

**ALBANIA**  
**Corporate Financial Reporting Enhancement Project (CFREP)**  
**PROJECT APPRAISAL DOCUMENT**  
**Europe and Central Asia Region**  
**Unit: ECCAT/Centre for Financial Reporting Reform**

Date: 10/30/2009 Country Director: Jane Armitage Sector Manager/Director: Ahmadou Moustapha Ndiaye/ Gerard A. Byam		Team Leader: Andrei Busuioc Sectors: FZ Gen finance sector 100% Themes: Standards and financial reporting 40% Regulation and competition policy 20% Legal institutions for market economy 20% Other human development 20%	
Project ID: P125591 Lending instrument: Recipient Executed Single Donor Trust Fund		Environmental screening category: C Safeguard screening category: n/a	
Project Financing Data:			
[ ] Loan [ ] Credit [X] Grant [ ] Guarantee [ ] Other:			
Total Donor financing (EUR m.): [1.25]			
Financing Plan (EUR\$m.)			
Source	Local	Foreign	Total
Recipient			0.2
IBRD/IDA			1.25
Others			
Total			1.45
Recipient: [IN KIND] Responsible agency: Ministry of Finance			
Estimated disbursements (Bank FY/US\$m)			
FY			
Annual			
Cumulative			
Project implementation period: 3 years Expected effectiveness date: 07/01/2010 Expected closing date: 06/30/2013			
Does the project depart from the CPS in content or other significant respects? Ref. PAD A.3		○ Yes x No	
Does the project require any exceptions from Bank policies? Ref. PAD D.7		○ Yes x No	
Have these been approved by Bank management?		○ Yes x No	
Is approval for any policy exception sought from the Board?			
Does the project include any critical risks rated “substantial” or “high”? Ref. PAD C.5		x Yes ○ No	

Project development objective Ref. PAD B.2, Technical Annex 3

The proposed Project Development Objective (PDO) is to create a transparent policy environment and effective institutional framework for corporate financial reporting in line with best international practices, aligned with EU *acquis communautaire*.

Specifically, the project's expected results are: (a) Improve legitimacy of the legal framework in the area of corporate financial reporting by aligning it with the EU *acquis communautaire*; (b) Strengthen standard setting by the National Accounting Council (NAC); (c) Improve standard setting and supervision of auditing practices by the audit oversight system; (d) Improve skills for compliance with new professional standards through revisions and updates of accounting and auditing curricula for university education and professional certification; and (e) Improve management of reforms in corporate financial reporting by the National Steering Committee and the MoF.

## CURRENCY EQUIVALENTS

Exchange Rate Effective March 23, 2010

Currency Unit - LEK; CHF 1= USD 0.94; USD 1= LEK 102.60

**FISCAL YEAR-** January 1 – December 31

## ABBREVIATIONS AND ACRONYMS

A&A	Accounting and Auditing
BCBS	Basel Committee on Banking Supervision
CAP	Country Strategy and Action Plan
CEBS	Committee of European Banking Supervisors
CEIOPS	Committee of European Insurance and Occupational Pensions Supervisors
CESRfin	Committee of European Securities Regulators – Operational Group on Financial Reporting
CPS	Country Partnership Strategy
CPD	Continuing Professional Development
EU	European Union
FBE	European Banking Federation
FEE	European Federation of Accountants
GDLN	Global Development Learning Network
IAASB	International Auditing and Assurance Standards Board
IAIS	International Association of Insurance Supervisors
IAPC	International Auditing Practices Committee
IAPS	International Auditing Practice Statement
IAS	International Accounting Standards
IASB	International Accounting Standard Board
IASC	International Accounting Standards Committee
IASCF	International Accounting Standards Committee Foundation
IEKA	Institute of Authorized Chartered Auditors of Albania
IES	International Education Standards
IFAC	International Federation for Accountants
IFRIC	International Financial Reporting Interpretation Committee
IFRS	International Financial Reporting Standards
IOSCO	International Organization of Securities Commissions
ISA	International Standards on Auditing
MoF	Ministry of Finance
NAS	National Accounting Standards
NSC	National Steering Committee
QA	Quality Assurance
REPARIS	Road to Europe – Program of Accounting Reform and Institutional Strengthening
ROSC	Report on Observance of Standards and Codes
SIC	Standing Interpretation Committee
SMEs	Small and Medium Enterprises
SMOs	Statements of Membership Obligations

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## ALBANIA

### Corporate Financial Reporting Enhancement Project (CFREP)

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## I. STRATEGIC CONTEXT AND RATIONALE

### A. Country and sector issues

#### *Country Background*

1. Despite recent reforms in the business regulatory framework, reflected in Albania's progress in Doing Business 2010 ranking at 82<sup>nd</sup> place out of 183 globally in 2010 (a slight improvement to 86<sup>th</sup> place out of 181 countries in 2009), its business environment remains to a great extent inadequate. The international integration of the Albanian economy is limited, thus constraining the opportunities that Albanian firms have to acquire knowledge from foreign competitors, customers and investors. Sectors in which Albania exports and receives foreign direct investment (FDI) are labor intensive, with a relatively low level of technological and marketing know-how.

2. Corporate financial reporting is an important element of developing the Albanian market and its role is growing, along with the corporate sector development and an increase in direct foreign investment (FDI)<sup>1</sup> by 45% in 2009, mainly due to privatization of large state-owned companies and some improvements in the business environment. FDI inflows are significant, around €650 million, which is about 7% of GDP, while corporate foreign financing remained low in 2009. The main challenge for Small and Medium Enterprises (SMEs) development remains the relatively poor investment climate. Also, poor law enforcement, weak corporate governance<sup>2</sup> both at the macro and at the enterprise levels, lack of management skills, lack of export competitiveness<sup>3</sup> and poor infrastructure constitute the major impediments to SME development. Additionally, the high rate of informal economy, which is estimated to be around 30-50%, remains also a serious concern.

#### *Key sector issues*

##### *Sectoral development issues*

3. The World Bank carried out a diagnostic assessment - Accounting and Auditing Report on the Observance of Standards and Codes (A&A ROSC) in 2006<sup>4</sup>. Although some progress in corporate financial reporting reforms was noted in the report, the report proposed a number of policy recommendations for further improvements in the statutory framework, and in institutional and professional capacity building :

- Enhancement of the statutory framework governing financial reporting;
- Enhancement and creation of sustainable standard setting structures for the production of high quality accounting and auditing standards and guidelines on their application;
- Establishment of systematic monitoring and enforcement mechanisms to ensure compliance with accounting and auditing standards;
- Improvements of the quality of the work done by the accounting and auditing profession through extensive capacity development initiatives aimed at existing practitioners; and

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<sup>1</sup>United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2009*, dated 18 September 2009.

<sup>2</sup> European Bank for Reconstruction and Development (EBRD), *corporate governance sector assessment of 2008* concluded that *Albania* was in "low compliance" with the relevant Organization for Economic Cooperation and Development (OECD) international standards on corporate governance.

<sup>3</sup>World Economic Forum: *The Global Competitiveness Index Report 2009-2010*, Albania's rank in economic competitiveness in 2010 improved from 108<sup>th</sup> out of 134 countries to 96<sup>th</sup> out of 133 countries with a score 3.72 out of 7, compared to 2009.

<sup>4</sup> [http://www.worldbank.org/ifa/rosc\\_aa\\_alb.pdf](http://www.worldbank.org/ifa/rosc_aa_alb.pdf)

- Increase in the number of accounting and auditing professionals able to prepare high quality financial statements and to conduct high quality audits, respectively. This would involve providing incentives to attract bright graduates to the profession and raising the recognition of the qualification.

### *Priority sector issues*

4. The recent legislation adopted in accounting and auditing (Law on accounting and financial statements and Law on statutory audit, organization of statutory auditor and certified accountant professions) is to a large extent based on relevant EU requirements. However, key policy makers and stakeholders in corporate financial reporting do not have clear knowledge and understanding of the degree of compliance of the recently adopted legislation with the EU *acquis communautaire*, hence there is no clear vision and roadmap as to how to align in full the statutory framework, over time, with the EU requirements. In addition, it seems that there is no full coherence among various pieces of legislation as it relates to corporate financial reporting matters. This could be attributed to institutional capacity constraints, limited knowledge and understanding among various stakeholders of the *acquis* provisions, their underlying principles and how they relate to the Albania's context.

5. The accounting standards setter needs technical and financial capacity to carry out its mandate to adopt and produce high quality standards. This relates to both IFRS to be applied by public interest entities (PIEs), and adequate accounting standards to be applied by SMEs. Currently, there are no sustainable mechanism for IFRS translation, publication and updates<sup>5</sup>; as for the accounting standards for SMEs, there is no clear vision on how to align the existing national standards with the EU requirements, or whether the IFRS for SMEs recently issued by IASB should be adopted. Also, the standards setting process requires further improvements with a view to becoming more open, transparent and participatory.

6. The new auditing law<sup>6</sup> requires establishing a public oversight system in auditing and this is currently in progress. There is an immediate need to develop bylaws and regulations of the public oversight system, including those related to IEKA and public oversight board, to address the issue of roles and responsibilities of different institutions, establish public registry of auditors, establish a sustainable mechanism for auditing standards translation and adoption, as well as tools and manuals to be created for the auditing quality assurance.

7. Although accounting and auditing are taught at local universities and the Ministry of Finance (MoF) is responsible for professional certification of auditors, the education curricula and teaching materials are not fully compliant with IFAC's International Education Standards (IES) and do not fully cover auditing, ethics and IFRS. There is a need to update the education curricula and teaching materials to be adopted and used by universities and professional bodies.

8. Although the National Steering Committee (NSC) chaired by Deputy Minister of Finance was created by the authorities in Albania to coordinate and oversee the corporate financial reporting

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<sup>5</sup> According to accounting law, IFRS are to be applied by public interest entities. IFRS in context of Albanian law, are those that are developed by IASB, translated into Albanian language under authority of national Accounting Council with no changes to original English text.

<sup>6</sup> The new auditing law was adopted by the Parliament of Albania in March 2009. The law is based on the key provisions of EU statutory audit directive and calls for establishing a public oversight system. A significant role in public oversight is assigned to IEKA, which in fact will play the role of Chamber of auditors. The law also contains requirements for entering the audit profession, registration of auditors, requires ISA as translated in Albanian to be applied by auditors and requires establishment of internal and external quality assurance systems.

reforms in Albania, the reform capacity of NSC and MoF should be strengthened to enable the authorities to adequately plan, undertake, coordinate and monitor progress with reform implementation.

### *Government strategies and commitment*

9. The Government of Albania has made some progress in reforms in corporate financial reporting: (i) the 2004 Accounting Law; (ii) the 2009 Auditing Law; and (iii) the Country Action Plan to Enhance Corporate Financial Reporting in Albania (CAP) was adopted in February 2009, based on the recommendations of the 2006 A&A ROSC.

10. The following three pillars and sub-activities are envisaged under the CAP:

- Enhancing the Institutional Framework: (i) Delivering a Complete, Consistent and Practical Statutory Framework; (ii) Establish “Education and Examination Center for Accountants and Auditors”; (iii) Enhancing the Institutional Framework: Establish Audit Oversight Body; (iv) Enhancing the National Accounting Council;
- Strengthening of the Institutional Capacity: (i) Central Bank: Enforcement of IFRS in the Banking Sector; (ii) Taxation Authorities: Use of NAS and IFRS for Taxation Reporting; (iii) Financial Services Authority: Enforcement of IFRS in the insurance sector and capital markets; (iv) National Registration Centre: Implement Effective Electronic Filing of Companies Financial Statements; (v) The Audit Profession (IEKA); (vi) The Accounting Profession; (vii) The University Sector;
- Raising Awareness on Corporate Financial Reporting: (i) Public Awareness Campaign on Informal Economy and benefits of Accounting & Auditing; (ii) Training for the Judiciary & Independent Financial Experts.

11. The overall objective of the CAP is to align corporate financial reporting standards and practices with the EU *acquis communautaire* through implementation of related reforms and institutional capacity strengthening. Given the complexity of the reforms, the Government is committed to implementation of the CAP in phases, in line with priorities, the absorptive capacity, and the proper sequencing of the reform activities. The rationale for the phased approach is the limitation of absorptive capacity and the complexity and long-term nature of the corporate financial reporting reforms.

