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AUDIT REPORT

ON THE ANNUAL FINANCIAL STATEMENTS OF THE PUBLICLY OWNED ENTERPRISE KOSOVO RAILWAIS - TRAINKOS J.S.C FOR THE YEAR ENDED 31 DECEMBER 2017

Prishtina, June 2018

The National Audit Office of the Republic of Kosovo is the highest institution of economic and financial control which, according to the Constitution and domestic laws, enjoys functional, financial and operational independence. The National Audit Office undertakes regularity and performance audits and is accountable to the Assembly of Kosovo.

Our Mission is through quality audits strengthen accountability in public administration for an effective, efficient and economic use of national resources.

We perform audits in line with internationally recognized public sector auditing standards and good European practices.

The reports of the National Audit Office directly promote accountability of public institutions as they provide a base for holding managers' of individual budget organisations to account. We are thus building confidence in the spending of public funds and playing an active role in securing taxpayers' and other stakeholders' interests in enhancing public accountability.

The Auditor General has decided on the audit opinion on the Annual Financial Statements of the Publicly Owned Enterprise Kosovo Railways – Trainkos J.S.C in consultation with the Assistant Auditor General, *Vlora Spanca,* who supervised the audit.

The report issued is a result of the audit carried out by *Team Leader Ganimete Dalloshi and team member Valmira Jonuzi* under the management of the Head of Audit Department *Enver Boqolli.*

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Executive Summary

Introduction

This report summarises the key issues arising from our audit of the 2017 Annual Financial Statements of Publicly Owned Enterprise Kosovo Railway - Trainkos J.S.C for 2017 which determines the Opinion given by the Auditor General. The examination of the 2017 financial statements was undertaken in accordance with the International Standards on Supreme Audit Institutions (ISSAIs). Our approach included such tests and procedures as we deemed necessary to arrive at an opinion on the financial statements. The applied audit approach is set out in our External Audit Plan dated 13/10/2017.

Our audit focus has been on:

The level of work undertaken by the National Audit Office to complete the 2017 audit is determined depending of the quality of internal controls implemented by the Management of the Trainkos.

The National Audit Office acknowledges Trainkos Senior Management and Staff for cooperation during the audit process.

Opinion of the Auditor General

<u>Adverse Opinion</u>

The Annual Financial Statements for 2017 do not *present a true and fair view* in all material aspects.

For more, please refer to Section 1.2 of this report.

Annex I explains the different types of Opinions applied by the National Audit Office.

Key Conclusions and Recommendations

Conclusion	Recommendation
The material misstatements spread within the entire financial statements have led to an Adverse Opinion on the AFS of 2017.	The Chairman of the Board should analyse the reasons for giving the Adverse Opinion on AFS of 2017 and undertake the actions required to enable a fair and true presentation of the AFS in 2018 (see issues at basis for opinon).
Non-current assets, stocks, advances, payables, tax liabilities & contributions and disclosures are audit components that have been identified incorrectly.	The Chairman of the Board should apply a detailed assessment to identify the reasons for the weaknesses and to take the necessary actions to address these (see issues 2 to 8 and 10).
Commitment is still required to eliminate all shortcomings during the staff recruitment processes.	The Chairman of the Board should ensure, in addition to legal requirements, to implement staff recruitment procedures and eliminate identified weaknesses (see issue 9).
Despite the progress shown in the implementation of the recommendations, most of the unimplemented recommendations relate to areas that had an impact on the opinion.	The Chairman of the Board should implement a rigorous process to ensure that the prior year's recommendations are addressed, with the focus being the recommendations that have an impact on opinion. (see issue 11).
Governance arrangements related to accountability, management reporting and risk management were improved. However, the lack of an Internal Auditor remains a matter of concern.	The Chairman of the Board should select an internal auditor to assist management in evaluating internal controls in the Enterprise (see issues 12-13).

Management response to audit 2017

The Chairman of the Board disagreed with all audit findings and conclusions. The comments of the Chairman of the Board on issues that we have not agreed upon are detailed in Annex III.

1 Audit Scope and Methodology

Introduction

The National Audit (NAO) is responsible for carrying out a Regularity Audit which involves the examination and evaluation of Financial Statements and other financial records and expression of opinions on:

1. Whether the financial statements give a true and fair view of the accounts and financial affairs for the audit period;
2. Whether the financial records, systems and transactions comply with applicable laws and regulations;
3. The appropriateness of internal controls and internal audit functions; and
4. All matters arising from or relating to the audit.

Audit work undertaken reflected our audit risk assessment for Trainkos. We have analysed the Trainkos' business to the extent to which management controls can be relied upon when determining the overall testing required to provide the necessary level of evidence to support the Auditor General's (AG's) opinion.

The following sections provide a more detailed summary of our audit finding with emphasis on observations and recommendations in each area of review. Management's responses to our findings can be found in Annex III.

Our procedures included a review of the internal controls, accounting systems and related substantive tests and related governance arrangements to the extent considered necessary for the effective performance of the audit. Audit findings should not be regarded as representing a comprehensive statement of all the weaknesses which exist, or all improvements which could be made to the systems and procedures operated.

2 Annual Financial Statements and other External Reporting Obligations

Introduction

Our audit of the Annual Financial Statements (AFS) considers both compliance with the reporting framework and the quality and accuracy of information recorded in the AFS. AFSs have been prepared and signed by the Chief Financial Officer and Treasury (CFOT) and the Chief Executive Officer (CEO) and submitted for approval to the Board of Directors (BoD).

The approval of the AFS incorporates a number of assertions relating to compliance with the reporting framework and the quality of information within the AFS. These assertions are intended to provide the Shareholder and wider public with the assurance that all relevant information has been provided to ensure that an audit process can be undertaken.

