

# KOSOVO POLICY NOTE

## Public Administration Reform

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February 2020



## Key Messages

Effective public administration is a key factor for an economy that aims to generate jobs and improve citizens' well-being. The recently adopted Law on Salaries, Law on Public Officials, and Law on Organization and Functioning of State Administration and Independent Agencies provide a basis to improve public sector management and enable the country to ensure more effective and efficient service delivery to citizens and businesses. However, the Constitutional Court's recent decision to suspend the laws on salary and public officials indicates the complex task of ensuring equality in human resources and pay management. Equality and transparency in the legal framework for public administration are critical for public sector performance and productivity.

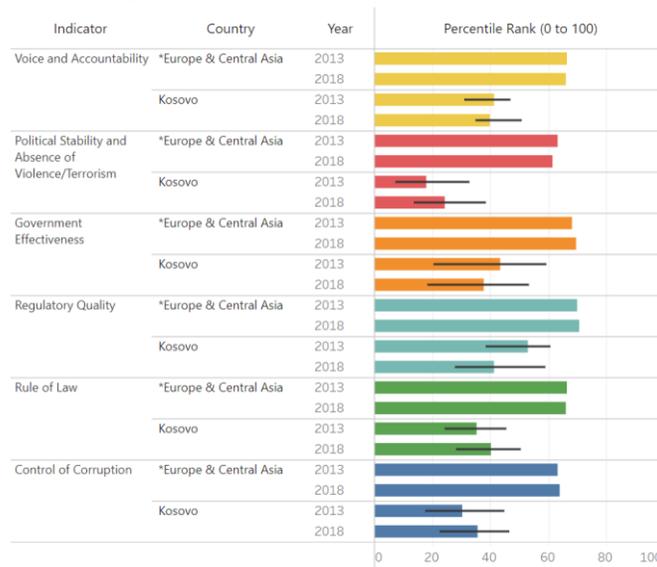
## Key Actions

- Mitigate the fiscal and social risks associated with job classification and the new salary scale through a phased approach for implementing the regulation on allowances, and establish the appeal mechanism for any contentious case. Clearly define the job classification in the regulation to avoid excessive coefficient inflation by categorizing public positions, which are not clearly mapped in the Law on Salaries.
- Evaluate whether the delays with entering the legislation into force due to the Constitutional Court challenge offer an opportunity to amend the primary legal framework to address any remaining inconsistencies in the application of the "equal pay for equal work" principle. Subsequently, develop consistent and coherent regulations to ensure the current implementation of the law.
- Conduct an in-depth analysis of the bottlenecks and foundational challenges in the performance and productivity of public administration and identify drivers for the growing public sector and its associated expenditures.

## Background and Context

**The weak performance of public institutions in Kosovo challenges efficient public service delivery and could impede faster growth.** Although some governance indicators show improvements, a significant gap remains relative to EU member states and regional peers (see figure 1). Inefficient public institutions coupled with weak institutional coordination and capacity constraints have led to substantial gaps in the implementation of public policies resulting in poor quality and coverage of public service delivery, and weak management of public assets including capital investments. These gaps, combined with weak enforcement of the rule of law and the regulatory environment, have also contributed to slow private sector development and the high level of informality.

**Figure 1: World Governance Indicators**



Source: World Bank.

**Addressing Kosovo’s existing structural challenges requires a holistic approach to public sector reform which should include measures to:** (i) ensure fiscal sustainability, including by containing the civil service wage bill and maximizing revenue collections; (ii) enhance spending efficiency and the performance of public sector staff; (iii) enhance accountability and transparency; and (iv) improve the quality and efficiency of services rendered to citizens and businesses. To address some of these challenges, the Government of Kosovo (GoK) has initiated a comprehensive public administration reform (PAR) program and is currently implementing major legal reforms to streamline the government’s organizational structure, rationalize public agencies and publicly owned enterprises (POEs), introduce a standardized and transparent public employment management and compensation system, and move toward performance-based management.