12. Albania is an active participant in The Road to Europe: Program of Accounting Reform and Institutional Strengthening (REPARIS) program, a regional program aimed at creating a transparent policy environment and effective institutional framework for corporate reporting within eight countries of the South Central and South East Europe<sup>7</sup>. The regional activities of this program are focused on creating awareness and reforms enabling environment, while the country focused activities are aimed at supporting implementation of those reforms in each participating country. The proposed CFRE project will comprise activities at the country level to enable transferring knowledge and experience

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<sup>7</sup> Participating countries/entities include Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Kosovo, the former Yugoslav Republic of Macedonia, Moldova, and Serbia and Montenegro. The REPARIS Program is designed around the introduction, implementation, and effective enforcement of relevant portions of the EU *acquis communautaire* with a view to contribute to foreign direct and portfolio investment, foster private and financial sector developments, improve the business environment and investment climate, and facilitate potential integration into (or harmonization with) the European Union. The program is supported by funding provided by Austrian and Luxemburg Governments.

acquired and exchanged in the context regional activities with a view to designing and implementing respective reform programs.

13. The reform program in Albania seeks to implement the 2009 CAP, over the medium- to long-term (8-10 years). The first phase will be focusing on the immediate priority actions, identified as critical for sustaining the on-going reform process, and for establishing building blocks as to facilitate subsequent and deeper reform activities. The second phase will build on the achievements of the first phase and will deepen the reforms, but will also support implementation of the CAP activities not addressed in the first phase. The third phase will seek to consolidate achievements from the first two phases and to complete the implementation of the remaining activities under the CAP, with focus on further institutional capacity development.

### ***B. Rationale for Bank involvement***

14. The 2006 A&A ROSC assessment indicated the incidence of some systematic issues as a result of previous reform activities. For example, building the profession without regulatory reforms to put in place a sound enforcement and monitoring institutional infrastructure may undermine reform efforts and results.

15. Until recently the Bank and other development partners were supporting some reform efforts in the area of corporate financial reporting: (i) USAID in professional development; and (ii) the Bank Financial Sector Adjustment Credit (FSAC) supported drafting the 2004 Accounting Law. Currently there are no development partners involved in a comprehensive manner in supporting reforms and institutional capacity building in this area. There are some isolated activities in the banking sector and taxation (twinning projects) funded by the European Commission (EC), as well as the World Bank Special Projects Initiative Project (SPI) in Albania<sup>8</sup>. Under the IFC Corporate Governance project, support is provided to improvements of corporate governance in selected companies and scaling up the benefits of good corporate governance practices to broader group of companies.

16. Implementation of the first phase of the CAP is in line with the CAS's objectives. The rationale for continued Bank support to implementation of the reforms in corporate financial reporting is to integrate the five key elements of the framework for strengthening corporate financial reporting : (i) a robust diagnostic instrument, the A&A ROSC; (ii) development of a CAP to implement the A&A ROSC policy recommendations; (iii) effective mobilization of adequate donor financing to support implementation of the CAP; (iv) implementation of the CAP at the country level expanding regional REPARIS program efforts, with technical advice and implementation support provided by the Bank; and (v) monitoring and evaluation and knowledge sharing at regional level, carried out and managed by the Bank with donor support.

17. The comparative advantage of the Bank is that the Centre for Financial Reporting Reform (CFRR), based in Vienna, Austria, has extensive knowledge and expertise in this area of corporate financial reporting reforms in the ECA Region, it has been set up to be close to the client countries, and it works both on country and regional level. In addition, the CFRR is in permanent contact with EC accounting and auditing partners, thus ensuring harmonization and adequate implementation or relevant parts of EU *acquis communautaire*.

18. In response to the Government's request in the context of the Regional REPARIS program, a World Bank project team at the CFRR, conducted project identification in May, 2009.

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<sup>8</sup> The SPI Unit in Albania is supported by the World Bank's Convergence Program in Rome, Italy and established under the regional SPI Adriatic initiative.



### ***C. Higher level objectives to which the project contributes***

19. The proposed project is in line with 2006 Country Assistance Strategy (CAS) objectives, and will be part of the new Country Partnership Strategy (CPS) currently under preparation. Specifically, the proposed project will support the current's CAS pillar (I) *Continued Economic Growth through Support to Private Sector Development* and expected outcome (f) *improved corporate governance*. The related CAS outcomes under this pillar include: Improved accounting and auditing standards and disclosure of corporate information in line with EU requirements by FY09.. The 2006 A&A ROSC was included in AAA for FY 2006, and the Road to Europe – Program of Accounting Reform and Institutional Strengthening (REPARIS) is indicated as the relevant Bank program to the country development goal 2 “enhance effectiveness of public sector and governance structures to support private sector development” of 2006 CAS.

## **II. PROJECT DESCRIPTION**

### ***A. Financing***

20. The proposed Corporate Financial Reporting Enhancement Project (CFREP) seeks to support the first three year phase of implementation of the CAP, in the context of an integrated programmatic approach to support improving financial reporting in Albania. Hence, the proposed project will support implementation of the first phase of the CAP, with the focus on priority activities envisaged under the CAP. In preparing foundations for implementation of the two subsequent phases, the proposed project will finance preparation of studies and will conduct workshops to facilitate the reforms decision making process of the key policy makers and stakeholders, in order to raise their awareness of pending institutional development challenges to be undertaken in the subsequent phases, with World Bank technical advice.

21. The proposed project will focus on priority activities for the corporate financial reporting through support in: (i) improving the legal framework; (ii) strengthening the national accounting standard setter; (iii) establishing a public oversight system for independent auditors; (iv) improving accounting and auditing curricula; and (v) strengthening reform capacity of the Government in area of corporate financial reporting, including preparation of the following phases of the reforms.

22. The project will be financed under a Swiss grant already identified, and yet to be set-up in a single donor trust fund, administered by the Bank and executed by the Ministry of Finance. The Government is not interested in borrowing from the World Bank for technical assistance. Thus far the Swiss State Secretariat for Economic Affairs (SECO) has pledged the financing for the implementation of the first phase of the project. No other donor, at this point, has expressed interest to contribute to implementation of the CAP. The Bank remains open to accommodate additional financing should any development partner expresses an interest to support implementation of the CAP.

23. The Government indicated its willingness to co-finance the project by an in-kind contribution of up to ten percent as a sign of its commitment.

24. Given the strong Government's commitment to the reforms, it is likely that subsequent phases of the CAP implementation will be financed under the EU Instrument for Pre-Accession (IPA) funds. In that case, the Bank, through the CFRR will be involved in providing implementation support and technical advice in design and implementation of reform and institutional strengthening activities for the next phase, along with monitoring and evaluation of progress, in the context of the Regional REPARIS Program.

## ***B. Project development objective and key indicators***

25. The Overall Development Objective of the reform program (CAP) is to improve accountability and transparency in corporate financial reporting in Albania in line with international good practices, by the way of aligning the statutory and institutional frameworks with the EU *acquis communautaire* with a view to Albania's aspiring to EU accession.

26. The proposed Project Development Objective (PDO) is to create a transparent policy environment and effective institutional framework for corporate financial reporting in line with best international practices, aligned with EU *acquis communautaire*.

27. Specifically, the project's expected results are: (a) Improve legitimacy of the legal framework in the area of corporate financial reporting by aligning it with the EU *acquis communautaire*; (b) Strengthen standard setting by the National Accounting Council (NAC); (c) Improve standard setting and supervision of auditing practices by the audit oversight system; (d) Improve skills for compliance with new professional standards through revisions and updates of accounting and auditing curricula for university education and professional certification; and (e) Improve management of reforms in corporate financial reporting by the National Steering Committee and the MoF.

28. Proposed project outcomes are expected to be sustained upon the project completion through: (i) a solid proposal for further improvements in the statutory framework prepared and discussed by concerned stakeholders and ready for decision making, while the essential capacity for the design and implementation of the next phase of reforms will be in place; (ii) achievements will serve as building blocks for further reform efforts in corporate financial reporting, to be financed under the EU IPA mechanism; and (iii) complemented with the knowledge acquired at the Regional REPARIS Program, the informed stakeholders and policy makers in Albania will be empowered to take further reform steps.

29. The monitoring and evaluation results framework for the project is in Annex 3. Given the length of the project of up to three years, the key intermediary outcomes will be measured in terms of how changes will be induced through project support:

- a. The policy makers and other key stakeholders are adequately informed to take decisions and committed to designing next steps in reforms to support the further alignment of corporate financial reporting legislation with the EU *acquis communautaire*. This outcome will influence stakeholders' participation in and commitment to decisions related to the reform process.
- b. The accounting and auditing standards setters are better equipped to adopt, translate and make available to the users and education institutions accounting and auditing standards on a regular basis. This outcome will influence the operational efficiency in accounting and auditing standards setting.
- c. The newly established audit oversight institutional arrangements and auditors are adequately informed about the mission of the public oversight system and requirements for auditors. This outcome will influence the clarity of mission of the audit oversight system.

## ***C. Project components***

The proposed project comprises five components.

**Component 1. Improving the legal framework in the area of corporate financial reporting (estimated cost EUR XXX)**

30. This component will finance technical assistance and workshops to establish a sound basis for corporate financial reporting legislation alignment with the EU *acquis communautaire*. A national legislation gap assessment vis-à-vis the EU *acquis communautaire* will be conducted. The assessment will include a review of the existing accounting, auditing, and company legislation, preparation of a comprehensive concordance tables to identify gaps and inconsistencies in the legislation, and will also finance preparation of a time-bound roadmap for the full alignment of the corporate sector relevant legislation with the EU *acquis communautaire*. Under this component, workshops will be financed to increase the awareness of the key stakeholders, and the public in general, on the importance of fully aligning the relevant Albanian legislation with the EU *acquis communautaire*, over time, in accordance with an agreed time-table. The beneficiary agencies for this component are the Ministry of Finance, Parliamentary Committee for finance, budget and economy, and other decision makers such as members of NSC.

### **Component 2. Strengthening the Capacity of the National Accounting Council (estimated cost EUR XXX)**

31. Under this component, the capacity of the National Accounting Council will be strengthened, as well as processes for the setting and endorsement of financial reporting standards, through technical assistance and training. Specifically, the proposed activities include: (i) enhancing the standard setting process and improving the content of accounting standards for SMEs through either improvement of National Accounting Standards (NAS) to be compliant with EU Fourth and Seventh Directive requirements, or adoption of the IFRS for SMEs (the decision will be made by the authorities on the basis of a detailed analysis of options and consultations); and (ii) enhancing NAC capacity in IFRS understanding, creating a sustainable mechanism for IFRS adoption, and translation updates, as part of the process of endorsing IFRS for use in Albania<sup>9</sup>. The Beneficiary/Responsible Agencies for this component are the National Accounting Council and MoF.

### **Component 3. Establishment of an Audit Oversight System (estimated cost EUR XXX)**

32. Under this component, the project will finance technical assistance, workshops and goods to support strengthening of the recently established public audit oversight system envisaged in the new auditing law adopted in 2009, will focus on: (i) drafting the secondary legislation for public oversight system and the development of public register for auditors; (ii) improving auditing standards setting through translation and adoption of ISA; and (iii) creation of tools and methodologies for an auditing quality assurance system. The beneficiaries of this component are – the Public Oversight Board (recently established according to the new Auditing law) and IEKA (the auditing professional body acting as an Auditing chamber in the proposed public oversight structure), and statutory auditors.

### **Component 4. Improving accounting and auditing curricula for university education and professional certification (estimated cost EUR XXX)**

33. Under this component, the project will finance TA and workshops to assist universities, professional bodies and the examination center (to be created under the MoF) to build foundations for sustainable curricula for accounting and auditing education and certification of whom accountants and auditors. The activities will include: (i) technical assistance to develop the core accounting and auditing curricula for professional certification and university education compliant with IFAC

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<sup>9</sup> Albania has chosen to apply IFRS as they are issued by IASB. In the case of EU accession, the country will have to adopt IFRS as endorsed by the EU.

International Education Standards (IES); (ii) technical assistance to create pilot training materials, manuals and case studies to support the education process. The activity will build on the results of regional activities in this area carried out under the Regional REPARIS Program, whereby common solutions are developed and proposed to participating countries. The beneficiary agencies for this component are universities, professional associations and MoF.

#### **Component 5. Project management, strengthening reform capacity, and monitoring and evaluation (estimated cost EUR XXX)**

34. This component will include necessary incremental operating costs related to project management, including the overall reform management and coordination, and project-related fiduciary activities (procurement and financial management). In addition, this component will monitor progress in implementation of the reform activities supported under the proposed project, and will facilitate preparation of the next phase of the reforms. It will also seek to build the capacity of the reform implementation group in planning and implementation of the EC IPA resources, likely to be used in support of implementation of next reform phases. The key beneficiaries of this component will be MoF and NSC.