2.1 Audit Opinion

Adverse Opinion

We have audited the AFS of the Trainkos for the year ended on 31st of December 2017 which comprise of the Balance Sheet, Statement of Incomes, Cash Flow Statement, Statement of Changes in Equity and the Explanatory Notes.

In our opinion, due to the effects of the matter described in the paragraph on the Basis for Adverse Opinion, the Annual Financial Statements for the year ended on 31st of December 2017 do not present a true and fair view in all material respects of Trainkos in accordance with International Accounting Standards (IAS), International Financial Reporting Standards (IFRS) and Kosovo Laws. The Annual Financial Statements have been prepared under the accrual basis of accounting, Law no.03/L-048 on Public Financial Management and Accountability (as amended and supplemented) and Law no.04/L-087 on Publicly Owned Enterprises (as amended and supplemented).

Basis for Adverse Opinion

1. Uncollected debts are debts which customers owe to the business and for which it is decided that they will never be paid. They are deleted from books as expenses and transferred to the income statement. Receivables during 2017 were reduced by €523,232 which were unrecovered old debts which the enterprise declared as bad debt. However, when recording in the bookkeeping these debts were not recorded as an expense in the income statement, but the reserve capital was reduced for that amount.
2. The following investments presented in the balance sheet totalled €247,164, out of which € 00,568 only meet the recognition criteria as the ongoing investment. While the

remaining amount of €146,600 is completed investments that should have been registered as non-circulating assets.

3. The enterprise did not make a revaluation of non-current assets even though it is required by IAS 16 to re-evaluate once in 3 to 5 years. This due to financial difficulties.
4. At the end of the year, the enterprise carried out stocktaking prepared the stocktaking report which did not comply with the accounting records. For the purpose of adjusting these differences, the enterprise cleared from its records the stocks which do not actually exist, but this adjustment was made by debiting the capital in the amount of €96,732.
5. The reserve fund at the end of 2016 had a balance of €5,003,218, but in 2017 the enterprise made some adjustments to some financial items of 2016 and to the closing of the pending account which, as counter account used reserve capital resulting with remaining balance at end of 2016 of €5,330,438. Further on, during 2017, this item was changed due to the recording of bad debts in this account as well as the adjustment of some other records.
6. The profit for the year does not represent a financial result of the enterprise as a result of not recording the costs of bad debts in the income statement in the amount of €523,232.
7. Under IAS 7, an entity presents the cash flow from its operating, investing and financing activities in the most appropriate manner for its business. Transactions with investment activities amounted to €964,095, which were received by MED for capital investments and should be categorised into financing activities. Further on, payments made for operational activities of €80,564 were presented as payments for investment activities.
8. Under IAS 20, grants received for depreciable assets are recognised as revenues over periods in which amortization is charged for those assets. Trainkos in the income statement from grants other than grant revenues that resulted from the amortization of grants funded assets, recognized the revenues from subsidies received by MED for operating expenses in the amount of €72,622.
9. The explanatory notes do not provide complete and accurate disclosures for some of the items presented in the financial statements, for more details see subchapter 3.6.

Our audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the AFS section of our report. NAO is independent of the Publicly Owned Enterprises in accordance with the ethical requirements that are relevant to our audit of the annual financial statements of Budget Organisations and POEs in Kosovo and we have fulfilled other ethical responsibilities in accordance with these requirements. We believe that the obtained audit evidence is sufficient and appropriate to provide a basis for the adverse opinion.

Responsibility of the Management and Persons Charged with Governance for AFS

The Chairman of the Trainkos Board is responsible for the preparation and fair presentation of financial statements in accordance with International Accounting Standards (IAS), International Financial Reporting Standards (IFRS) and Laws of Kosovo, as AFS have been prepared under the accrual basis of accounting, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error. This includes the application of Law no. 03/L-048 on Public Financial Management and Accountability (as amended and supplemented) and Law no.04/L-087 on Publicly Owned Enterprises (as amended and supplemented).

The Chairman of the Board is responsible to ensure oversight of Trainkos' financial reporting process.

Auditor General's Responsibility for the Audit of the AFS

Our objectives were to obtain reasonable assurance on whether the annual financial statements as a whole are free from material misstatement, whether due to fraud or error and give an audit opinion. However, due to the significance of issues described in the Basis for Disclaimer of Opinion paragraph, we have not been able to obtain the required audit evidence to formulate proper basis for an opinion.

2.2 Compliance with AFS and other reporting requirements

POE is required to comply with a specified reporting framework and other reporting requirements. We considered:

- Requirements of Law no.03/L-048 on Public Financial Management and Accountability (as amended and supplemented);
- Requirements of the Law no.02/L-123 on Business Organisations;
- Requirements of the Law no.04/L-087 on Publicly Owned Enterprises (as amended and supplemented);
- Requirements of the Law no.04/L-104 on Accounting, Financial Reporting and Auditing;
- Requirements of the Law on Public Procurement (as amended and supplemented);
- Requirements of the Instruction no.2/2013/MF on the Structure and Content of Annual Financial Reports; and
- POEs are also required to prepare the following reports:
    - POE Charter;
    - Business Plan;
    - Quarterly reports;
    - Annual reports;
    - Consumer satisfaction Report; and
    - Draft and final procurement plan in time.

Draft AFS dated 07/05/2018 required some financial adjustments in the balance sheet, income statement, statement of changes in equity, cash flow statement and explanatory notes that were followed by material errors. Following our suggestions to undertake the required actions, Trainkos made some adjustments, but failed to fully eliminate the errors. As a result we have identified the findings that we have presented to the basis for the opinion.

Given the above – AFS prepared by CEO and CFOT when submitted to the BoD cannot be considered accurate.

In the context of other external reporting requirements, we have no issues to raise.