## Challenges to Public Administration Reform

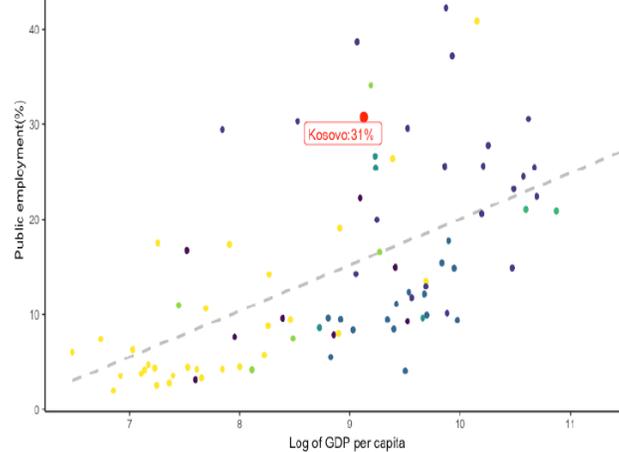
**Weak public sector employment and pay management practices present a major challenge.** Kosovo has a large public sector, composed of 82,223 public servants corresponding to 4.6 percent of the population, and 31 percent of total employment (see figure 2). The generous public sector wages (on average, 30 percent higher than in the private sector in 2016) and high allowances (up to 50 percent of total pay) have encouraged a preference for public sector employment.<sup>1</sup> Combined with the pay increase, the public sector wage bill has increased over the past 10 years (see figure 3)—the largest budget item accounting for 31 percent of government expenditure (2018).

**The lack of transparent, equal, and merit-based human resources and pay management has undermined public sector performance and citizens’ trust in the state.** Although current legislation defines the principle of merit-based employment and pay management, non-merit-based recruitment, pay, and management practices have been persistent across the public sector.

<sup>1</sup> 85 percent adults prefer public over private jobs. Average 2015–19, Balkan Public Opinion Barometer.

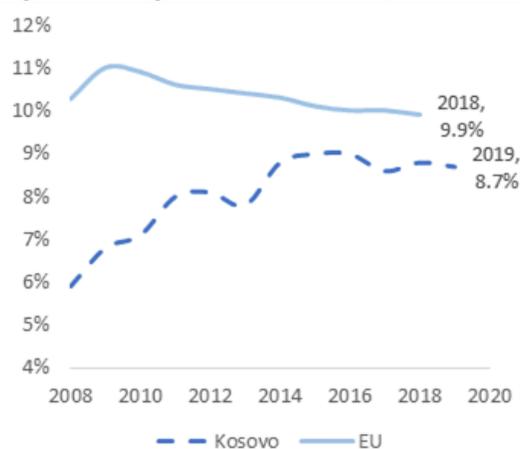
Uncontrolled hiring and inconsistent regulations for internal government organizations have also led to oversized and fragmented institutions with low capacity for coordination and implementation of public policies. The lack of clear legislation has led to a proliferation of allowances—over 60 different allowances, and ad hoc government decisions to top-up salaries for different categories of public officials, which resulted in different wage levels for similar jobs across the government. These have adversely impacted the motivation and productivity of public servants and undermined the performance of public services. According to the Balkan Public Opinion Barometer, about 30–40 percent of Kosovars are unsatisfied with public services, while 60 percent feel the public service is corrupt, and more than half do not trust the government.

**Figure 2: Public share in total employment**



Note: public sector employment measure includes employment in POEs. Sources: Worldwide Bureaucracy Indicators.

**Figure 3: Wage bill share in GDP, 2008–19**



Sources: IMF and EU government finance statistics.

**To address these challenges, the GoK has embarked on an ambitious PAR program.** In March 2019, the National Assembly passed three laws: the Law on Salaries, the Law on Public Officials, and the Law on Organization and Functioning of State Administration and Independent Agencies. The new laws introduce clearer public administration structures by rationalizing and restructuring public institutions, applying a coherent, transparent, and equitable salary system for all public sector employees, and introducing performance-based public sector management. The main

feature of the new laws is a salary scale that integrates most of the fragmented allowances into the base pay and aims for “equal pay for equal work.”

**The fiscal impact is a concern for the ongoing reform process.** The application of the new salary scale is expected to substantially increase salaries for most public officials. According to the World Bank’s rough estimate, without allowances and with constant employment, wage spending in 2020 could reach €631.6 million and stay within the wage bill ceiling.<sup>2</sup> But if allowances are paid up to the current ceiling of 8 percent of total base salaries, the wage bill would breach the fiscal rule on public wages by approximately €76.2 million and could surpass €735 million. The figures should be verified after classifying all public officials into the new pay scale to confirm the real fiscal impact on the wage bill for 2020. If the GoK does not exercise significant restraints over new employment, or if other commensurate cuts are not implemented, it runs the risk of breaching the legally binding deficit ceilings of 2 percent of gross domestic product (GDP).