#### ***D. Lessons learned and reflected in the project design***

35. The design of the proposed project reflects lessons learned from the implementation of a similar project in the ECA Region. Invariably, country-specific CAPs are overambitious; they include too many activities to be implemented over too short time period, without adequate prioritization, sequencing through a phased-approach, unrealistic expected outcomes, and without specific outputs and related terms of reference for specific assignments in the initial phase of the CAP implementation. In addition, a weak political commitment and a frequent lack of buy-in into the CAP implementation by the key stakeholders, as well as inadequate project management capacities, including lack of realistic procurement plans and related TORs are likely to cause significant delays in project implementation.

36. The following lessons have been incorporated into the design of the proposed project: (i) implementation of reforms and related capacity development will be carried out in phases over the short, medium- and long-term; (ii) a clear evidence of the sustained political commitment and support to the reform process; (iii) only high-priority activities of the reform are being addressed in the first phase, by focusing on adequately sequencing reform activities in line with the absorptive capacity of the key beneficiaries; and (iv) assistance under the proposed project is targeted to achieve clearly defined intermediary project outcomes, with a view to achieving broader program development outcomes as set out in the CAP, over the medium to long-term; (v) using the existing institutional arrangements and capacity for implementing similar operations, particularly in the area of procurement and financial management; and (vi) building capacity in planning, coordinating and implementing reforms in corporate financial reporting is one of the project objectives, included in the project activities with a view to enabling the Government to continuing with the next phase of CAP implementation.

#### ***E. Alternatives considered and reasons for rejection***

37. No alternative funding instrument has been considered to the proposed project as the authorities are not interested in borrowing from the Bank for technical assistance activities, While and

Institutional Development Facility (IDF) would be able to support only a small segment of the CAP and could not ensure the sustainability of the reform process. In addition, in the case of Development Policy Lending (DPL) option, even if the financial reporting agenda were included, the reform program would require significant technical support and time for capacity development which would not be available under such an instrument. Although complementary assistance is available under the Regional REPARIS activities, this is not sufficient to underpin institutional development at the country level. Thus, the combination of regional activities with focused support at the country level is envisaged to achieve tangible and sustainable outcomes.

### **III. IMPLEMENTATION**

#### ***A. Institutional and implementation arrangements***

38. The responsibility for the project implementation will be with key stakeholders, project coordination and day-to-day project management with the MoF, while the NSC will have an overall oversight role. The MoF will set up a reform implementation group (RIG), as set out in the 2009 CAP, which will include qualified MoF staff for the day-to-day work on the project management and coordination. The project will include the provision of both technical and financial resources to strengthen the reform implementation capacity of the reform implementation group.

39. Fiduciary aspects of the trust fund management, including procurement and financial management, will be handled by the Central Finance and Contracting Unit (CFCU) at the MoF, primarily responsible for implementation of the EU IPA funds. CFCU is also responsible for managing fiduciary aspects of the existing Integrated Planning System Multi-Donor Trust Fund (P105143, TF90843-recipient-executed and World Bank administered); the unit has an adequate financial management and procurement capacity to manage an additional donor trust fund. The fiduciary arrangements will be further assessed and confirmed during the project appraisal. The EU is currently financing the provision of technical assistance to strengthen the unit's capacity for implementation of EU IPA funds (Annex 4 contains detailed implementation arrangements).

#### ***B. Monitoring and evaluation of outcomes/results***

40. During project implementation, project monitoring and evaluation (M&E) will be the responsibility of the reform implementation group and supervised by the World Bank project team, with periodic consultation with donors and facilitation of stakeholder participation. The MoF will monitor progress by using the agreed project results framework (Annex 3).

#### ***C. Sustainability***

41. The adoption of the Government CAP in early 2009 is a clear indication of commitment. In addition, the political agenda of the Albanian Government for EU accession includes a comprehensive alignment of all statutory and institutional frameworks with EU requirements, including the alignment of corporate financial reporting requirements and practices. The MoF and NSC have worked closely with the Bank project team in conducting the A&A ROSC diagnostic work, definition of the CAP and in designing the proposed project. In their work under the Regional REPARIS program, they have confirmed their strong support to project implementation. Proceeding to the subsequent phase in implementation of the CAP will be conditioned on the results established under the previous phase. In

turn, achieved results at the end of the first phase will give a strong signal to the EU institutions on progress in the alignment with the EU requirements.

***D. Critical risks and possible controversial aspects***

42. Potential project risks may broadly be defined as generic and project specific risks. The overall risk for the proposed project is considered modest to substantial.

<b>Risk</b>	<b>Risk rating</b>	<b>Mitigating Measures</b>
<b><i>General Risks</i></b>		
<i>Government commitment risk.</i> Newly formed Government may not be fully supportive of the proposed reforms.	Modest	One of the key priorities of the new Government is to work in earnest towards the full alignment with the EU requirements with a view to EU accession.. The current Deputy Minister of Finance, in charge of corporate financial reporting reforms, is actively involved in the Regional REPARIS program and he confirmed at the December 2009 Ministerial conference in Vienna his Government’s commitment to and priority to implement the CAP. Putting corporate financial reporting reforms in the center of country objectives to support private sector development in the new Bank CPS, will make it an important item of the Bank policy dialogue with the authorities. The risk will be further mitigated through the revision of the NSC’s composition to ensure a better link with the Regional REPARIS activities to assist them as the Chapter 6 team in negotiations with the EU. Continued involvement of the former Deputy Minister of Finance as an active member of NSC in his new capacity as a member of the Parliament.
<b><i>Project-Specific Risks</i></b>		
<i>Institutional capacity risk.</i> Not all the members of the NSC fully understand the scope of the proposed project and the effort needed to fully implement it as designed.	Substantial	The NSC has been informed by the Bank project team on the importance of the phased-approach to implementation of the CAP, and how the proposed project focuses on the first phase. Several members of the NSC are involved in the Regional REPARIS program, where they actively participate in prioritizing and sequencing activities to be implemented at specific country level for participating REPARIS countries. Workshops and seminars will be supported under the proposed project to broaden the understanding of best practice settings and other countries. Moreover, training and assistance will be provided in project management and change management through raising awareness activities, as well as leadership development for further reform implementation. To further mitigate this risk, the Deputy Minister of Finance intends to re-convene the NSC and consider an option of its wider membership, so that all the stakeholders that have a role to play in corporate financial reporting reform are involved.

Risk	Risk rating	Mitigating Measures
<i>Policy choice decisions.</i> Stakeholders cannot agree on strategic decision during the project on adopting IFRS-for-SMEs versus development of NAS, causing delays and potentially blocking the process.	Modest	The risk will be mitigated through specific capacity building activities, aimed among the other things, to assess the adequacy for the country to implement IFRS for SMEs, and also to better inform national accounting standards setter about the implications of NAS development that have to be compliant with the EU requirements.
Difficulty to identify consultants with appropriate competence and ability to operate in the Albanian environment	Modest	The risk will be mitigated through appropriate procurement planning enabling wider competition and identification of consultants familiar with the region and through the knowledge and contacts of international expertise and relevant regulatory bodies, consulting firms and renowned individuals established at the CFRR in Vienna.
<i>Implementation capacity.</i> Implementation and M&E capacity of the key stakeholders in planning activities and managing project resources is limited.	Substantial	This risk will be mitigated through support to be provided under the proposed project through: (i) using the MoF unit in charge of implementation of similar multi-donor trust-fund with sufficient fiduciary capacity; and (ii) day-to-day project implementation will be supported by technical assistance to advice relevant stakeholders on a day-by-day basis.

### ***E. Trust Fund conditions and covenants***

43. The proposed project will become effective upon the signature of the legal Grant Agreement between the Bank and the Government of Albania. Prior to the Grant Agreement, the Bank will sign a Trust Fund Administration Agreement with the Donor.

44. **The conditions for signing the Grant agreement** are: (i) appointment of the reform implementation group and its head by the MoF; and (ii) procurement plan acceptable for the Bank for the first 18 months developed.

45. The MoF, through its Central Finance and Contracting Unit will maintain a financial management system acceptable to the Bank. The project financial statements will be audited by independent auditors acceptable to the Bank and on terms of reference acceptable to the Bank. The annual audited financial statements and the audit report will be provided to the Bank within six months of the end of each fiscal year. The MoF shall also prepare and furnish to the Bank not later than forty five (45) days after the end of each calendar quarter, interim unaudited financial reports for the project covering the quarter, in form and substance satisfactory to the Bank.

## **IV. APPRAISAL SUMMARY**

### ***A. Economic and financial analyses***

46. The detailed economic and financial analysis for this project was not undertaken due to its relatively small size and difficulty to appraise all benefits to the society. The main benefits for Albania of this project will be: (i) the complex approach to corporate financial reporting reform is taken through supporting key priority areas of CAP; (ii) the project will build foundation for the next phase of implementation of the CAP; and (iii) inform policy makers decisions on options for changes in the statutory and institutional frameworks suitable to ring Albania in pursuing its accession to the EU agenda as it relates the EU *acquis communautaire* in the field of financial reporting.

47. Expected benefits from implementation of the reform program over the medium to long-term are likely to: (i) lead to the transparency and accountability in financial reporting; (ii) improve investment and lending decision-making in corporate sector; (iii) increase confidence of potential investors, and (iv) contribute to the on-going efforts in combating corruption. Albania will also benefit from higher transparency in corporate sector through better tax collection and increased FDI

### ***B. Technical***

48. The rationale for the selected project design is based on the idea of supporting the broader reform agenda set out in the CAP, as well as of implementing the requirements of the new accounting and auditing laws to allow for their enforcement in the areas already aligned with the EU *acquis communautaire*. The activities selected jointly with the MoF and NSC, are indicated as the key building blocks for a healthy financial reporting regime and as the main priorities that will enable further reform steps.

49. The project will support the following essential pillars of the financial reporting infrastructure: (i) accounting standards setting and adoption; (ii) establishing an audit oversight system; (iii) accountancy education; and (iv) government's reform capacity in area of corporate financial reporting. The main benchmark for the reforms is the EU *acquis communautaire* and their relevant practical application in the Albanian context.

### ***C. Fiduciary***

#### ***a) Financial Management***

50. The CFREP will be implemented by the CFCU within the MoF. An assessment of financial management arrangement at the CFCU including staffing, project accounting and financial reporting systems, internal controls, flow of funds mechanism and auditing arrangements for implementation of the proposed project were reviewed during project preparation. The organizational structure of CFCU comprising of three sub-units each headed by a director i.e. finance, procurement, monitoring and evaluation facilitates coordinated and efficient management and implementation of project activities. Three financial staff (finance director and two financial officers who report to general director) are experienced in implementing Bank projects and other donors' operations. The existing Alpha (PMR) accounting and financial reporting system is considered adequate for maintaining and posting accounting records, and for automatically generating interim and annual financial statements. Accounting and administrative systems and controls are documented in an operational manual that is updated as needed.



51. With respect to flow of funds, Country Financing Parameters (CFP) for Albania have been approved by the Bank, allowing for 100 percent financing of eligible project expenditures, including taxes and duties. Donors Designated Accounts would be maintained at the Bank of Albania, as is the current procedures for all Bank and donor funded projects, to facilitate payments of project expenditures through sub-accounts. Counterpart funds financed from the national budget, if allocated to finance project expenditures, would be secured through preparation of annual budget of the spending unit, in this case Ministry of Finance, channeled through the treasury account. The project financial statements would be audited by independent auditors contracted by the MoF under the existing 'global' audit arrangements, where the MoF annually appoints auditors for the entire portfolio of Bank funded projects.

52. The conclusion derived from the assessment is that the existing financial management arrangements, systems and controls at the CFCU are considered adequate for project implementation and meet Bank requirements. Overall financial management risk level is assessed as 'Moderate'. The risk would be reduced to "Low" level after mitigation measures, as outlined in Annex 5 'Financial Management and Disbursement Arrangements'.

#### *b) Procurement*

53. The 2006 Bank's Country Fiduciary Assessment (CFA) for Albania assessed the risk for conducting public procurement as significant. Albania's ranking in international country surveys on perceptions and control of corruption suggests that the fiduciary risk associated with corruption is high. The 2006 CFA report provides key recommendations and an action plan for the Government and other relevant stakeholders for mitigating the fiduciary risk.

54. The overall implementation of the project will be carried out by the already existing Central Finance and Contracting Unit at the MoF. The project team will conduct and manage project procurement, in close cooperation with the relevant departments of the MoF and the relevant beneficiaries involved in the project. When there is no in-house capacity for development and preparation of terms of references and technical specifications, consultants will be engaged under the proposed project to assist with that.