2.3 Recommendations related to Annual Financial Statements

Recommendation 1 The Chairman of the Board should ensure that an analysis is undertaken to determine the causes of the Adverse opinion. Actions need to be undertaken to address the causes in a systematic and pragmatic manner to remove errors in the Annual Financial Statements and ensure a true and fair view.

Further on, the Chairman of the Board should ensure that effective processes are in place to confirm that the 2018 AFS production plan formally addresses all compliance related issues. This should also include Management review of the draft AFS with specific focus on high risk areas and areas where errors have been identified in previous years. The Statements should not be signed by the CEO and CFOT unless all necessary checks have been applied before the same are submitted to the BoD.

3 Financial Management and Control

Introduction

Our work related to Financial Management and Control (FMC) reflects the detailed audit activities undertaken on Revenue and Expenditure Systems within POEs. Specifically, the focus of the audit was management of revenues, expenses, assets, liabilities and receivables.

Financial Management and Control Conclusion

In the context of financial systems, revenue controls in general are strong and are being implemented effectively. However, in many areas when preparing financial statements, obvious shortcomings were noticed such as: non-presentation of non-circulating assets, inventories, advances, payables and tax liabilities and contributions.

Engaging employees for specific duties and assignments for regular job positions and without developing any competitive process, and testing of candidates that do not comply with legal requirements, are an indication that internal controls in human resource management need to be improved.

3.1 Business Plan (Revenues and Expenditures)

We have considered the sources of revenues and expenditures planned with the annual business plan according to the respective categories. This is highlighted in the following tables:

Table 1. Table on Revenues and Expenditure according to annual plan for 2017 (in €)

Description	Initial Planning	Final Planning	2017 Outturn	2016 Outturn
Revenue from freight transport	1,266,000	1,030,000	842,835	589,146
Income from passenger transport	211,135	185,676	125,387	188,906
Revenues from MED subsidies	500,000	500,000	744,814	500,000
Revenues from MoI subsidies	1,967,292	1,967,293	1,151,613	759,766
Other revenues	125,000	140,000	385,839[1]	173,670
Revenues from guarantors for capital investments by MED	1,000,000	1,000,000	891,480	939,804
Total Revenues	5,069,427	4,822,969	4,141,968	3,151,292
Salary expenditures	1,873,500	1,781,000	1,674,841	1,769,155
Goods and Services (including Utilities)	380,800	332,300	272,946	245,393
Cost of service	1,675,010	1,645,500	1,151,853	1,338,142
Total Expenditures	**3,929,310**	**3,758,800**	**3,099,640**	**3,352,690**

Explanations for changes in planning revenues and expenditures are given below:

- Initial planning of revenues from sales/services and subsidies was significantly higher than the final plan. However, at the end of the year the Enterprise managed to collect 86% of the planned amount. Exceeding the planned amount is seen in the MED grant revenue, where the planned amount was exceeded by 49%. This because MED in addition to the amount planned in the subsidy agreement at the end of the year had also transferred €244,814 to cover some expenses arising from a court dispute inherited from former UNMIK Railways. Further on, as a result of transferring of €268,526 from MED to cover certain expenses, the amount planned in other revenues was exceeded by 176%. However, a lower level of execution compared to the planning is noticed in the revenues from subsidies from the Ministry of Infrastructure where the plan was met only by 59% and on passenger transport revenues, which were collected only 68%.
- As far as expenditures are concerned, the Enterprise has been more cautious in relation to the previous year. Expenditures executed this year in relation to planning were 82%. The

[1] Other revenues include: revenues from other services €26,368, revenues from the sale of oil for Infrakos 45,217, revenues from damage to wagons and other €45,727 and revenues from subsidies from MED of €268,526

highest expenditures occurred in wages, which accounted for 54% of total expenditures. Their execution in relation to planning was 94%. Regarding the cost of service, around 37% of the expenditures occurred for this category. However, compared with the previous year, this category has a budget saving of 14%.

Recommendations

We have no recommendations in this area.

3.2 Balance Sheet[2] (Statement of Financial Position)

We have audited the Balance Sheet by testing the account balances of accounts as well as the transactions occurring during the year within these accounts. In addition to examining the accounting balance of accounts, we have also addressed aspects of compliance with laws and regulations and we have provided the following recommendations.

Table 2: Balance Sheet of Trainkos on 31st of December 2017 **(in €)**

Assets	**2017**	**2016**	**Liabilities and Equity**	**2017**	**2016**
Land, buildings, equipment and machinery	6,108,772	5,794,005	Charter capital	25,000	25,000
Ongoing investments	247,165	698,539	Reserve Capital	4,738,813	5,162,474
Stocks	455,752	534,198	Carried forward Profit/Losses	(1,102,387)	398,245
Receivables	1,329,087	1,515,446	Profit/Loss of the Year	113,861	(1,500,632)
VAT Prepayment	382,841	294,038	Long Term Liabilities	3,933,999	3,965,552
Other Receivables (advances given)	23,489	23,489	Payables	1,291,295	829,271
Cash in the bank and cash register	695,291	51,047	Employee Obligations	3,953	1,721
			Obligations on taxes and contributions	225,212	29,131
			Profit Tax Obligations	**12,651**	
Total:	**9,242,397**	**8,910,762**		**9,242,397**	**8,910,762**

[2] IAS has changed the term "Balance Sheet" has been changed into "Statement of Financial Position" according to IAS, but as long as the company has named it the Balance Sheet, we have referred to this designation in order to be consistent with the designation in AFS we are auditing.

Issue 2 – Inaccurate presentation of non-current assets

Finding Accounting records should be a reliable source for preparation of financial statements. However, we noticed discrepancies between them for the following items: the facilities, equipment and machinery presented in the balance sheet were understated by €8,074 (facilities, equipment) and €7,699 (machinery presented). This understatement resulted due to reconciliations made in the balance sheet.

