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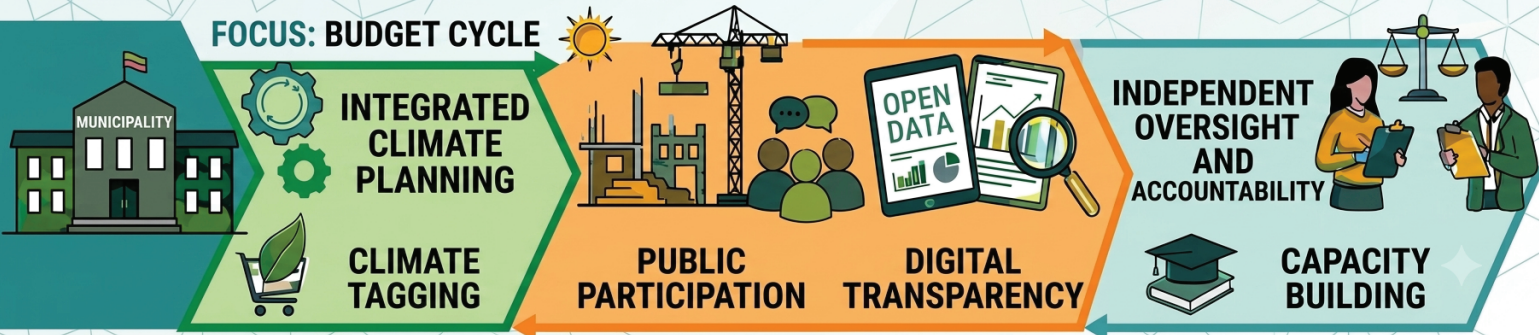
Policy Brief No. 1
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Strengthening the Integrity of Local Climate Finance: Improving Transparency and Accountability in the Municipal Budget Cycle

Strengthening integrity in climate finance management is a fundamental prerequisite for achieving effective and sustainable climate outcomes. Only an integrated approach—one that connects rigorous financial discipline, transparency, and accountability directly with climate goals—can ensure the efficient use of public funds, bolster citizen trust, and position local governments to better attract international climate support.

STRENGTHENING INTEGRITY IN LOCAL CLIMATE FINANCES: ADVANCING TRANSPARENCY AND ACCOUNTABILITY OF THE BUDGET CYCLE FOR MUNICIPALITIES

FOCUS: BUDGET CYCLE



Executive summary

Local Self-Government Units (LSGUs) in North Macedonia play an increasingly vital role in executing climate policies, yet existing weaknesses in the existing Public Financial Management (PFM) system significantly limit the effective and accountable utilization of funds. This analysis demonstrates that risks of irregularities and corruption are not isolated incidents; rather, they stem from systemic vulnerabilities across the entire fiscal cycle—from early strategic planning through to external audit.

The Budget Cycle - In the planning phase, political influences and unclear selection criteria open create space for projects that diverge from actual climate mitigation and adaptation needs. During budget execution, complex procurement processes and weak contract oversight foster conditions for potential favouritism and conflicts of interest. Furthermore, limitations in coverage of financial reporting and under-resourced audit mechanisms impede the timely detection of irregularities, ultimately undermining public trust.

Standard Diagnostics according to International Standards - Benchmark assessments utilising the PEFA Climate framework reveal that Climate Budget Tagging (CBT) among Macedonian municipalities remains at an early stage. Although formal policy structures exist, their minimal practical application exposes a gap between the normative legal framework and functional operational reality.

Transparency and Public Participation - While municipal budget documents are formally published, tracking specific climate expenditures is limited by fragmented data and the absence of a formalized tagging architecture. Citizen engagement is typically delayed, reactive, and procedural, preventing meaningful public input into core strategic priorities before key allocation decisions are finalized.

Opportunities for Improvement - Despite these challenges, a solid foundation for incremental reform exists. The current program-based budgeting structure, existing local strategies, and established legal frameworks offer practical entry points for effective advancements.

Context: Global Goals versus Local Challenges

LSGUs in North Macedonia are increasingly assuming greater responsibilities for both the strategic planning and local implementation of climate policies. However, systemic limitations within national and local Public Financial Management (PFM) frameworks restrict the transparent, efficient, and accountable use of climate funds.

This policy brief summarizes the key findings from an in-depth analysis of corruption risk assessment, diagnostics conducted under the international PEFA Climate framework, and a series of actionable, targeted measures designed to strengthen the institutional integrity and effectiveness of local climate finance.

To understand the systemic response, we have prepared a visual representation that shows that reforms are not separate activities, but rather integrated improvements in each phase of the budget cycle. This overview illustrates how each phase of the budget cycle should be strengthened by interrelated reforms - from early strategy planning to functional performance auditing. In particular, Climate Budget Tagging and Green Public Procurement are pillars of transparency and effectiveness.