55. Procurement for the project will be carried out in accordance with the World Bank's "Guidelines: Procurement under IBRD Loans and IDA Credits" published May 2004 and revised in October 2006 (Procurement Guidelines); and "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" published May 2004 and revised in October 2006 (Consultant Guidelines) and the provisions stipulated in the Grant Agreement. The overall risk for the project after mitigation is rated "substantial". Annex 8 provides details on the risks associated with procurement, the mitigation measures, the initial procurement plan and the relevant procurement arrangements for the project.

#### ***D. Social***

56. The project has a broader political impact for the ability of Albania to undertake the necessary reforms in order to get on the EU accession path. Also, the main social benefits will be realized through improved transparency of corporate sector, leading to improved business environment and access to finance. This in turn will generate development through more investments and jobs generation in the country.

57. The key stakeholders were engaged into the project preparation process through NSC specifically created by the Government authorities to oversee and coordinate the reforms in corporate

financial reporting. Each stakeholder institution is engaged through representation in the NSC and has a specific role to play in the reform. The MoF intends to re-convene the NSC and consider an option of its wider membership, so that all the stakeholders that have a role to play in corporate financial reporting reform are involved. There are no specific social issues to be addressed in this project, such as distributional issues, conflicting demands on the same resources, or adequacy of targeting and delivery mechanisms.

#### ***F. Environment***

58. This is the C category project; hence it is not subject to environmental impact assessment.

#### ***G. Safeguard policies***

59. The project raises no safeguards issues.

<b>Safeguard Policies Triggered by the Project</b>	<b>Yes</b>	<b>No</b>
<u>Environmental Assessment</u> ( <a href="#">OP/BP 4.01</a> )	[ ]	[X ]
Natural Habitats ( <a href="#">OP/BP 4.04</a> )	[ ]	[X ]
Pest Management ( <a href="#">OP 4.09</a> )	[ ]	[X ]
Physical Cultural Resources ( <a href="#">OP/BP 4.11</a> )	[ ]	[X ]
Involuntary Resettlement ( <a href="#">OP/BP 4.12</a> )	[ ]	[ X ]
Indigenous Peoples ( <a href="#">OP/BP 4.10</a> )	[ ]	[X ]
Forests ( <a href="#">OP/BP 4.36</a> )	[ ]	[X ]
Safety of Dams ( <a href="#">OP/BP 4.37</a> )	[ ]	[ X ]
Projects in Disputed Areas ( <a href="#">OP/BP 7.60</a> )*	[ ]	[X ]
Projects on International Waterways ( <a href="#">OP/BP 7.50</a> )	[ ]	[ X ]

#### ***H. Policy Exceptions and Readiness***

60. There are no exceptions required from Bank policies.

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\* By supporting the proposed project, the Bank does not intend to prejudice the final determination of the parties' claims on the disputed areas

## Annex 1–Results Matrix

### Results Framework

PDO	Project Outcome Indicators	Use of Project Outcome Information
Create a transparent policy environment and effective institutional framework for corporate financial reporting in line with best international practices, aligned with EU <i>acquis communautaire</i> , specifically:		YR1-3: Measure progress in implementation of reforms (CAP)  YR1-2:
(1) Improve legitimacy of the legal framework in the area of corporate financial reporting by aligning it with the EU <i>acquis communautaire</i>	Indicator (1) The roadmap for further alignment of the legislation with the EU <i>acquis communautaire</i> is approved by the Government to underpin implementation of the next phase of the reforms	Inform the EU partners and key stakeholders about the Government’s commitment and steps towards the full alignment of the legislation with the EU requirements
(2) Strengthen standard setting by the National Accounting Council (NAC)	Indicator (2) The NAC aligns the core NAS with EU requirements or adopts IFRS for SMEs	YR2-3: Ensure sustainability of the reform process in terms of prioritizing and sequencing of activities and planning of the use of EU IPA resources
(3) Improve standard setting and supervision of auditing practices by the Audit Oversight Body and IEKA	Indicator (3) Number of satisfactory audit quality inspection reports prepared and follow-up decisions duly taken	Determine whether the national law requirements to use high quality financial reporting standards could be applied by preparers of financial information, auditors, and education institutions
(4) Improve skills for compliance with new professional standards through revisions and updates of accounting and auditing curricula for university education and professional certification	Indicator (4) Accounting and auditing curricula and certification standards satisfy IES	YR3: Determine if the prerequisites for further development of auditing oversight system are in place  Determine if CAP needs adjustments and prioritize activities for the implementation of the next phase of reforms
(5) Improve management of reforms in corporate financial reporting by the National Steering Committee and the MoF	Indicator (5) The MoF successfully manages implementation of the reforms	

Intermediate Outcomes	Intermediate Outcome Indicators	Use of Intermediate Outcome Monitoring
Component 1:		
<p>Completed analysis of the existing legislation in the area of corporate financial reporting, its cohesiveness with other company related laws, and assessment of the degree of compliance with the EU <i>acquis communautaire</i></p> <p>Increased awareness of the key policy makers and stakeholders on the EU <i>acquis communautaire</i> for further improvement of legislation</p> <p>Improve consensus of key decision makers on actions to include in the roadmap for improvement and alignment of the national legislation on corporate reporting with the EU <i>acquis communautaire</i></p>	<p>Comprehensive concordance table for the accounting and auditing legislation prepared</p> <p>Participant policy makers and stakeholders expressed better understanding of how local legislation needs to be modified to reflect the requirements of the EU <i>acquis communautaire</i></p> <p>Members of NSC and the MoF, relevant Parliamentary committee and other actors responsible for legislation adoption in Albania reached agreement about organizational arrangements, change management requirements and the implementation time table for the roadmap</p>	<p>YR1-YR3 : Low levels may flag either poor training programs and workshops or insufficient client ownership of developed recommendations</p>
Component 2:		
<p>Improved consensus on the approach for development of accounting standards for SMEs in Albania</p>	<p>Members of the NAC and the MoF agree to the approach for further development of accounting standards for SMEs or eventual adoption of IFRS for SMEs</p>	<p>YR1-2: Will inform development of accounting standards for SMEs in Albania</p>
Component 3:		
<p>Systems and processes to ensure auditors' compliance with professional standards (ISAs and Code of Ethics) established</p> <p>Raised awareness of the auditors about the new oversight system</p>	<p>Secondary legislation for audit oversight prepared. Improved knowledge of the Audit Oversight Body's and IEKA's staff of tools, manuals, procedures, methodologies and templates for external quality assurance of professional standards</p> <p>Improved understanding by auditors of the requirements of new oversight system</p>	<p>YR1-2: Will inform development of policy on oversight</p> <p>YR3: Flags possible payoffs or other problems in compliance by auditors with professional standards</p>
Component 4:		
<p>Formulated plans to develop new accounting and auditing certification and education curricula in professional certification bodies and universities</p>	<p>Staff of beneficiary professional associations (IEKA, IKM, SHKFSH, KKK) and universities (University of Tirana, University of Agriculture ) developed proposals for new core curricula based on IES, IFRS and ISAs for their organizations</p>	<p>YR1-YR2: Low levels may flag either poor activity design or lack of incentives to develop new curricula</p>
Component 5:		
<p>Operational plan for the second phase of the reform prepared</p>	<p>The next phase of the reform is finalized by the MoF RIG and endorsed by NSC, including results framework</p>	<p>YR3: Feeds into broader reform</p>

Institutional Outcome Indicators	Baseline	Milestones			Data Collection and Reporting		Responsibility for Data Collection
		YR1	YR2	YR3	Frequency and Reports	Data Collection Instruments	
Indicator (1)							
Roadmap for further alignment of the legislation with the EU <i>acquis communautaire</i> approved by the Government to underpin implementation of the next phase of the reforms	Statutory framework recently updated, but no comprehensive basis for its full alignment with the EU <i>acquis communautaire</i> corporate financial reporting legislation	A comprehensive concordance table for the accounting and auditing legislation is prepared	Proposed roadmap for alignment of legislation with <i>acquis communautaire</i> is endorsed by key stakeholders	Draft proposal for the legislation approved by the MoF	Annual project progress report  Bank A&A ROSC	Annual report prepared by the MoF reform implementation group  A&A ROSC at the end of the project to validate results	MoF reform implementation group  Bank for the ROSC
Indicator (2)							
The NAC aligns the core NAS with EU requirements or adopts IFRS for SMEs	NAC does not have a clear vision of further financial reporting standards for SMEs development	-Skills enhanced for NAC members and staff in IFRS and IFRS for SMEs	Members of the NAC and the MoF agreed to the approach for further development of accounting standards for SMEs or eventual adoption of IFRS for SMEs	Draft of core NAS or IFRS for SMEs translated by NAC and adopted by MoF	Annual project progress report  Bank A&A ROSC	Annual report prepared by the MoF  A&A ROSC	MoF reform implementation group  Bank for the ROSC
Indicator (3)							
Number of satisfactory audit quality inspection reports prepared and follow-up decisions duly taken	No audit quality inspections are currently performed	Requirements for audits and inspections published and disseminated	At least 5 pilot audit quality inspections performed and their reports state the follow-up decisions	At least 15 audit quality inspections performed and their reports state the follow-up decisions	Annual project progress report  Bank A&A ROSC	Annual report prepared by the MoF  A&A ROSC	MoF reform implementation group  Bank for the ROSC

Indicator (4)							
Accounting and auditing curricula and certification standards satisfy international requirements	The university and professional certification curricula is not compliant with IFAC IES	The task force for beneficiary professional associations and universities is set-up and they agreed on the objectives and scope of TA for curricula development	Core curricula and pilot training materials developed	New curricula adopted by at least two professional associations and 2 universities	Annual project progress report  Bank A&A ROSC	Annual report prepared by the MoF  A&A ROSC	MoF reform implementation group  Bank for the ROSC
Indicator (5)							
The MoF successfully manages implementation of the reforms	The MoF's capacity to plan, coordinate and manage implementation of the reforms is limited	Annual work and procurement plan for project implementation prepared by RIG	Procurement plan updated on a regular basis for project implementation by RIG	Project proposal for national IPA is submitted by MoF	Annual project progress report	Annual report prepared by the MoF	MoF' reform implementation group

Intermediate Outcome Indicators	Agent of Change	Data Collection and Reporting		
		Reports	Data Collection Instruments and frequency	Responsibility for Data Collection
Component 1				
Comprehensive concordance table for the accounting and auditing legislation prepared	MoF and NCS members	Consultant report submitted to RIG and NSC, and written feedback provided	Information from the RIG included in the project progress report	MoF
Participant policy makers and stakeholders expressed better understanding of how local legislation needs to be modified to reflect the requirements of the <i>EU acquis communautaire</i>	MoF NCS members, Parliamentary Committee on Budget and Finance, other local decision makers	Evaluations/feedback from participants following each event/workshop	Information from the RIG included in the project progress report	MoF
Improve consensus of key decision makers on actions to include in the roadmap for improvement and alignment of the national legislation on corporate reporting with the <i>EU acquis communautaire</i>	MoF NCS members, Parliamentary Committee on Budget and Finance, other local decision makers	Agreement reached among key decision makers on actions to include in the roadmap	Roadmap incorporates actions agreed to by key decision makers, information included in the project progress report	MoF
Component 2				
Members of the NAC and the MoF agree to the approach for further development of accounting standards for SMEs or eventual adoption of IFRS for SMEs	MoF NAC members	Agreement reached among key decision makers on SMEs financial reporting standards	The NAC document on approach on SMEs financial reporting standards reflects the consensus among stakeholders involved	NAC
Component 3				
Secondary legislation for audit oversight prepared.	Staff of the Audit Oversight Body and IEKA	Draft Secondary legislation is submitted by IEKA and Public oversight board to the MoF	Information from the MoF, reflected in the project progress report	Public oversight board and IEKA
Improved knowledge of the Audit Oversight Body's and IEKA's staff of tools, manuals, procedures, methodologies and templates for external quality assurance of professional standards	Staff of the Audit Oversight Body and IEKA	Tools, procedures and manuals developed; feedback by IEKA and Public Oversight board on readiness for application	Information from the Public Oversight board and IEKA, reflected in the project progress report	Audit oversight body and IEKA
Improved understanding by auditors of the requirements of new oversight system	Auditors community	% of auditors who report improved understanding of the requirements of new oversight system	Survey by IEKA once a year	IEKA

Component 4				
Staff of beneficiary professional associations (IEKA, IKM, SHKFESH, KKK) and universities (University of Tirana, University of Agriculture ) developed proposals for new core curricula based on IES, IFRS and ISAs for their organizations	Core universities and professional associations; and MoF	Agreement reached among beneficiary institutions on the curricula and subsequently adopted based on consultant's proposal	Level of consensus measured as number of agreeing participants, reflected in regular project reports	MoF and IEKA
Component 5				
The next phase of the reform is finalized by the MoF RIG and endorsed by NSC, including results framework	MoF and NSC	IPA project proposal prepared and submitted	Annual project reports starting from 2012	MoF



## **Annex 2– Project Description**

1. The proposed project comprises five components: (i) Improving the legal framework in the area of corporate financial reporting; (ii) Strengthening the Capacity of the National Accounting Council; (iii) Establishment of an Audit Oversight System; (iv) Improving accounting and auditing curricula for university education and professional certification; (v) Project management, strengthening reform capacity, and monitoring and evaluation.

