part of revenues. Instead, these are recorded as a domestic financing (Net acquisition of financial assets).

8. **Reporting requirements.** Data on the monthly execution, budget appropriations, and budget allocations of revenues and expenditures will be provided monthly no later than five weeks after the end of each month, including (i) government domestic revenue detailing by components direct taxes, indirect taxes, and nontax revenues; (ii) external budget support grants; (iii) primary recurrent expenditure, (iv) domestic and external interest payments and receipts, (v) capital expenditure detailing all those related to the construction of Route 7 and including domestically and budget support financed capital expenditure and externally project financed capital expenditure; (vi) the gross payment and gross accumulation of domestic payments arrears; (vii) external loan receipts and principal payments; (viii) external arrears payments and

accumulation; (ix) bank and nonbank financing; (x) privatization and receipts of the sales of nonfinancial assets; and (xi) any other revenue, expenditure, or financing not included above.

D. Primary Fiscal Balance of the General Government

9. **Primary fiscal balance** of the general government is defined as revenues and grants minus primary expenditures cumulatively since the beginning of the calendar year. Expenditures of the Privatization Agency of Kosovo (PAK) are excluded. Revenues do not include privatization receipts.

- The floor on the primary fiscal balance set in Table 2 will be lowered by the excess in project loans relative to program assumptions.

- The floor on the primary fiscal balance set in Table 2 will be raised by

- the shortfall in project loans relative to program assumptions

- the excess in budget grants relative to program assumptions.

E. Contracting and Guaranteeing Nonconcessional Debt by the General Government

10. **Nonconcessional debt** is defined as debt contracted or guaranteed by the general government with a grant element of less than 35 percent. The grant element of a debt is the difference between the present value (PV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The PV of debt at the time of its contracting is calculated by discounting the future stream of payments of debt service due on this debt. The discount rates used for this purpose are the using currency-specific commercial interest reference rates (CIRRs) published by the Development Assistance Committee of the Organization for Economic Cooperation and Development (OECD). For debt with a maturity of at least 15 years, the ten-year-average CIRR will be used to calculate the PV of debt and, hence, its grant element. For debt with a maturity of less than 15 years, the six-month average CIRR will be used. To both the ten-year and six-month averages, the same margins for differing repayment periods as those used by the OECD need to be added (0.75 percent for repayment periods of less than 15 years, 1 percent for 15 to 19 years, 1.15 percent for 20 to 29 years, and 1.25 percent for 30 years or more).

11. The ceilings on contracting and on guaranteeing nonconcessional debt cover both domestic and external debt, but exclude purchases from the IMF and the sale of the SDR holdings allocated to Kosovo. Debt rescheduling and debt reorganization of debts contracted before the approval of the SBA are excluded from the limits on nonconcessional debt. The quantitative performance criteria apply not only to debt as defined below but also to commitments contracted or guaranteed for which value has not been received. The contracting or guaranteeing nonconcessional debt by the general government will be assessed at each test date.

12. The government of Kosovo will consult with Fund staff before contracting or guaranteeing any new debts in circumstances where they are uncertain whether the instrument in question is covered under the quantitative performance criterion.

13. **Definition of debt.** The definition of debt is set out in Executive Board Decision No. 12274-(00/85), Paragraph 9, as amended on August 31, 2009 (Decision No. 14416-(09/91)):

> "(a) For the purpose of this guideline, the term **"debt"** will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows:
>
> > "(i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);
> >
> > "(ii) suppliers' credits, i.e., contracts where the supplier permits the obligor to defer payments until some time after the date on which the goods are delivered or services are provided; and
> >
> > "(iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair or maintenance of the property.
>
> "(b) Under the definition of debt set out in this paragraph, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt."

14. **Reporting requirements.** Details of all new debt taken or guaranteed, indicating terms of debt and creditors, will be provided on a quarterly basis within five weeks of the end of each quarter.

F. Domestic Payments Arrears

15. A domestic payment obligation to suppliers or creditors is deemed to be in **arrears** if: (a) goods and services have been received; (b) they have been certified to conform to the order of the contract; and (c) the obligation has remained unpaid for more than 60 days after the invoice was received. A payment obligation is defined to be domestic if the creditor is resident in Kosovo.

16. **Reporting requirements.** The Ministry of Finance will submit a monthly table with the stock of domestic payments arrears and not in arrears. The data are to be provided within five weeks after the end of the month.

G. External Payments Arrears

17. **External arrears** are defined as total external debt service obligations of the government that have not been paid by the time they are due (after the expiration of the relevant grace period). External arrears exclude external debt service obligations subject to ongoing good faith negotiations of debt-rescheduling agreements. A debt service obligation is defined to be external if the creditor is not resident in Kosovo.

18. **Reporting requirements.** The Ministry of Finance will inform the Fund staff immediately of any accumulation of external arrears. Data on (i) debt-service payments; and (ii) external arrears accumulation and payments will be transmitted on a quarterly basis by the Ministry of Finance within five weeks of the end of each quarter.

II. Other Data Requirements

19. The monthly monetary statistics (including balance sheets and monetary surveys) of the CBK, the consolidated commercial banks and revisions to historical data (if any) will be transmitted on a monthly basis with a maximum delay of five weeks

20. Data on exports and imports, including volume and prices and compiled by the Statistical Office of Kosovo (SOK), will be transmitted on a quarterly basis within forty-five days after the end of each quarter.

21. A preliminary quarterly balance of payments, compiled by the CBK, will be forwarded within three months after the end of each quarter.

22. The table of Financial Soundness Indicators and the regulatory capital and liquidity ratios of individual banks will be transmitted by the CBK to the IMF on a monthly basis within six weeks after the end of each month.

23. A monthly report on the number of employees will be transmitted to the IMF by the Treasury Department of the Ministry of Finance within two weeks after the end of each month.