Key findings

• Systemic Gap Between Regulation and Practice

The analysis indicates that while local governments in North Macedonia have formally accepted their mandate in climate governance, they face structural and interconnected risks of corruption across all phases of the budget cycle:

- **Budget Planning:** The lack of objective, transparent and clear criteria for prioritizing climate projects created room for political influence and heightens the risk of greenwashing. Capital investment priorities frequently favour short-term political interests over climate vulnerabilities.
- **Budget Execution:** This spills over into the execution phase, where complexity of public procurement, weak contract management, and the lack of mandatory environmental criteria generate risks for favouritism, conflicts of interest, and financial mismanagement. The current PFM framework lacks safeguards to prevent the reallocation of climate-earmarked funds toward lower-priority municipal expenditures.
- **Reporting & Transparency:** Limited transparency reporting mechanisms elevate the risk of undetected inefficiencies.
- **Oversight & Audit:** Constrained capacity and inter-governmental coordination during the audit phase present a risk to full accountability.

Consequently, one of the conclusions is that these risks do not reflect as isolated instances of individual misconduct; they are structural, institutional deficits embedded into the PFM system itself.

• Low Development of Climate Budgeting (PEFA Climate Indicators)

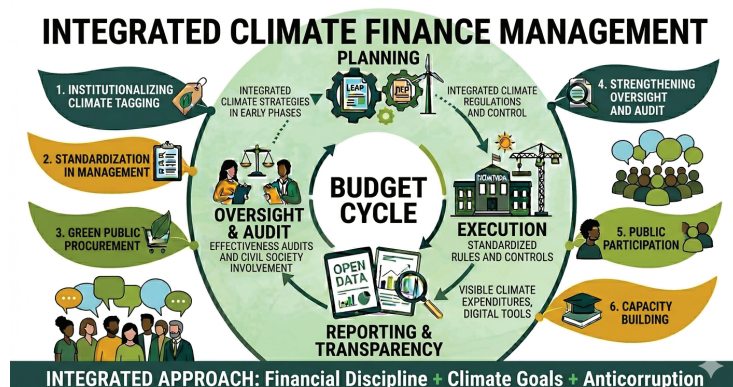
The diagnostic assessment indicates that the climate budgeting system is in an early stage of development, evidenced by the dominant **D** and **D+** scores under the international PEFA Climate framework. This reflects the gap between the normative setting as formal frameworks and strategies exist – **scores C**, however with limited practical application.

The institutional foundations exist, but functional integration into daily financial operations is lacking.

• Limited Transparency and Superficial Public Participation

Fiscal transparency and accountability, which should serve as safeguards, are at the basic compliance-driven level. Although budget documents are formally published, climate expenditures remain difficult to identify due to their fragmentation and the absence of a climate budget tagging system. Furthermore, local audit capacities are constrained and skewed towards formal compliance, rather than performance audits, undermining effective oversight. Limited visibility of spending prevents the public from identifying inefficiencies and intervening in a timely manner. Public participation, as a pillar of local accountability, occurs late in the budget formulation cycle, when opportunities for influence on strategic climate priorities are closed and often focused on short-term issues.

Hence, transparency can be categorized as to a larger degree more declarative than substantive.



<i>Key challenges detected in the system</i>	<i>Detected strengths of the system</i>
• <i>Absence of Climate Budget Tagging (CBT) system</i> • <i>Limited administrative and technical capacities</i> • <i>Weak central–local intergovernmental coordination</i> • <i>Low budget execution rates and frequent reallocations</i> • <i>Insufficient oversight and public accountability</i>	• <i>Alignment between the existing program-based budget structure</i> • <i>Active local strategies in place (LEAP, LED, etc.)</i> • <i>Weak central–local intergovernmental coordination</i> • <i>A functional external audit institutional system</i> • <i>Broad historic institutional experience with donor-funded projects</i>

Foundation for Reform by Leveraging Existing Strengths

Despite the profound structural challenges, there is a solid foundation for reform that allows for incremental improvements without the need for a full-scale systemic reform. The existing program budget structure offers a format that can be easily adapted, and local strategic documents, such as LEAP and LED, are already in place across most LSGUs. Furthermore, there is a functioning external audit system and significant experience with donor projects. Combined with an existing legal basis for integrating green public procurement criteria, the structural groundwork is ready for systemic implementation. Reforms can build directly upon these elements to achieve meaningful change without systemic disruption.

Hence, the conclusion that the existing elements enable reforms without the need for a complete systemic reform.