### **Component 1. Improving the legal framework in the area of corporate financial reporting (Estimated cost EUR XXX)**

2. Component 1 has two main activities: (i) Review of the legislation and assessment of the progress achieved in compliance with EU *acquis communautaire*; (ii) Increasing awareness of the key policy makers and stakeholders on the EU *acquis communautaire* for further improvement of legislation.

3. *Review of the legislation and assessment of the progress achieved in compliance with the EU acquis communautaire.* The need for this activity is based on the 2006 A&A ROSC findings and it is included in the CAP adopted by the Government of Albania. This activity will provide technical assistance to perform an analysis of the existing legislation in the area of corporate financial reporting, its cohesiveness with other company related laws, and assessment of the degree of compliance with the EU *acquis communautaire* through preparation of a comprehensive concordance table for the accounting and auditing legislation. The results of this assessment will be transformed into a time-bound roadmap for the full alignment of accounting and auditing legislation with the requirements of the EU *acquis communautaire*. The relevant part of the EU legislation consists of Directives 4, 7, and 8, as particularly relevant to the establishment of a robust financial reporting framework.

4. The activity will finance technical assistance up to 4 months. The expected outputs will be (i) a concordance table on compliance with the EU *acquis communautaire*; and (ii) proposals for the improvement and alignment of the national relevant legislation with the EU *acquis communautaire* – a time-bound roadmap taking into account the degree of compliance and realistic estimates of the required timing given particularities of the legislation process in Albania. The major risk of this activity is that the major stakeholder may not agree to the proposed roadmap. This risk will be mitigated through further raising the awareness of key decision makers, such as the members of NSC and the MoF, relevant Parliamentary committee and other actors responsible for legislation adoption in Albania.

5. *Increasing awareness of the key policy makers and stakeholders on the EU acquis communautaire for further improvement of legislation.* The need for this activity is based on the fact that the relevant stakeholders in Albania need to get a better understanding of the implications of full alignment with the European legislation and to ensure sound technical knowledge of decision makers as to what institutional arrangements should be strengthened and what change management will be required over a realistic time table for the Albanian environment, taking into account the experience of other countries of the similar size and the level of institutional and individual capacity development.. The activity, through training and workshops, will aim to create an enabling environment for the adoption of a time-bound roadmap for full legislation alignment in the foreseeable future, as well as draft of new legislation to be adopted during the next reform phases.

6. This activity should be realized in 2-3 months following the completion of the analysis of legislation. The outputs will aim at agreeing and adopting the roadmap for corporate financial reporting legislation alignment with EU *acquis communautaire*.

### **Component 2. Strengthening the Capacity of the National Accounting Council (Estimated cost EUR XXX)**

7. This component 2 has two activities: (i) enhancing standard setting process and improving the content of accounting standards for SMEs; and (ii) creating a sustainable mechanism for IFRS adoption, translation updates, as part of the process of endorsing IFRS for use in Albania.

8. *Technical assistance to enhance the standard setting process through improving its transparency and broader participation of stakeholders.* Although the A&A ROSC recommended that the accounting standards setting should become sustainable, as of today this is still not the case. The activity will support improvements in the standards setting process through technical assistance for establishing regulations and mechanisms and training of the members of the NAC to: (i) enhance transparency in the standards setting process through the involvement of a broader range of stakeholders and consultations; (ii) define the approach for further development of accounting standards for SMEs or eventual adoption of IFRS for SMEs; depending on the approach taken – the project will help with either adoption and translation of IFRSs for SMEs or with strengthening capacity to develop NAS; this activity will also include a survey to assess whether IFRS for SMEs would be a relevant tool for in-country stakeholders.

9. The timescale for this activity is 12 months. The expected outcomes are: (i) a transparent accounting standards setting or adoption process, established through appropriate regulations/bylaws; and (ii) adequate sustainable funding is secured for NAC activity.

10. *Creating sustainable mechanism for IFRS adoption, translation updates, as part of the process of endorsing IFRS for use in Albania.* This activity is based on A&A ROSC recommendations and is included in the CAP. It will provide technical support to enhance NAC understanding of IFRS, particularly the most recent changes; and technical assistance to enhance the translation process and publication of updated translation of IFRS.

11. The timescale of this activity is 12 months and the output is a sustainable mechanism to secure regular updates and publication.

### **Component 3. Establishment of an Audit Oversight System (Estimated cost EUR XXX)**

12. Component 3 has three activities: (i) drafting the bylaws and regulations for public oversight system and the development of public register for auditors; (ii) improving auditing standards setting; and (iii) creation of tools and methodologies for auditing quality assurance system.

13. *Drafting bylaws and regulations for public oversight system and development of public register for auditors.* The need for this activity is based on the requirements of the 2009 auditing law. It will provide TA and workshops for drafting the secondary legislation for audit oversight based on the 2009 audit law. It will also finance small equipment and software to establish the public register of auditors.

14. The timescale of this activity is up to 12 months, the main outputs being bylaws and regulations and the public register of auditors. The beneficiary is the Audit oversight body (recently established according to the new Auditing Law) and IEKA, which, according to the new audit law, is assigned the role of Chamber of Auditors in the public oversight system.

15. *Improving auditing standards setting.* The need for this activity is based on the ROSC A&A, CAP and will entail establishing a sustainable auditing standard-setting process, ensuring the translation of ISAs compliant with IFAC translation policies and developing relevant audit practices, as well as securing sustainable mechanisms, technical expertise and funding to ensure that ISA are translated, adopted and published in a timely manner. The assistance will include TA and equipment & software for supporting the translation process. The beneficiary of this activity is IEKA.

16. The timescale for this activity is up to 12 months and the key output is publication of new ISAs translation and a sustainable mechanism for auditing standards adoption.

17. *Creation of tools and methodologies for auditing quality assurance system.* This activity will provide technical assistance, equipment and software, and training to develop appropriate tools, manuals, procedures and templates for external quality assurance, including the tools needed for field inspections, such as methodologies and templates. The activity will also aim to inform auditors about the oversight system and raise their awareness.

18. The timescale of this activity is up to 18 months and the outputs include: tools, manuals and templates developed, equipment and software ready to use. The risk related to this activity is that adequate staff will not be available on the market to perform quality assurance function. This risk will be mitigated through appropriate training and building an in-house capacity at IEKA and the Public Oversight Board.

#### **Component 4. Improving accounting and auditing curricula for university education and professional certification (estimated cost EUR XXX)**

19. Component 4 will include one activity: Development of core accounting and auditing curricula and basic training materials for accountancy education and raise awareness among stakeholders for consensus building needed for its adoption.

20. *Development of core accounting and auditing curricula and of basic training materials for accountancy education.* This component activity will help universities, professional bodies and the examination center (to be created under the MoF) to build the foundations for sustainable curricula for accounting and auditing education and certification. The activity will include: (i) technical assistance to develop the core accounting and auditing curricula for professional certification and university education; (ii) technical assistance to assist with the development of the core training materials, manuals and case studies to support the education process. The activity will build on the results of regional activities in this area carried out under the Regional REPARIS Program, whereby common solutions are developed and proposed to participating countries. The activity will also fund the raising awareness workshops.

21. The timescale for this activity is up to 12 months. The beneficiaries are professional associations and the leading university in the area of accountancy education. The outputs include the core curricula supported by training materials available for use by professional associations and universities in Albania. The curricula developed will be based on IFRS and ISAs.

#### **Component 5. Project management, strengthening reform capacity, and monitoring and evaluation (Estimated cost EUR XXX)**

22. The component 5 will include the following activities: (i) project management; (ii) strengthening reform capacity and monitoring and evaluation.

23. *Project management.* This activity will provide for incremental operating costs needed for the project management, and technical assistance (local and international) to assist the MoF in day-to-day project implementation (one local project management consultant full time, and international strategic consultant available for short regular visits and online support on technical issues).

24. *Strengthening reform capacity and monitoring and evaluation.* This activity will provide technical assistance to the MoF on planning further reforms beyond this project and securing domestic or international funding for next phases of reforms, and ensuring monitoring and evaluation of results framework of this project.

### Project Activities Implementation Tables

Components/Sub-components	Activities	Category/Co st EUR 000'	Timing	Output	Responsibility	Target group	Intermediary Outcome indicators	Risks
<b>Total cost</b>		1,250 (taking into account TF fee for the WB)						
<b>Component 1. Improving the legal framework in the area of corporate financial reporting</b>							The road map for the further alignment of the legislation with the EU <i>acquis communautaire</i> is prepared, endorsed by NSC and approved by the Government	
<b>Review of the legislation and assessment of the progress achieved in compliance with EU <i>acquis communautaire</i></b>	(i) reviewing the existing laws; (ii) preparing a gap analysis and proposals for a time-bound roadmap for the further alignment of national legislation with the <i>acquis communautaire</i> .	Consulting services (i)	09/2010 - 12/2010	(i) a concordance table on compliance with the <i>acquis communautaire</i> ; and (ii) proposals for improvement and alignment of legislation with EU <i>acquis communautaire</i> – a time-bound roadmap.	MoF	MoF NSC members Parliamentary committee on budget and finance Other decision makers		The stakeholders do not agree with the roadmap proposed
<b>Increasing awareness of the key policy makers and stakeholders on the EU <i>acquis communautaire</i> for further improvement of legislation</b>	(i) training and workshops on <i>acquis communautaire</i> . (ii) informing national decision making processes about good practices in countries of similar size and conditions.	Training/workshops (i)	01/2011 - 03/2011	(i) Agreed roadmap of legislation alignment  (ii) Draft legislation	MoF	MoF NSC members Parliamentary committee on budget and finance Other decision makers		Low stakeholder participation during the workshops

Components/Sub-components	Activities	Category/Co st EUR 000'	Timing	Output	Responsibility	Target group	Intermediary Outcome indicators	Risks
<b>Component 2. Strengthening the capacity of the National Accounting Council</b>		300						
<b>Enhancing standard setting process and improving the content of accounting standards for SMEs</b>	(i) TA to strengthen the standard setting process; (ii) TA and training for setting accounting standards for SMEs (i.e. non-public-interest entities).	Cons. Serv and study tours (i)	12/2010 - 12/2011	(iii) Transparent standard setting process, core standards are updated to comply with the EU requirements	MoF NAC	NAC members		The agreement is not reached on NAS or IFRS for SMEs;
<b>Creating a sustainable mechanism for IFRS adoption, translation updates, as part of the process of endorsing IFRS for use in Albania</b>	Assistance on establishment of an institutionalized translation process o ensure that high-quality translations of IFRS are kept up-to-date on a sustainable basis.	Cons. Serv. ; Equipment	12/2010 - 12/2011	(iv) NAC members trained in IFRS updates; IFRS published and sustainable mechanism in place for regular updates;	MoF NAC	NAC members	IFRS translation updated regularly and publicly available in the local language	
<b>Component 3. Establishment of an Audit Oversight System</b>								
<b>Drafting the bylaws and regulations for public oversight system and the development of public register for auditors</b>	TA and Training for Drafting the secondary legislation for the functioning of a public audit oversight system & development of public registry of auditors.	Cons. Services/train ing  Equipment & software	01/2011 - 12/2011	By-laws and regulations are drafted and public awareness is raised with a view to informing the decision makers in preparation of adopting them in due course.  Public registry developed	Audit oversight body IEKA	Auditors community	The auditing oversight institutions have in place systems and processes to ensure auditors' compliance with regulatory standards, and these are	Bylaws and regulations are not adopted