Risk Discrepancies between accounting evidence and the amount of figures presented in the statements except presenting inaccuracies, increase the risk of misuse with non-current assets.

Recommendation 2 The Chairman of the Board should ensure that an accurate list of non-current assets has been drafted and that the necessary actions are taken to adjust the financial statements and ensure that, when drafting them, the source is the accounting evidence.

Issue 3 – Non-reconciliations in the physical condition of stocks with accounting records

Finding The Enterprise at the end of the year had made stocktaking and prepared an inventory report. However, this inventory report does not comply with the accounting evidence, even though the enterprise has taken the necessary actions for the factual reconciliation of inventories according to recording into accounting records. This discrepancy is an overstatement of €1,972. Due to this, there were ineffective controls in reconciliation of accounting records with factual situation of stocks.

Risk The management of the enterprise does not have an accurate picture of the stocks and as a consequence may make unnecessary supplies or will not be able to make the necessary supplies due to insufficient accounting information. Furthermore, this increases the risk of avoidance and misuse of stocks.

Recommendation 3 The Chairman of the Board should ensure that stock records are reconciled in the accounting records with their actual situation and ensure that controls are in place to track stocks and that reports are made to management on a regular basis.

Issue 4 - Failure to properly present other receivables (advances given)

Finding	The Enterprise in the AFS presented other receivables (advances given) in the amount of €23,489 while in the accounting records, the value of this account is €26,893. Furthermore, this amount of advances also contains data from 2014, for which services/supplies were not yet received in exchange for this value. Failure to take proper care in the case of supplies/services and the lack of internal controls function has made these advances not be used since 2014.
Risk	Understatement of financial items results in presentation of an incorrect statement of financial position. Failure to get long-term services/supplies increases the risk that the enterprise cannot exercise its rights due to the age of the debt.
Recommendation 4	The Chairman of the Board should ensure that financial statements present an accurate financial value when AFS are drafted. Further on, to ensure that the services/supplies in return for this amount are executed in the optimum terms for the amount paid as advance.

Issue 5 - Inaccurate presentation of payables

Finding	Payables presented in the balance sheet do not present an accurate balance of liabilities to suppliers. Compared to the accounting records they were understated by €26,893. In addition, in the two letter confirmations received from the suppliers, discrepancies have been noticed with the accounting entries. From a confirmation letter received by one supplier, the value of the confirmed debt is €425, while in the bookkeeping notes the value of the liability to this supplier was €644. While in another case, the supplier has confirmed the debt in the amount of €6,715, while in the accounting records, this value is €6,090. Furthermore, a debt of €3,171 has not been adjusted from the previous year and continues to appear in the accounting records. The inaccuracies associated with payables result from non-compliance of accounting records with suppliers.
Risk	Failure to keep accurate accounts for payables increases the risk of making more payments to suppliers or even creating litigation.
Recommendation 5	The Chairman of the Board should ensure that the completeness and accuracy of the list of obligations to suppliers is verified on a regular monthly basis and that the respective officers are reporting in this regard.

Issue 6 - Failure to properly present tax liabilities and contributions

Finding Source tax withholding obligations and contributions presented in the balance sheet show an increase compared to the previous year. The value of these liabilities was €225,212. However, this amount presented does not reflect the real situation for these obligations. This, since, according to the Tax Administration of Kosovo (TAK) report on the taxpayer's debts situation, the amount of taxes and contributions was €7,113 lower than the amount presented in the balance sheet. This has been the consequence of not reconciling accounting records with TAK records. The enterprise has not been subject to TAK control since its establishment.

Risk Failure to properly present liabilities creates inaccuracies in the balance sheet. Similarly, the lack of accurate evidence regarding these obligations risks the enterprise to pay more than the amount of the obligation.

Recommendation 6 The Chairman of the Board should take necessary actions to ensure that the accounting records are in line with the balance of debts in TAK and that the obligations are paid according to the foreseen deadlines. At the same time, it should provide accurate presentation of financial items.

3.3 Statement of Income and Expenditures

Trainkos has all types of revenues it has generated during the year, expenses, and financial outcome presented in the following statement.

Table 3: Statement of Income and Expenditures as of 31st of December 2017 (in €)

Revenues	**2017**	**2016**
Revenues from sales/services	2,953,314	2,157,031
Other revenues	224,552	11,179
Income from grants	991,591	990,579
Total Revenues	4,169,457	3,158,788
Cost of service	**1,151,853**	**1,238,149**
Salary expenditures	1,674,841	1,761,366
Depreciation Expenses	943,305	997,101
Operational and Administrative Expenses	272,946	431,108
Other extraordinary events	-	231,696
Total Costs	**4,042,945**	**4,659,420**
Profit / Loss before tax	**126,512**	**(1,500,631)**
Tax on profit	12,651	-
Profit / Loss	**113,861**	**(1,500,631)**

Our audit examinations regarding the statement of income and expenses have resulted in the following findings:

Issue 7 - Recognising revenues not in accordance with the accrual principle

Finding	According to accrual accounting principle, transactions and economic events are recognised at the moment when they occur and not when cash is accepted or given. In passenger transport revenues, in two cases amounting to €4,364, revenues collected for the service provided in the previous year were recognized as revenues of this year. This has happened due to non-disclosure of fiscal coupons and sales reports.
Risk	Failure to recognize economic events and transactions at the time they occur increases the risk that the incomes of the respective year are understated/overstated.
Recommendation 7	The Chairman of the Board should ensure that sales reports are submitted in time and that revenue recognition and reporting for the relevant period is being made at the time of occurrence and not when cash is accepted.