**The current laws and draft regulations may need improvements to ensure equality and efficiency across the public sector.** The delays with entering the legislation into force due to the Constitutional Court challenge may offer an opportunity to amend the primary legal framework to address any remaining inconsistencies in applying the “equal pay for equal work” principle. Subsequently, consistent and coherent regulations to ensure the law is implemented need to be developed. Clarity in the legal framework is critical to avoid any unintended negative outcomes, such as creating inequality and distortions in the compensation structure or undermining the performance of public services, as well as the fragmentation or proliferation of institutional structures and overlapping government functions.

**Job classification, which needs to be undertaken as part of the new laws, is the most challenging task because of the current legislation’s lack of clear classification criteria and principles.** The exact criteria have yet to be developed under the secondary legislation, which has not been completed. This task is complex and time-consuming, and initially the Law on Salaries defined a very tight legal deadline of December 2019 for applying the new salary scale. Since the two mentioned laws have been sent to the Constitutional Court, the classification has not yet been completed. Classification poses significant risks from legal, social, fiscal, and administrative perspectives, and the GoK would need to consider a cautious approach.

## Addressing the Challenges

**It would be appropriate to phase in implementation of the Law on Salaries and moratorium measures for the provision of allowances.** Compliance with the fiscal rule is key for sound and sustainable fiscal management and to avoid fiscal disruptions. If classifying all staff positions into the new salary scale breaches the wage bill ceiling, the “salary co-efficient value” may need to be lowered in the 2020 budget, and the implementation of allowances (such as those for performance) may need to be delayed.

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<sup>2</sup> The wage bill rule was introduced in 2018 and limits nominal wage bill to a ceiling of €664 million in 2018 and caps its year-on-year growth at the nominal GDP growth rate.

**As per the recent Constitutional Court decision, the GoK may need to consider amendments to the laws to address inequality and inconsistencies, and also ensure full alignment of the law with the secondary legislation, i.e., regulations.** The World Bank has previously provided comments (in October 2019) to revise the law and draft regulations. These comments can help improve the quality of the legal framework. International experiences suggest that the lack of clarity in the legal frameworks lead to unintended negative outcomes such as creating inequality and distortions in the compensation structure, undermining the performance of public services.

**There are risks associated with job classification.** Due to legal, social, and fiscal risks associated with the temporary classification and readjustment of salaries, the GoK may need to consider different options, including delaying the application of the new salary scale until job classification is officially validated under the new regulations, and retroactively pay the difference between the old and new salary scales. In all cases, the independent appeal mechanism, the Independent Oversight Board of Civil Service, stipulated in the Law on Public Officials, should be fully operational to address any complaints.

### **How Can the World Bank Help?**

**In the short term, the World Bank could continue to support the GoK in revising and implementing the laws and regulations on public officials and salaries in line with the recommendations provided.** In the medium term, there are additional areas in which the World Bank could provide support with a view toward improving public sector performance.

**One is to provide an in-depth analysis of broader PAR challenges.** While the current legal reform is expected to have positive impacts, implementation will be a challenge. The World Bank could help the GoK conduct an in-depth analysis on the bottlenecks and foundational challenges regarding the performance and productivity of public administration and identify drivers for growing public sector and employment, high costs, key constraints in current HR management practices, and weaknesses in government functions, including POEs' performance, and develop medium-term policy measures. A public expenditure review can also be useful for understanding gaps in resource allocation to key sectors and efficiency in expenditures, including current expenditure and public investment for service deliveries.

**Investment lending could also be explored, if there is demand from the GoK, to underpin reforms through structural change.** Since the World Bank-financed Public Sector Modernization Project, which ended in 2015, there is a longstanding partnership between Kosovo and the World Bank to support public sector reforms. Most recently, the World Bank has been supporting this PAR agenda, as well as e-governance and tax administration, through advisory and technical assistance. While it could support the analytical work and help address specific issues such as regulatory and institutional foundations for the short term, the investment operation could be used to support the structural issues and public sector modernization, including a digital governance and e-services reform agenda.