Priority Recommendations for Actionable Measures

To strengthen fiscal integrity and drive sustainable development, changes need to focus on institutionalization of functional mechanisms over formal procedures. Key policy interventions should focus on:

- **Introducing Climate Budget Tagging:** through integration into the existing program budget, which will allow for clear identification of climate expenditures and quarterly monitoring and reporting
- **Standardizing Climate Finance Management:** through the preparation and adoption of unified municipal acts that will contain criteria and methodologies for project assessment, as well as unified reporting.
- **Public Procurement Reform:** by introducing mandatory "green" criteria in procurement, with automated controls and binding conflict of interest declarations.
- **Strengthening Oversight and Audit:** through development of a methodology for auditing climate finance, conducting performance audits (shifting away from exclusive compliance audits), building audit capacities at the local level, and active involvement of civil society organizations.
- **Structuring Early Public Participation and Transparency:** through the introduction of substantive participatory budgeting mechanisms, conducting thematic climate consultations, open data, as well as building capacities for climate budgeting and anti-corruption mechanisms.

Effective Climate Finance Through Collaboration and Integrity

Strengthening integrity in climate finance governance is not a technical issue, but a matter of integrity, trust and development. Effective governance at the national level is crucial for the integrity and sustainable development. Without strong systems of transparency, accountability and control, there is a high risk that the public funds will be used inefficiently or misallocated, undermining the credibility of the policies.

In this effort, central government agencies, LSGUs, and civil society organizations must operate in close synchronization.

While the **central government** is obliged to provide a clear legal and regulatory framework and strong control mechanisms, **local self-government** should pay attention to strengthening capacities, transparent planning and accountability. Only through coordination and proactive management public funds can contribute to real climate results and increased citizen trust. Civil society organizations have an important role as watchdogs and partners in the process. Involving citizens at an early stage allows community priorities to be translated into real actions, and the risks of abuse to be minimized.

... for the central government: effective climate finance management at the national level is a key for integrity, trust and sustainable development of the country. Without clear and consistently implemented mechanisms for transparency, accountability and control, there is a high risk that the funds intended for climate activities will be used inefficiently, diverted or create a perception of injustice, thereby undermining the credibility of policies. Strengthening institutional capacities, oversight systems and accountability mechanisms not only reduce the risks, but also increases the likelihood that climate investments will achieve visible and sustainable results, contribute to citizen trust and attract additional financial resources.

...for local self-government: effective management of climate finance at the local level is key to ensuring visible results and trust between citizens and institutions. The local government is closest to citizens and has an important role in implementing national laws and policies. To ensure that climate investments are efficient, fair and accountable, local governments should pay attention to strengthening capacities and transparent planning, accountability and control mechanisms. They should also signal to the central government when there are difficulties in implementing measures or when additional support is needed, especially in rural and smaller municipalities that do not have sufficient resources to mitigate the effects of climate change. Only through coordination with central government and proactive management at the local level can public funds contribute to real climate results and increased citizen trust.

... for civil society organizations and the public: effective management of climate finance is essential to ensure fair, sustainable and visible results for the community. Civil society organizations and the public have an important role as oversight and partners in the planning and implementation process of climate projects. Through active participation, monitoring and constructive recommendations, they can assist in ensuring transparency, accountability and proper allocation of funds. Involving citizens early in the budgeting and decision-making process ensures that community priorities are translated into real actions, while minimizing the risks of misuse. Only jointly, through dialogue, oversight, and partnership with local and central governments, can public funds create concrete climate outcomes that strengthen citizens' trust in institutions and contribute to resilient, sustainable, and inclusive communities. Without sufficient transparency, accountability, and public oversight, there is a risk that funds earmarked for climate action are not used efficiently or do not respond to the real needs of the community.

Conclusion

North Macedonia has a solid foundation for developing climate-responsible public finance management at the local level. However, a clear transition from formal procedures to functional systems is needed. This transition requires a unified approach that fuses financial discipline, national climate targets, and targeted anti-corruption mechanisms. Systematizing these linkages will directly yield superior climate outcomes, optimal public spending efficiency, and enhanced public trust in state and local institutions.



ABOUT THIS BRIEF

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The project aims to contribute to the enhancement of the local governance integrity through improved transparency and accountability in climate-related financing, thereby mitigating irregularity risks and optimizing local resource allocation.

The findings and policy recommendations presented in this brief are derived from: **Baseline Assessment: Climate Finance in North Macedonia: Analysis of Public Financial Management (PFM) Processes in the Context of the Budget Cycle**, prepared by CEA.

Source of illustrations: Visual illustrations and thematic diagrams within the brief were generated utilizing artificial intelligence design tools.

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