Components/Sub-components	Activities	Category/Co st EUR 000'	Timing	Output	Responsibility	Target group	Intermediary Outcome indicators	Risks
							adequately communicated to auditors	
<b>Improving auditing standards setting</b>	Improving the auditing standard setting process through translation and adoption mechanisms for ISAs.	Cons. Serv. ; Equipment	01/2011 - 01/2012	An auditing standards translation/adoption mechanism is in place and trainers trained;	Audit oversight body IEKA	Auditors community	ISA translation updated at least once a year and publicly available in the local language	The system may be not sustainable due to lack of funding
<b>Creation of tools and methodologies for auditing quality assurance system</b>	TA and Training for creation of methodologies and tools for national audit quality assurance system.	Cons. Serv./training ; Equipment and software	06/2011 - 12/2012	(i) the adoption of quality assurance tools, such as manuals, methodologies and templates; and (ii) training of the staff dealing with quality assurance, including on-the-job training during audit quality inspections	Audit oversight body IEKA	Auditors community	Number of satisfactory audit quality inspection reports prepared and follow-up decisions duly taken	Adequate staff for QA is not available
<b>Component 4. Improving accounting and auditing curricula for professional certification and university education</b>							The core education curricula updated in line with IFRS and ISA	
	Development of core accounting and auditing curricula and basic training materials for accountancy education	Cons. Serv and workshops ;	01/2012 - 04/2013	(i) the core accounting and auditing curricula developed; and (ii) Training materials, manuals and case studies for pilot courses developed and available for use by universities and professional bodies; and training of trainers	Professional associations and one leading university	Core professional associations and universities ; and Ministry of Finance; NAC		The basis for A&A curricula is not adopted at the national level

Components/Sub-components	Activities	Category/Co st EUR 000'	Timing	Output	Responsibility	Target group	Intermediary Outcome indicators	Risks
<b>Component 5. Project management, strengthening reform capacity, and monitoring and evaluation</b>							The reform unit in the MoF has designed the second phase of the reform ready to be operational	
	Incremental operating costs related to project management, including overall reform management and coordination, and fiduciary activities. TA for Monitoring and reform momentum, capacity building for project management	Incremental operating costs/equipment and cons. Services ;	07/2010 - 06/2013	(i) day-to day project activities , and managed during implementation and completion; (ii) the second phase of the project is prepared.	MoF and its contracting unit	MoF and NSC		

### Annex 3: Project Costs

#### ALBANIA: CORPORATE FINANCIAL REPORTING ENHANCEMENT PROJECT

Project Cost By Component	EUR million	Total EUR million	% of Total Costs
1. Improving the legal framework			
2. Strengthening the capacity of NAC			
3. Establishing of Auditing oversight system			
4. Improving accounting and auditing curricula			
5. Project management and reform capacity			
<b>Total Project Costs</b>	<b>1.75</b>	<b>1.75</b>	<b>100</b>

**Financing Plan (EUR million)**  
(including contingencies)

<u>Component/Activity</u>	SECO	Gov. Albania	Total
1. Improving the legal framework			
2. Strengthening the capacity of NAC			
3. Establishing of Auditing oversight system			
4. Improving accounting and auditing curricula			
5. Project management and reform capacity			
<b>Total Financing Required</b>	<b><u>1.25</u></b>	<b>[0.2]</b>	<b><u>1.45</u></b>



## **Annex 4–Implementation Arrangements**

*The responsibility for the project implementation* will be with key stakeholders, project coordination and day-to-day project management with the MoF, while the NSC will have an overall oversight role. The Deputy Minister of Finance, in his capacity as responsible for financial reporting reforms in Albania and a Chair of the NSC, will be accountable for progress in project implementation.

*Day-to-day project management and coordination.* The MoF will set up a reform implementation group, as set out in the 2009 CAP, which will include qualified MoF staff for the day-to-day work on project implementation. The project will include the provision of both technical and financial resources to strengthen the reform implementation capacity of the reform implementation group, which will be materialized in one local consultant/coordinator and one international strategic advisor under the TORs agreed upon with the World Bank project team and reporting to the reform implementation group and the Deputy Minister of Finance.

*Fiduciary aspects in project management,* including procurement and financial management, will be handled by the Central Finance and Contracting Unit (CFCU) at the MoF, primarily responsible for implementation of the EU IPA funds. CFCU is also responsible for managing fiduciary aspects of the existing Integrated Planning System Multi-Donor Trust Fund (P105143, TF90843-recipient-executed and World Bank administered); the unit has an adequate financial management and procurement capacity to manage an additional donor trust fund. The fiduciary arrangements will be further assessed and confirmed during the project appraisal. The EU is currently financing the provision of technical assistance to strengthen the unit's capacity for implementation of EU IPA funds. For the purpose of this project, the unit will report to the reform implementation group and Deputy Minister. The CFCU will have the overall responsibility on fiduciary aspects of the project, including:

- Project planning and budgeting
- Financial management -project accounting, financial reporting, Grant/Government counterpart funds disbursement
- Auditing arrangements
- Procurement and contracting

The MoF reform implementation group will be responsible for:

- Monitoring and evaluation of all project activities and indicators for project implementation;
- Review and approve consultants' reports (within a month after the reports' submission);
- Coordination what – not project activities, but be specific what they coordinate -- with project beneficiaries, the NSC , the World Bank and other donors;
- Reporting on project and reform implementation progress to the Minister and Deputy Minister of Finance, the World Bank and the donors.

*National Steering Committee.* The NSC is established for oversight and coordination of the reforms in area of corporate financial reporting. Initially it was headed by Deputy Minister of Finance. The MoF intends to re-convene the NSC and consider an option of its wider membership, so that all the stakeholders that have a role to play in corporate financial reporting reform are involved. The NSC is made up by a multi-disciplinary group of public and private sector stakeholders with an interest and responsibilities in area of corporate financial reporting. It includes representatives from the government, financial sector regulators, the accountancy profession, academia, commercial banks, insurance companies and large and medium

enterprises. The NSC was created for the purpose of development CAP and overseeing its implementation. The role of the NSC will be to make decisions on key legal and regulatory issues affecting project implementation, and to approve annual work plans and budgets. NSC will convene meetings at quarterly basis to guide and steer the project implementation staff and other stakeholders. NSC will review and approve the yearly project implementation plans, reflecting clear objectives, priorities, milestones, key project activities with their indicators and deadline, which is prepared by the project manager in consultation with other stakeholders.

In particular, the NSC will be responsible for:

- Perform overall oversight of the project implementation
- Review and approve the project's annual work plans and budgets
- Propose strategic reform decisions for the relevant stakeholders
- Facilitate proposed amendments and changes to the legislation framework addressed within the project
- Issue quarterly press releases for public on project's progress

*Readiness for implementation.* While the Government lacks the specific capacity to implement reforms in accounting, auditing and financial management, they have shown a strong commitment to the project and its objectives. The Government recognizes the need for such a project to address the critical need for accountants in the corporate sector and for the long-term training of accounting and auditing professionals. The project will build on the existing capacity in the country and will leverage the enthusiasm of the Government and of the private sector to drive the reform for long-term sustainability.

The Government is ready to appoint the head of the reform group and to agree with the Bank on the procurement plan for the first 18 months at the time of project appraisal.

**Annex 5: Financial Management and Disbursement Arrangements**  
**ALBANIA: Corporate Financial Reporting Enhancement Project (CFREP)**

**A. Financial Management Arrangements**

1. **Executive Summary and Conclusion.** An assessment of financial management arrangements for implementation of the proposed CFREP was carried out during project preparation. The objective of the assessment was to review the adequacy of financial management systems and controls in place at the CFCU within the Ministry of Finance which would be responsible for overall financial management arrangements for project implementation. The systems reviewed included budgeting and funds flow, project accounting, financial reporting, internal controls, staffing and auditing arrangements as outlined in this Annex. The organizational structure of CFCU as outlined in Table 3 of this Annex comprises of general director and three directors responsible for financial management, procurement and monitoring and evaluation. The financial management staff (finance director and two finance officers) are experienced in implementing Bank/donor funded projects and operations having implemented three other Bank/donor funded operations i.e. the Public Administration Reform Project, the PHRD Grant for the preparation of DPL II and the Multi Donor Grant for Capacity Building for Poverty Reduction Strategy. The existing Alpha (PMR) accounting and financial reporting system is capable of maintaining and processing accounting records and accounts, and automatically generating interim and annual financial statements. Accounting and administrative systems and controls are documented in an operational manual which is updated as needed. With respect to flow of funds, donors' Designated Accounts are maintained at the Bank of Albania, with sub-accounts also opened to facilitate payments of project expenditures. The project financial statements would be audited by independent auditors under the existing 'global' audit arrangements coordinated by the Ministry of Finance, and under terms of reference cleared by the Bank. Conclusion derived is that the existing financial management arrangements, systems and controls are considered adequate and they meet Bank requirements. *Overall financial management risk level is assessed as 'Moderate', but reduced to low level after mitigation measures.*
2. **Country Issues.** The Accounting and Auditing Report on Observance of Standards and Codes (ROSC) carried out in 2006 identified shortcomings in accounting and financial reporting frameworks in the corporate sector. Lack of cohesiveness in the legal framework and weak institutional and professional capacity deterred preparation of high quality financial information for public interest entities on which users could make informed economic decisions. The audit framework although in line with the EU 8<sup>th</sup> Directive was not credible for users to place reliance on the audit opinion issued by local auditors. Recent developments include development of a new Law on Accounting and Auditing and adoption of a Country Action Plan for further enhance transparency and accountability in financial reporting in the corporate sector. The Law on the Management of the Budgetary System in Albania was passed by the National Assembly in 2008, setting a process for preparation, analysis and approval of the annual State Budget that is set firmly within a medium-term planning framework, with strong performance orientation. Corruption perception has declined and governance has been improving in Albania, but the situation is far from satisfactory. The creation in 2007 of a special task force on economic crime and corruption under the authority of the prosecutor, and the establishment of the High Inspectorate for Declaration and Audit of Assets and of the Department for Internal Administrative Control and Anti-Corruption represent a positive step, if these institutions can be made to be more effective.

3. **Planning and Budgeting.** The Budget Systems Law in Albania sets down a process for preparation, analysis and approval of annual State budget that is set firmly within a medium-term planning framework, with a strong performance orientation. The State budget is prepared on cash basis covering all budget spending units, in this case the Ministry of Finance. By July of each year, the CFCU Finance Director in coordination with the Procurement Director would prepare the project budget for the following year based on the procurement plan. After review and approval by the CFCU General Director, the budget would be submitted to the Ministry of Finance for consolidation with the spending unit budget, and for approval. Counterpart funds for financing project expenditures from the State budget would be made available as expenditures are incurred i.e. VAT and local costs.
4. **Project Accounting and Financial Reporting.** The CFCU uses the Alpha PMR software for accounting and financial reporting. The software/system which has security features is capable of multi-currency financial reporting and automatically generates interim financial reports (IFRs) for submission to the Bank and the donors, for project management decision making. This system is used in parallel with the Single Treasury System. Some of the sub-modules of the latter system are however not fully operational for the project to fully rely on the treasury system for accounting and financial reporting for the project. *A financial covenant requiring the project to submit to the IFRs on quarterly basis, and within 45 days after the end of each reporting period will be included in the financing agreement.* The format and content of the IFRs agreed upon.
5. **Internal Controls and Internal Audit.** The CFCU has adequate systems, controls and staffing in place to implement the CFREP. The current organization structure facilitates adequate controls and segregation of duties over the implementation of the project. Financial management, procurement, monitoring and evaluation functions are segregated which facilitates proper segregation of duties and controls over the implementation of the project. Controls, policies and procedures are documented in an Operation Manual available to all project implementing staff. With respect to internal audit, the Ministry of Finance has in place an internal audit department which is benefiting from capacity building funded through EU program.
6. **External Audit.** The current auditing arrangements of auditing all Bank-financed projects' financial statements under a 'global' audit coordinated by the Ministry of Finance will be applied for the audit of the proposed project. The audit of the project's financial statements will be conducted annually by independent auditors selected and contracted by the Ministry of Finance, under terms of reference acceptable to the Bank, and in accordance with International Standards on Auditing (ISA). The first audit for the project will be conducted at the end of the first year of project implementation. The scope of the last audit would cover the last year of project implementation including payments made during the grace period for contracts signed before the closing date. The audit report with accompanying management letter will be submitted to the Bank no later than six months after end of each calendar year audited. *A financial covenant for the annual audit of Project Financial Statements is included in the legal agreement.*
7. **Risk Analysis and Mitigation Strategy.** Consistent with the risk based approach to financial management, due consideration was given during project preparation for the design of anti-corruption and mitigation measures in the project. A summary of the risk assessment for the project is as follows:

8.