Issue 8 - Overstating costs of fuel loss

Finding	It is a requirement of IAS 1 that all items of income and expense recognized over a period should be included in profit or loss unless a Standard or an Interpretation requires otherwise. The enterprise in the income statement has presented expenses for the losses of fuel in the amount of €2,434, out of which €4,291 belong to the 2016 period. This was due to the non-adjustment of the accounting records in the relevant period.
Risk	Presentation of the prior-year costs of fuel losses results in overstatement of costs and respectively understatement of the financial result.
Recommendation 8	The Chairman of the Board should ensure that the necessary adjustments are made and also that the expenses are recognized at the time of the occurrence, respectively in the period incurred.

Issue 9 – Shortcomings in Human Resource Management

Finding During the audit of this category, the following weaknesses were identified:

- Based on the Labour Law, every public sector employer is obliged to announce public vacancy whenever an employee is hired and an employment relationship is established. By June 2017, Trainkos had hired four employees for specific jobs and duties covering regular job positions and for which they did not develop recruitment procedures. However, after receiving our 2016 report there were no such cases.

- Administrative Instruction no. 14/2011 on Labour Relations on the Recruitment Process stipulates that the written test should consist of three parts with a defined number of points for each of them: the percentage for general knowledge, the percentage of general skills questions and personality, as well as the question related to the workplace. We have noticed that in three recruitment processes, the test of candidates was drafted only with job-related questions. This is due to ineffective internal controls and inadequate management oversight on the recruitment committee.

Risk Weaknesses in the staff recruitment process, i.e. testing of candidates only with job-related questions and engagement of assigned employees for specific assignments and works in a regular job position without developing any competitive process, except that it is in contradiction with the regulation in force, increases the risk of inadequate staff selection which may reflect on the performance of the organization in general.

Recommendation 9 The Chairman of the Board should review the identified shortcomings and take the necessary measures that the engagement of employees for specific assignments and works and the drafting of the test are done according to the relevant legal provisions in force.

3.4 Statement of Changes in Equity

In the Annual Financial Statements of the enterprise, capital is presented under the following structure:

Table 4: Capital of the Trainkos on 31.12.2017 **(in €)**

Description	**31 December 2017**	**31 December 2016**
CAPITAL	**3,775,287**	**4,085,087**
Charter Capital	25,000	25,000
Reserve Capital	4,738,813	5,162,474
Profits/Losses carried forward	(1,102,387)	398,245
Current Year Profits/Loss	113,861	(1,500,632)

Shortcomings regarding the presentation of capital are presented within the basis for the opinion.

3.5 Cash Flow Statement

Table 5: Cash Receipts and Spending **(in €)**

Description	31 December 2017	31 December 2016
Net cash from operating activities	**415,918**	**(2,807,979)**
Cash receipts from buyers	3,026,152	657,228
Cash receipts from insurance for damage compensation	6,831	
Other cash receipts from operating activities	195,904	
Cash payments for suppliers	(1,314,864)	(1,505,426)
Payments of Cash to employees	(1,418,622)	(1,728,085)
Payments of Cash for taxes	(64,706)	
Other cash payments for operating activities	(14,777)	(231,696)
Net cash from investing activities	**228,326**	**(998,969)**
Other cash receipts from investment activities	964,095	
Other cash payments from investment activities	(735,770)	(998,869)
Net cash from financing activities		**2,031,959**
Other cash receipts from financing activities		2,031,959
Increase / decrease of Cash during the year	644,244	(1,774,989)
Cash and its equivalents at the beginning of the year	51,047	1,826,036
Cash and its equivalents at the end of the year	**695,291**	**51,047**

Shortcomings related to cash flow presentation have been presented to the Basis for the Opinion.

3.6 Handling of Explanatory Notes

Explanatory notes provide information on the basis of preparing the financial statements and accounting policies required by the IFRS and provide additional information that is not disclosed in the Balance Sheet, Income Statement, Cash Flow Statement or Statement of Changes in Equity, but are important to understand each one of them.

Issue 10 - Incomplete disclosure of explanatory notes

Finding

Explanatory notes should be disclosed systematically as long as this is possible. Each item of the financial statements should be referred to the relevant information in the notes.

When analysing the notes, the following weaknesses were identified:

- Information on the ongoing investments presented in the balance sheet was not disclosed;
- Information on cash flow statement items was not disclosed;
- Information on the statement of changes in equity was not disclosed; and
- Explanatory notes for: non-current assets, stocks, advances, payables and tax liabilities and contributions do not present accurate information.

Risk

The incomplete presentation and shortcomings in disclosures have an impact on the quality of the financial statements, the uncertainty of the figures presented ad limit the users of the statements to understand the true and fair situation of the financial and business outcomes of the enterprise.

Recommendation 10

The Chairman of the Board of Directors should ensure when preparing the AFS, the explanatory notes will present all detailed, complete and accurate information as required by the accounting standards.

4 Progress in implementing recommendations

Our Audit Report on the 2016 AFS of Trainkos resulted in 19 key recommendations. Trainkos prepared an Action Plan stating how given recommendations will be implemented.

Compared to the previous year, a more serious approach and a higher commitment to address issues and recommendations stemming out from the previous audit report, where around 74% of them are implemented or are in process. By the end of our audit, the implementation of the 2016 recommendations was as follows: 7 (seven) recommendations were implemented, 7 (seven) were in process of implementation and 5 (five) have not yet been implemented.

While, , out of six recommendations covering 2015 given by the external auditor only one was not implemented. For a more thorough description of the recommendations and how they are addressed, see Annex II.

Issue 11 – Implementing Prior and Earlier Year Recommendations

Finding	Despite the progress shown in the implementation of the recommendations, most of the unimplemented recommendations relate to areas that have impacted the audit opinion, such as receivables, non-current assets, reserve assets and explanatory notes.
Risk	Failure to implement the recommendations, especially those that have impacted the audit opinion in the previous year, may result in a modification of the opinion in the audit report for the following year. While failure to implement other recommendations increases the risk of continued presence of the same shortcomings, which may affect both financial management and control weaknesses.
Recommendation 11	The Chairman of the Board should ensure that the action plan for the implementation of the recommendations is being monitored on a regular basis and is being implemented in line with the deadlines set. The main focus should be recommendations that have an impact on the opinion and affect the most important areas of financial management and control.

5 Good Governance

Introduction

Specific areas of our governance related reviews have been the internal audit, accountability and risk management process, while the other components are handled within the chapters or subchapters above.

Overall Governance Conclusion

Trainkos generally has good controls in relation to its statutory obligations. In relation to the previous year, the management made significant improvements in good governance. We aknowledge the progress made in drafting the risk management plan as well as reviewing the business plan according to legal requirements.

However, to support an effective management of the enterprise, a number of governance processes need to be further improved: functionalizing the internal audit unit and clear division of duties according to the organizational structure.

5.1 Internal Audit System

Internal Audit is an independent activity to provide objective assurance and advisory activity, designed to add value and to improve the operations of the enterprise. It also helps the enterprise to meet the objectives by promoting a systematic and disciplined approach to assessing and improving the effectiveness of risk management, controls and governance processes.

Issue 12 - Non-Functioning of the Internal Audit Unit

Finding	The Internal Audit Unit (IAU) since March 2017 had no internal auditor in place, due to his resignation. During 2017, the Enterprise had announced three times the vacancy to cover the position for internal auditor. In the first occasion, it failed due to the lack of qualified candidates according to the requirements of the competition. Then in the other two occasions, it failed to complete this position due to the incomplete audit committee, which, with effect from 21.09.2017 (when the Chairman resigned) remained with only two members. However, even after completing the audit committee, this position had not yet been completed (until the end of the audits on 01.06.2018).
Risk	Non-functioning of IAU increases the risk that due to the complexity and size of the enterprise, senior managers have difficulty controlling its processes and operations effectively. This may result in unidentified weaknesses and the continuation of ineffective practices that may end up in poor controls and financial losses for the enterprise.
Recommendation 12	The Chairman of the Board should ensure that the enterprise functions effectively and an internal auditor is selected according to legal requirements to assist management in evaluating internal controls within the Enterprise.

5.2 Management Reporting, Accountability and Risk Management

Accountability as a process is the acceptance of responsibilities, holding persons into account for their actions and disclosing results in a transparent way. Whereas, risk management is a process related to identification, analysis, evaluation and actions/measures taken by the Management to control and respond to risks threatening the Organization.

Following our recommendations, the management of the Enterprise had taken the necessary actions by providing a risk management plan and reviewing and completing the content of the business plan with all legal requirements.

The Enterprise implemented a number of controls that include the management and organization of operational activities. While controls in some areas have operated relatively well, irregularities have been encountered in the segregation of duties.

Issue 13 – Improper segregation of duties

Finding	Trainkos has established its organizational structure, but failed to clearly segregate duties. It is a requirement of a Regulation on the management of non-current assets (Article 4.7) for the enterprise to appoint an asset officer or the duties of the Asset officer may be only part of the full work in the Enterprise. Trainkos except that did not have an Asset Officer, did not secure proper segregation of duties and clarify delegated responsibilities regarding the duties of the Asset officer. The duties of the Asset officer were performed by the Finance Officer. The lack of an Asset Officer is due to the appointment of a former Asset officer as a certifying Officer.
Finding	improper Authorization and segregation of duties and responsibilities reduce effective control and management's ability to effectively manage non-current assets. Further on, this risks their loss and the presentation of financial statements with inaccuracies.
Recommendation 13	The Chairman of the Board should make a review of the existing arrangements for proper segregation of duties for the management of non-current assets.

Annex I: Explanation of the different types of opinion applied by NAO

(extract from ISSAI 200)

Form of opinion

147. The auditor should express **an unmodified opinion if** it is concluded that the financial statements are prepared, in all material respects, in accordance with the applicable financial framework.

If the auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement, or is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement, the auditor should modify the opinion in the auditor's report in accordance with the section on "Determining the type of modification to the auditor's opinion".

148. If financial statements prepared in accordance with the requirements of a fair presentation framework do not achieve fair presentation, the auditor should discuss the matter with the management and, depending on the requirements of the applicable financial reporting framework and how the matter is resolved, determine whether it is necessary to modify the audit opinion.

Modifications to the opinion in the auditor's report

151. The auditor should modify the opinion in the auditor's report if it is concluded that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement, or if the auditor was unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement. Auditors may issue three types of modified opinions: a qualified opinion, an adverse opinion and a disclaimer of opinion.

Determining the type of modification to the auditor's opinion

152. The decision regarding which type of modified opinion is appropriate depends upon:

- The nature of the matter giving rise to the modification – that is, whether the financial statements are materially misstated or, in the event that it was impossible to obtain sufficient appropriate audit evidence, may be materially misstated; and
- The auditor's judgment about the pervasiveness of the effects or possible effects of the matter on the financial statements.

153. The auditor should express a **qualified opinion if**: (1) having obtained sufficient appropriate audit evidence, the auditor concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or (2) the auditor was unable to obtain sufficient appropriate audit evidence on which to base an opinion, but concludes that the effects on the financial statements of any undetected misstatements could be material but not pervasive.

154. The auditor should express an **adverse opinion if**, having obtained sufficient appropriate audit evidence, the auditor concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

155. The auditor should **disclaim an opinion if**, having been unable to obtain sufficient appropriate audit evidence on which to base the opinion, the auditor concludes that the effects on the financial statements of any undetected misstatements could be both material and pervasive. If, after accepting the engagement, the auditor becomes aware that management has imposed a limitation on the audit scope that the auditor considers likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor should request that management remove the limitation.