**Table 1: Summary Financial Management Risk Rating**

	Comments	FM Risk (at appraisal)	Risk Mitigating Measures	FM Risk (after mitigation)
<b>INHERENT RISK</b>				
1. Country Level Financial Management	<p>The country's fiduciary capacity in managing public funds, and related laws and regulations has improved with donor support. Further strengthening of institutional and capacity building would be required, including operational of the treasury system before the Bank could rely on use of country systems for implementation of the project.</p> <p>Political interference on the budget process.</p> <p>A special task force on economic crime and corruption under the authority of the prosecutor has been created, and the High Inspectorate for Declaration and Audit of Assets, and Department for Internal Administrative Control and Anti-Corruption established to fight corruption in Albania.</p>	S	Implementation of the Country Strategy and Action Plan to support Government reform and institutional capacity building in the area of corporate financial reporting. The proposed CFREP will support implementation of the first phase of the Country Strategy and Action Plan.	M
		S	Continue dialogue with borrower on importance of governance and transparency in financial reporting through strengthening formal oversight institutions and engaging civil society enabling citizens and firms to hold state institutions accountable.	M
2. Entity Level Financial Management	Project to be implemented through the Ministry of Finance	M	Project will maintain organizational structure and staffing satisfactory to the Bank. Any changes to the structure or staff will require Bank agreement	M
3. Project Level Financial Management	Financial management capacity of the CFCU for project implementation and coordination with key project beneficiaries	M	Continued capacity building and training of CFCU staff	L
<b>Overall Inherent Risk</b>		<b>S</b>		<b>M</b>
<b>Control Risk</b>				
4. Budget	Political interference in the budget planning process.	S	The new Budget Law sets down a process for preparation, analysis and approval of the annual state budget that is set firmly within a medium-term planning framework, with a strong performance orientation.	M
5. Accounting	Alpha PMR system is adequate with controls in place to safeguard project assets.	L		L
6. Internal Controls	The CFCU has in place adequate systems and controls in place to safeguard project assets. The policies and procedures are documented in an Operational Manual.	L	.	L
7. Funds Flow	Improved budgeting and planning would minimize delays in provision of counterpart funding, if required.	M	Monitoring timing of release of counterpart funds, and compliance with financial covenants.	L

8. Financial Reporting	Interim Financial Reports for the project	L	Interim Financial Reports (IFRs) will automatically be generated from the Alpha accounting system and submitted to the Bank.	L
9.	PFS will be audited by independent auditors and under TORs acceptable to the Bank	M	Auditors appointed early to minimize delays in completion of the audit and submission of the audit reports to the Bank.	L
<b>Overall Control Risk</b>		<b>M</b>		<b>L</b>
<b>Overall FM Risk</b>		<b>M</b>		<b>L</b>
<i>H = High S = Substantial M = Moderate L = Low</i>				

9. **Overall financial management risk** level for the proposed project is rated as ‘Moderate’, but reduced to ‘Low’ level after mitigation measures.

10. **Strengths and Weaknesses.** Significant strengths that provide basis of reliance on the project financial management systems and controls include experience of the CFCU staff in implementing Bank and other donors’ projects, and having in place adequate accounting systems in place for project implementation. To further strengthen the capacity of the financial management staff, additional training in financial management and disbursements will be provided during the implementation phase of the proposed project.

## B. Flow of Funds and Disbursement Arrangements

11. The total project cost of US\$ 1.75 million will be financed with a single-donor fund funded by SECO. The project funds would finance consulting services, goods, and incremental operating costs.

12. **Methods of Disbursements.** The donor funds would be disbursed on basis of Bank traditional disbursement methods. Based on current disbursement procedures for all Bank operations in Albania, a Designated Account would be opened at the Bank of Albania. As the Bank of Albania does not transfer funds to the consultants and suppliers, the project would open a sub-account to facilitate payments of project expenditures. Other available methods of disbursements are reimbursements, direct payments to third parties and special commitments. The latter method is used for procurement of goods. Country Financing Parameters for Albania have been approved by the Bank, allowing for 100 percent financing of eligible project expenditures, including taxes and duties.

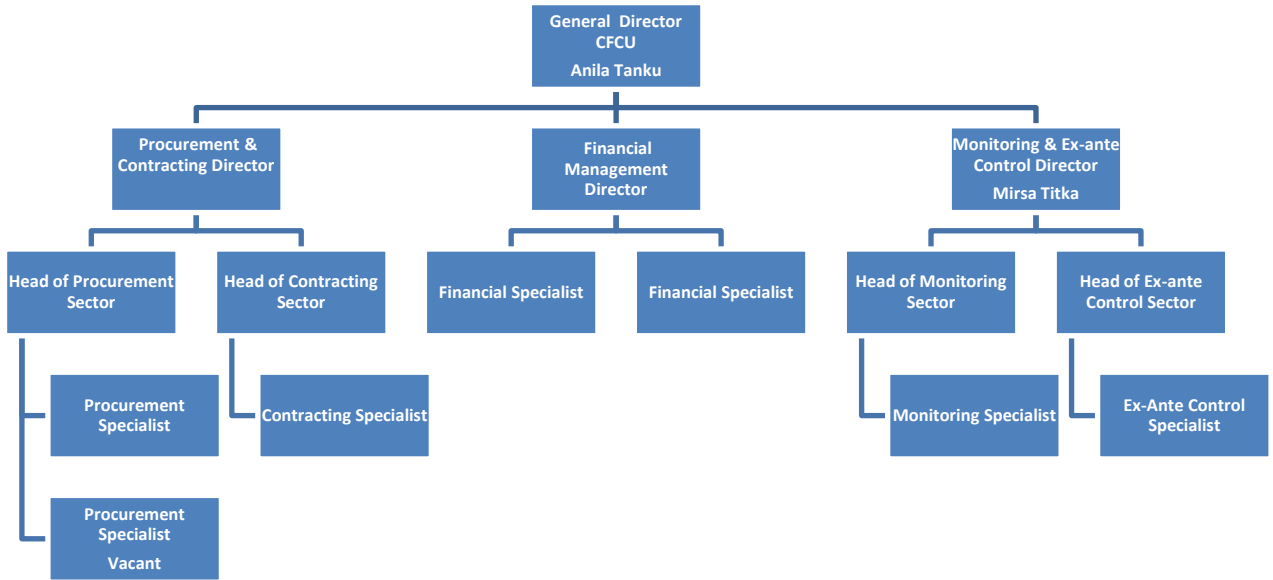
13. **Statements of Expenditures (SOEs).** Disbursements on basis of Statements of Expenditures (SOEs) will be used for contracts valued at less than US\$150,000 equivalent for goods, less than \$50,000 equivalent for consultant services and for all other expenditures/contracts. Payments against contracts above these limits will be fully documented. Full documentation in support of the SOEs will be retained in the CFCU for at least two years after the project closing date. This information will be available for review by Bank missions during project supervisions and by the project auditors. SOEs will be audited in conjunction with the annual audit of the project financial statements.

**Table 2: Allocation of TF Proceeds (to be updated)**

	<b>Expenditure Category</b>	<b>Amount in EUR thousands</b>	<b>Financing Percentage</b>
<b>1</b>	<b>Consultant Services, including training, Goods, Incremental Operating costs</b>	<b>1,250,000</b>	100%
	<b>Total</b>	<b>1,250,000</b>	

13. **Government’s Contribution.** Government counterpart funding to finance project activities would be provided in kind.
14. **Financial Covenants.** The Borrower will be required to maintain a financial management system, including accounts and records sufficient to monitor sources and uses of funds for project implementation. Un-audited interim financial statements will be submitted to the Bank no later than 45 days after end of each quarter. The project financial statements will be audited annually by independent auditors and under terms of reference acceptable to the Bank, and report submitted to the Bank no later than six months after end of such year audited. Financial management covenants were discussed and agreed upon, and included in the legal agreement.
15. **Action Plan.** The existing Alpha PMR system will require minor revisions of the chart of accounts to introduce additional accounting classification for the proposed project’s activities.
16. **Supervision Plan.** The Bank will conduct regular financial management supervisions initially every six months to monitor progress of project implementation, with the supervision frequency decreasing if there are no major issues. The financial management supervision would pay particular attention to: (i) assessment of continued adequacy of overall financial management systems and controls for project implementation; (ii) review of the project’s Interim Financial Reports and audited financial statements; and (iii) review of implementation of auditor’s recommendations on strengthening systems and controls as outlined in the Management Letters issued by the auditors with the annual Audit Reports and operational reviews.

**Table 3: CFCU ORGANIGRAM**





## **Annex 6: Procurement Arrangements**

### **ALBANIA: Corporate Financial Reporting Enhancement Project (CFREP)**

#### **A. General**

Procurement for the CFREP will be carried out in accordance with the World Bank's "Guidelines: Procurement under IBRD Loans and IDA Credits" published May 2004, revised in October 2006, and revised in May 2010 (Procurement Guidelines); and "Guidelines: Selection and Employment of Consultants by World Bank Borrowers" published May 2004, revised in October 2006 and revised in May 2010 (Consultant Guidelines) and the provisions stipulated in the Grant Agreement (GA). The various procurement actions under different expenditure categories are described in general below. For each contract to be financed under the GA, the various consultant selection methods, estimated costs, prior review requirements, and time frame have been agreed between the Borrower and the Bank in the Procurement Plan (PP). The PP will be updated at least annually or as required to reflect the actual project implementation needs and improvements in institutional capacity. A General Procurement Notice (GPN) will be published after the signing of the GA in UNDB on-line and in its printed version as well as in dgMarket online, as well as in the Albanian Official Gazette and on the website of the Ministry of Finance (MOF). Specific Procurement Notices (SPN) will be published for all ICB procurement as the corresponding bidding documents become available, and Consulting contracts estimated to cost Euro 70 000 equivalent and above as the corresponding Request for Proposals (RFPs) become ready and available, in UNDB on-line, in dgMarket, in the Albanian Official Gazette, in at least one widely circulated national daily newspaper or at the website of the MOF. SPN for National Competitive Bidding (NCB) will be published as the corresponding bidding documents become available, and Consulting contracts estimated to cost below Euro 70 000 equivalent as the corresponding Request for Proposals (RFPs) become ready and available, in the Albanian Official Gazette and in at least one widely circulated national daily newspaper or at the website of the MOF.

#### **B. Assessment of the Agency's capacity to implement procurement**

The Bank carried out a Country Fiduciary Assessment (CFA) for Albania and the report was issued in August 2006. Based on the findings of the above referenced report, risk for the general environment in Albania for conducting public procurement is assessed as significant. Albania's ranking in international country surveys on perceptions and control of corruption suggests that the fiduciary risk associated with corruption is high. The CFA report provides key recommendations and an action plan for the Government and other relevant stakeholders for mitigating the fiduciary risk.

The overall implementation of the project will be carried out by the already existing Central Finance and Contracting Unit at the Ministry of Finance in close cooperation with the beneficiaries of the relevant project components. The specific procurement arrangements are detailed in paragraph D below.

#### **C. Procurement risk assessment**

The overall procurement risk is rated **Substantial**. The risks associated with procurement and the mitigation measures were identified in the assessment of Central Finance and Contracting Unit at the Ministry of Finance procurement capacity and are summarized in the table below:

**Table 1: Summary Risk Assessment**

<i>Description of risk</i>	<i>Rating<sup>a</sup> of risk</i>	<i>Mitigation measures</i>	<i>Rating<sup>a</sup> of residual risk</i>
There is no sufficient in-house capacity available for development and preparation of terms of reference, which may lead to delays in initiating the procurement process and in the project implementation.	<b>S</b>	<ul style="list-style-type: none"> <li>(i) Providing training to the beneficiaries, responsible for developing TORs under the relevant project components in</li> <li>(ii) Preparation of the proposal documents for the first two priority contracts by the time of signing of the Grant Agreement;</li> <li>(iii) Hiring a local consultant to coordinate the work of project related activities between the project beneficiaries, Ministry of Finance and CFCU;</li> <li>(iv) Involving/hiring as relevant a foreign strategic adviser to provide assistance in preparation of TORs as needed.</li> </ul>	<b>M</b>
The overall environment in the country for carrying out public procurement and the surveys on perceptions and control of corruption suggest that the fiduciary risk associated is high.	<b>S</b>	<ul style="list-style-type: none"> <li>(i) Disseminating the Bank's procurement and anticorruption rules and practices to procurement and administrative staff related to the Project; application of Transparency provisions of the Bank Guidelines;</li> <li>(ii) Publication of all procurement notices and contract awards on the website of Ministry of Finance website and UNDB;</li> <li>(iii) Members of evaluation committees to sign declaration of confidentiality and impartiality before their nomination.</li> </ul>	<b>M</b>

H: High; S: Substantial; M: Moderate and L: Low.