156. If expressing a modified audit opinion, the auditor should also modify the heading to correspond with the type of opinion expressed. ISSAI 1705[19] provides additional guidance on the specific language to use when expressing a modified opinion and describing the auditor's responsibility. It also includes illustrative examples of reports.

Emphasis of Matter paragraphs and Other Matters paragraphs in the auditor's report

157. If the auditor considers it necessary to draw users' attention to a matter presented or disclosed in the financial statements that is of such importance that it is fundamental to their understanding of the financial statements, but there is sufficient appropriate evidence that the matter is not materially misstated in the financial statements, the auditor should include an Emphasis of Matter paragraph in the auditor's report. Emphasis of Matter paragraphs should only refer to information presented or disclosed in the financial statements.

158. An Emphasis of Matter paragraph should:

- be included immediately after the opinion;
- use the Heading "Emphasis of Matter" or another appropriate heading;
- include a clear reference to the matter being emphasised and indicate where the relevant disclosures that fully describe the matter can be found in the financial statements; and
- indicate that the auditor's opinion is not modified in respect of the matter emphasised.

159. If the auditor considers it necessary to communicate a matter, other than those that are presented or disclosed in the financial statements, which, in the auditor's judgement, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report, and provided this is not prohibited by law or regulation, this should be done in a paragraph with the heading "Other Matter," or another appropriate heading. This paragraph should appear immediately after the opinion and any Emphasis of Matter paragraph.

Annex II: Progress in implementing Prior and Earlier Year recommendations

Audit Component	Recommendation carried forward from 2015	Implemented during 2017	Under implementation during 2017	Not implemented
1. Financial Statements - Assets	The Auditor recommends that the company creates accurate and complete register for each asset separately including all expenses incurred for significant repair or maintenance so that at every time we have a full and objective coverage for each asset separately.	Implemented		
2. Statement of financial position - Assets	The auditor recommends that you make frequent reconciliations with your clients and harmonize the notes so that the values match fully. At least before the financial statements are closed, you should harmonize your notes with the resulting amounts in the accounting records of your customers.	Implemented		
3. Statement of financial position - Liabilities - Share capital	During the auditing process, the notes of the underlying capital and those of the accumulated and unallocated profits are not reflected separately but accumulated in a single account with the term "Opening Balance" at which moment no performance of the company's financial results is seen in perspective. This finding was also noticed in the 2014 statements and the auditor's recommendation remains in force.	Implemented		
4. Statement of financial position - Liabilities - Other payables and trade	The auditor recommends that after the closing of the financial statements at the end of the reporting period, the items of other trade receivables and other and trade payables should be handled according to the obligation or request relation and not by class or group of accounts. (Additional clarification)	Implemented		

	If a buyer has made a prepayment to be handled as an obligation towards buyers rather than being broken by the value of other buyers to which the company has claims, the same applies to suppliers.			
5. Comprehensive income statement	During the audit process, we have come across non-compliances with various sources of assertion in relation to: 'Comprehensive Company Revenue' since the assertions for receipts in the verifying balance respectively in the "Comprehensive Income Statement" do not fully correspond to the revenues from VAT tax declarations, but the same phenomenon was also noticed in the statements of operating expenses reflected in BV, respectively in PAGJ.P. which do not correspond fully with the notes of the purchases which belong to the operating expenses of the company, and which are reflected in the tax returns for VAT. This finding was also noted during the audit of the 2014 financial statements, and the auditor's recommendation remains the same.	Implemented		
6. Purchase by applying minimum procedures	The contracting authority should avoid the frequent use of minimum procedures and use open procedures for the purpose of equal treatment, promotion of competition and achievement of quality through value for money principle.			Not implemented

Audit component	Recommendations given in 2016	Implemented	In process of implementation	Not implemented
1. Financial Statements	1. The Chairman of the Board should ensure that an analysis has been carried out to determine the causes which have affected in Disclaimer of the Opinion. Actions need to be taken to address the causes in a systematic and pragmatic manner to remove errors in the annual financial statements and ensure a true and fair view.			Not implemented, there are still material errors in AFS of 2017
	2. The Chairman of the Board should also ensure that effective processes have been established to confirm that the AFS 2017 drafting plan addresses all compliance related issues. This should include the review of the draft of the AFS by Management, with particular focus on high risk areas and/or areas where errors in previous years have been identified. AFS should be approved if all the necessary controls have been applied to the draft.			Not implemented
Good Governance	3. The Chairman of the Board should ensure the action plan is implemented, which sets the time limits for the implementation of the recommendations given by the External Auditor with the responsible staff identified, focusing primarily on the most important areas. The reasons for not addressing prior year recommendations should be considered with the relevant directors and reported to the Chief Executive Officer.		Out of the six recommendations given in 2015, only one was not implemented.	
	4. The Chairman of the Board should ensure that the business plan, along with business goals and approach to their implementation, also contains the timeframes for their execution.	Implemented		

	5. The Chairman of the Board should consider the reasons for not applying the controls effectively in the areas mentioned above and ensure their elimination in order to improve these weaknesses.		The Management of the enterprise had taken the necessary actions regarding the strengthening of the controls. However, in some areas controls were not effective.	
Internal Audit	6. In order to achieve the maximum benefit from internal audit activity, the Chairman of the Board of Directors should ensure that the Audit Committee critically reviews the internal audit plans, the execution of the plan, the results and the quality of the audit reports. It should also review the actions taken by management in relation to internal audit recommendations			Not implemented. The Internal Audit Unit (IAU) in Trainkos since March 2017 is not functional. This is due to the fact that the Internal Auditor has resigned.
Cost of Service	7. The Chairman of the Board of Directors should ensure that only those costs that are related to the cost of the service are included within the cost of the service, while other expenses are recognized as expense of the period.	Implemented		
Revenues	8. The Chairman of the Board should ensure that revenues are monitored systematically and any changes or deviations from the initial plans are reflected in the revenue plan.	Implemented		
	9. The Chairman of the Board should take measures to ensure that the recording of revenues is timely made, maintain a register of paid and unpaid invoices by customers and in case of customer delays, apply penalties.			Not implemented