#### **D. Procurement implementation and arrangements**

Procurement activities will be carried out by the Central Finance and Contracting Unit (CFCU) at the Ministry of Finance. The staff in the Procurement and Contracting Department (PCD) of

the CFCU will be directly responsible for the fiduciary aspects of the project implementation. The PCD comprises 5 staff, including a Director, 2 Procurement Specialists and 2 Contracting Officers. The team is involved in the procurement management of two more multi-donor trust funds, one of which already closed and the second one - - Integrated Planning System of Euro 4 500 000 - - is ongoing, with a possibility of extension by one year and additional financing of Euro 1 000 000. Both Procurement Specialists have knowledge and experience with the World Bank procurement policies and procedures, which is a benefit for the implementation of the project. The procurement staff has practical experience in selection of consultants, both individuals and firms (through QCBS and CQ methods), and procurement of goods (through ICB and Shopping methods). The consultancy contracts are in the range of Euro 120 000 up to Euro 1 000 000 for firms, and up to Euro 50 000 for individual consultants. The ICB contract is at the amount of Euro 800 000. The procurement plan for the entire duration of the project has been prepared.

Procurement of Goods: A small portion of the grant will be spent for financing of – standard off-the-shelf hardware and software. *National Competitive Bidding (NCB)* procedure with the modifications set forth below shall be used for contracts estimated to cost less than Euro 350 000 equivalent per contract.

NCB modifications:

The National Competitive Bidding procedures shall be based on the Open Tendering procedures as defined in the Public Procurement Law of Albania, and the following additional provisions:

- (i) "Open Tendering" procedures as defined in Public Procurement Law of Albania shall apply to all contracts;
- (ii) Foreign bidders shall not be precluded from bidding and no preference of any kind shall be given to national bidders in the bidding process. Government-owned enterprises in Albania shall be permitted to bid only if they are legally and financially autonomous and operate under commercial law of the Borrower;
- (iii) Procuring entity shall use sample bidding documents approved by the Bank;
- (iv) In case of higher bid prices compared to the official estimate, all bids shall not be rejected without the prior concurrence of the Bank;
- (v) A single-envelope procedure shall be used for the submission of bids;
- (vi) Post-qualification shall be conducted only on the lowest evaluated bidder; no bid shall be rejected at the time of bid opening on qualification grounds;
- (vii) Bidders who contract as a joint venture shall be held jointly and severally liable;
- (viii) Contracts shall be awarded to the lowest evaluated, substantially responsive bidder who is determined to be qualified to perform in accordance with pre-defined and pre-disclosed evaluation criteria;
- (ix) Post-bidding negotiations shall not be allowed with the lowest evaluated or any other bidders; and
- (x) Contracts of long duration (more than 18 months) shall contain appropriate price adjustment provisions.

*International Competitive Bidding (ICB)* procedure will be used for procurement goods estimated to cost more than Euro 350 000 equivalent per contract. *Shopping* procedure will be used, if the estimated contract cost is less than Euro 70 000 equivalent. Procurement will be

carried out on the basis of comparing written quotations obtained from at least three qualified suppliers and the Bank's sample Invitation to Quote and evaluation report will be used. *Direct Contracting* procedure will be used for goods contracts, which the Bank agrees meet the requirement for Direct Contracting. Such contracts may be procured in accordance with the provisions of par. 3.6 of the Procurement Guidelines.

Selection of Consultants: Consultants' services contracts to be procured under this project will include technical assistance for establishment of a sound basis for corporate financial reporting legislation alignment with the EY acquis, enhancement of standard settings and IFRS adoption process, drafting relevant by-laws and regulations in the area of public audit, etc. Shortlists for consultants' services for contracts estimated to be less than Euro 70 000 or equivalent may be composed entirely of national consultants. The following consultant selection procedures will be applied for the project: Quality and Cost Based Selection (QCBS), Least Cost Selection (LCS), Consultant Qualification (CQ), Single Source Selection (SSS), Individual Consultants (IC), and Sole Source basis for individual consultants.

Operating Cost: These expenditures are estimated at Euro 36 000 and would cover (**office rent, vehicle rent for supervision, utility and communication costs, translation cost, bank charges, office supplies, advertisement cost, photocopying, mail, etc**) which would be financed by the project as per annual budget approved by the Bank would be procured using the implementing agency's administrative procedures which were reviewed and found acceptable to the Bank. Operating cost will not include salaries of civil servants.

Technical issues as part of procurement decisions: Request for proposals, bidding documents and evaluation reports shall be prepared by the staff in the PCD of the CFCU. The Terms of References (TORs) and Technical Specifications (TS) shall be prepared by the beneficiaries of the relevant project components. When in-house capacity for developing TORs is not sufficient, a foreign strategic adviser shall be involved. The evaluation committees will be appointed before the initiation of each procurement and selection procedure and will comprise representatives of each beneficiary and relevant experts familiar with the assignment. The two procurement staff of the PCD will be available to assist and provide guidance with regard to the procurement process to the evaluation committees. They will be observers with no voting rights. The evaluation committee members will be required to sign a confidentiality and impartiality declaration before their nomination. A standard form of such declaration has been already prepared and is available in the CFCU. The Minister of Finance will issue an order defining who would be the responsible official to appoint the evaluation committees and to sign contracts.

Filing and records keeping: All documents concerning the procurement and selection process, including and not limited to invitation for expressions of interest, request for proposals, evaluation reports, proposals, correspondence between the CFCU and the consultants/bidders, one original of the contract shall be kept on file in the PCD. One original of the contract and the invoices and guarantees (wherever relevant) shall be kept in the Financial Management Department.

## **Procurement Plan**

The Central Finance and Contracting Unit at the Ministry of Finance prepared the Procurement Plan (PP) for the entire project scope consistent with the implementation plan. The PP provides information on procurement packages, methods Bank review method, and the indicative date of initiating the procurement and selection processes, expected date of contract signing and contract completion. The plan was agreed upon during appraisal. It will be available at the CFCU and on the Bank's external website. The PP will be updated in agreement with the Bank

project team annually or as required to reflect the actual project implementation needs and improvements in the implementing agency institutional capacity.

### **Frequency of Procurement Supervision**

Given the small number of contracts (about 7) to be financed from the project and that the estimated value of each is above the regional review thresholds, post review of contracts is not envisaged. It is expected that a supervision mission in the field will be conducted every six months.

### **Anti Corruption Measures**

Considering that the project's risk is rated **Substantial**, a list of anti-corruption measures is recommended:

- The Central Finance and Contracting Unit at the Ministry of Finance will maintain a simple procurement monitoring system with all the milestone dates starting from preparation of technical specs/ terms of reference to contract payment; the system should have: % of contracts awarded to lowest bidders, # of cancelled procurement processes, # processes on which questions raised on evaluation reports, complaints from consultants/bidders, etc.
- All procurement notices and contract awards irrelevant of value and method as well as the procurement plan and its all updated versions shall be published on MoF website and in UNDB;
- A foreign strategic adviser will provide assistance to the entire project team with regard to the project implementation, and on as needed basis for the preparation of TORs and other documents relevant to the project;
- Close monitoring on the conflict of interest situations by asking the evaluation committees to sign impartiality declarations and to check all bids for potential conflict of interest;
- Development and maintaining of an appropriate system for handling complaints;
- FCU will not enable services of firms and individuals debarred by the Bank. The list of such debarred firms and individuals can be found at the following site: <http://www.worldbank.org/html/opr/procure/debarr.html>

**ALBANIA: Corporate Financial Reporting Enhancement Project (CFREP)  
Procurement plan for the whole project duration dated April 2010**

**(a) Goods**

Package No.	Description/ Location		No. of Packages	Procurement Method	Review By Bank (PRIOR / Post)	Invitation Date	Expected Bid-Opening Date	Contract Award Date	Start Date	Completion Date
A	B	C	D	E	F	G	H	I	K	
<b>1. GOODS</b>										
AL-CFREP/G/ICB	Hardware		1	ICB	Prior					
AL-CFREP/G/ICB	Software		3	ICB	Prior					
<b>Total 1. for goods</b>										
<b>Legend:</b>										
ICB =	International Competitive Bidding (in accordance with section 2 of the Guidelines) For goods contracts valued more than <b>Euro 350 000</b>									
NCB =	National Competitive Bidding with the modifications set forth in par. D above For goods contracts valued less than <b>Euro 350 000</b>									
DC =	Direct Contracting (in accordance with section 3.6 of the Guidelines)									
SH =	Shopping (in accordance with section 3.5 of the Guidelines) For goods contracts valued at or less than <b>Euro 70 000</b>									
<b>Prior review</b>										
For Goods contracts: All ICB contracts. First NCB and first Shopping contract.										

**(b) Consultants' Services**

Package No.	Description of Assignment/ Location		Selection Method	Review by Bank Prior / Post	Advertisement for EOI Date	Expected Proposal Submission Date	Contract Award Date	Start Date	Completion Date	
A	B	C	D	E	F	G	H	I	J	
<b>3. CONSULTANTS' SERVICES</b>										
AL-CFREP/I-CS/CQ	Improving the legal framework in the area of corporate financial reporting		CQ	Prior						
AL-CFREP/II-CS/QCBS	Strengthening the capacity of the National Accounting Council		QCBS	Prior						
AL-CFREP/III-CS/QCBS	Establishment of an Audit Oversight System		QCBS	Prior						
AL-CFREP/IV-CS/QCBS	Development of core accounting and auditing curricula and basic training materials for accounting education		QCBS	Prior						
AL-CFREP/V-CS/IC-01	Strategic adviser		IC	Prior						
AL-CFREP/V-CS/IC-02	Implementation Support Consultant		IC	Prior						

AL-CFREP/V- CS/LCS-03	Project Audit		LCS	Prior					
	Incremental operating costs								
<b>Legend:</b>									
QCBS =	Quality and Cost-based Selection (in accordance with sections 2.1 - 2.28 of the Consultant's Guidelines)								
CQ =	Consultants Qualifications (in accordance with section 3.7-8 of the Consultant's Guidelines)								
LCS =	Least-Cost Selection (in accordance with section 3.6 of the Consultant's Guidelines)								
IC =	Individual Consultant (in accordance with section V of the Consultant's Guidelines)								
<b>Prior Review</b>									
	For firms: All contracts equal to Euro 70 000 or more. First two contracts regardless of value and all SSS contracts. For individual consultants: All contracts equal to Euro 20 000 equivalent or more. First two contracts regardless of value and all SSS contracts.								

## Annex 7: Project Preparation and Supervision

### ALBANIA: CORPORATE FINANCIAL REPORTING ENHANCEMENT PROJECT

	Planned	Actual
QER	02/18/2010	02/17/2010
Decision Meeting	04/12/2010	
Appraisal	04/15/2010	
Negotiations	N/A	
Board/RVP approval	N/A	
Planned date of effectiveness of the Grant agreement	07/2010	
Planned closing date of the Grant Agreement	06/2013	

Key institutions responsible for preparation of the project:

- Ministry of Finance

Bank staff and consultants who worked on the project included:

Name	Title	Unit
Andrei Busuioc	Task Team Leader/Financial Management Specialist	ECCAT
Jan Tyl	Team member/Senior Financial Management Specialist	ECCAT
John Hegarty	Head - Center for Financial Reporting Reform	ECCAT
Gradimir Radisic	Senior Operations Adviser, Consultant	ECCAT
Ida N. Muhoho	Senior Financial Management Specialist	ECSC3
Antonia Viyachka	Procurement Specialist	ECSC2

Bank funds expended to date on project preparation:

1. Bank resources: US\$15,000 (2009); FY 2010 US\$30,000;

Estimated Approval and Supervision Costs:

1. Estimated Cost to Approval: US\$45,000
2. Estimated Annual Supervision Cost: [US\$50,000 – to be funded by reg. REPARIS]



## **Annex 8–Documents in the Project’s File**

### Bank Assessment

1. 2006 Accounting and Auditing Report on Observance of Standards and Codes (ROSC)

### Other Bank Documents

1. Country Strategy and Action Plan to Enhance Corporate Financial Reporting in Albania
2. Identification Mission Aide MemoireProject concept note (PCN) and minutes of PCN review meeting
3. Minutes of Quality Enhancement (QER) review
4. Pre-appraisal Mission Aide Memoire