Wages and Salaries	10. The Chairman of the Board should review identified shortcomings and take the necessary measures to comply with the relevant legal provisions in the case of new staff commitments, as well as posts with operational responsibilities should be exercised by officials/employees with regular employment contracts .		A part of the findings related to this recommendation has not yet been implemented.	
Expenditures	11. The Chairman of the Board should ensure that controls are enhanced so that all costs are verified and approved by the Certifying Officer prior to recording in the accounting system.	Implemented		
	12. The Chairman of the Board should ensure that the certifying officer verifies the costs under the contract and for the part paid more request the return of funds to the enterprise budget.	Implemented		
	13. The Chairman of the Board should ensure appropriate measures to adhere to public procurement rules and exercise appropriate management oversight.	Implemented		
Non-current assets	14. The Chairman of the Board should produce an internal regulation defining the standard procedures for the management of non-current assets and ensure that assets are handled under IAS and the rules in force, presenting their fair value in the AFS.		The enterprise has drafted a regulation on asset management, but the value of assets presented in the AFS was incorrect.	
Current Assets	15. The Chairman of the Board should ensure that requests for financing official travel are evaluated in accordance with applicable regulations and funded only when appropriate criteria are met.	Implemented		
Equity	16. The Chairman of the Board should ensure that the necessary corrections are made by setting up a review mechanism to confirm the accuracy of the amounts entered in the accounts and to present them to the AFS.		Retained earnings were reversed, but the retained capital was not corrected.	

	17. The Chairman of the Board and the Chief Executive Officer should draft a strategic plan for sustainability and business improvement that should be compulsory in practice.		The enterprise has not developed any strategic plan although this year has operated profitably.	
Payables	18. The Chairman of the Board of Directors should ensure that the accounting records are harmonized with the suppliers, while the negative values are treated and recorded in the appropriate accounting records.			Not implemented
Explanatory notes	19. The Chairman of the Board of Directors should ensure that, when AFS are prepared, in the notes, detailed and complete information is provided for each item in the financial statements.		Explanatory notes this year were more complete, but some shortcomings were identified.	

Annex III: POE's comments on the findings of the audit report

Findings/Issues	Agree Yes/No	Comments from the BO in case of disagreement	NAO view
Basis for Opinion - Item 1.	No	Based on the audit recommendations from the previous year that the financial statements should present a more realistic situation, we prepared the action plan and took concrete steps regarding the receivables. The amount of receivables from €523,232 relates to the period 2002-2011 carried forward by the dividing report of Kosovo Railways. These old-age debts do not meet the legal criteria for bad debt pursuant to Law no. 05/L-029 on Corporate Income Taxes and as such they were not allowed by TAK to be recorded as an expense in the income statement, therefore we have decided that these should be debited in the company's capital. These debts have not been forgiven and it is consistently requested by the staff of the enterprise to aim to collect them. According to paragraph 3.4 of Article 12 of Law no. 05/L-029 on Corporate Income Tax, if a certain amount has not been received within 24 months from the date of the payment obligation, then it cannot be considered as bad debt, quote: *"3. Uncollected amount will not be considered a bad debt if:* *3.1. transactions with the same debtor were repeated after the announcement of bad debt, with the exception of public services;* *3.2. bad debt is between related parties;*	The Annual financial statements should be prepared in accordance with International Accounting Standards and International Financial Reporting Standards. As defined by Law 04/L-014 on Accounting, Financial Reporting and Auditing. Trainkos recorded bad debts when recording within accounting registers in accordance with the requirements of the abovementioned standards. While TAK requirements for bad debts apply only for tax purposes, but not for financial reporting purposes. Finding and recommendation of the Auditor remain.

		3.3 there is insufficient evidence that substantial efforts have been made to recover the debt, including any action to maximize debt collection; ***3.4. twenty-four months (24) months have passed from the date of the payment obligation."*** Under the legal definition given above, while debts cover the period 2002-2011, then they cannot be considered as bad debts and as such are not recognized in the Income Statement as an expense.	
Basis for Opinion - Item 4	No	The stock difference was the result of incorrect registration in the Kosovo Railways dividing report, where it was transferred from 2011 to 2016. After registering the stocks (including spare parts) for 2016 we have noticed that the difference in the amount of 96,732 was a value to be cancelled because **they do not exist and we have no arguments that we have stocks of this value in possession.** Stocks are part of the current assets in the Statement of Financial Position (Balance Sheet) in the position of assets and as such depending on the stock value as it is showing the largest capital of the enterprise and vice versa. Therefore, in this value of stocks, we have deducted from (capitalized) the capital to give a true statement of the enterprise's assets/capital and not include as an expense in the income statement, an expense that does not exist.	In the case of ascertaining the difference between the stock and the accounting records, these differences in accounting should be recognized as expenses and are not allowed to be closed with capital. Therefore, Finding and recommendation of the Auditor remain.

Basis for Opinion - Item 6		Profit is an accurate financial result and we in point 1 of this appendix have explained that: under paragraph 3.4 of Article 12 of Law no. 05/L-029 on Corporate Income Tax clarifies that debts older than two years are not considered as bad debts and as such cannot be included in the statement of income as expenses.	The Annual financial statements should be prepared in accordance with International Accounting Standards and International Financial Reporting Standards. As defined by Law 04/L-014 on Accounting, Financial Reporting and Auditing. Trainkos recorded bad debts when recording within accounting registers in accordance with the requirements of the abovementioned standards. While TAK requirements for bad debts apply only for tax purposes, but not for financial reporting purposes. Finding and recommendation of the Auditor remain.