



REPUBLIKA E KOSOVËS / REPUBLIKA KOSOVA / REPUBLIC OF KOSOVA

**ZYRA KOMBËTARE E AUDITIMIT
NACIONALNA KANCELARIJA REVIZIJE**

NATIONAL AUDIT OFFICE

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AUDIT REPORT

**ON THE ANNUAL FINANCIAL STATEMENTS OF PEJA
MUNICIPALITY FOR
THE YEAR ENDED 31 DECEMBER 2016**

Prishtina, jun 2017

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 to contribute to sound financial management in the public administration. 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 report on the Annual Financial Statements of Peja Municipality in consultation with the Assistant Auditor General, *Qerkin Morina*, who supervised the audit.

The opinion and report issued are a result of the audit carried out by *Edon Kabashi* (team Leader) *Pleurat Isufi* and *Mehmet Kurti* (team members) under the management of the Head of Audit Department, *Astrit Bllaca*.

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Executive Summary

Introduction

This report summarises the key issues arising from our audit of the 2016 Annual Financial Report of Peja Municipality, which determines the Opinion given by the Auditor General. The examination of the 2016 financial statements was undertaken in accordance with the International Standards on Supreme Audit Institutions. 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 Plan¹ dated 19.10.2016.



(For more details, see Annex 1)

The level of work undertaken by the National Audit Office to complete the 2016 audit is a direct reflection of the quality of internal controls implemented by the Management of the Municipality.

Opinion of the Auditor General

Unmodified Opinion with emphasis of matter

In our opinion, the Annual Financial Statements *present a true and fair view* in all material aspects.

Emphasis of matter

As an emphasis of matter, we would like to draw your attention to the fact that the Municipality's assets were understated by €5,254,200 and property tax accounts receivable were overstated by €545,629 whilst those from business activities were understated by €209,520.

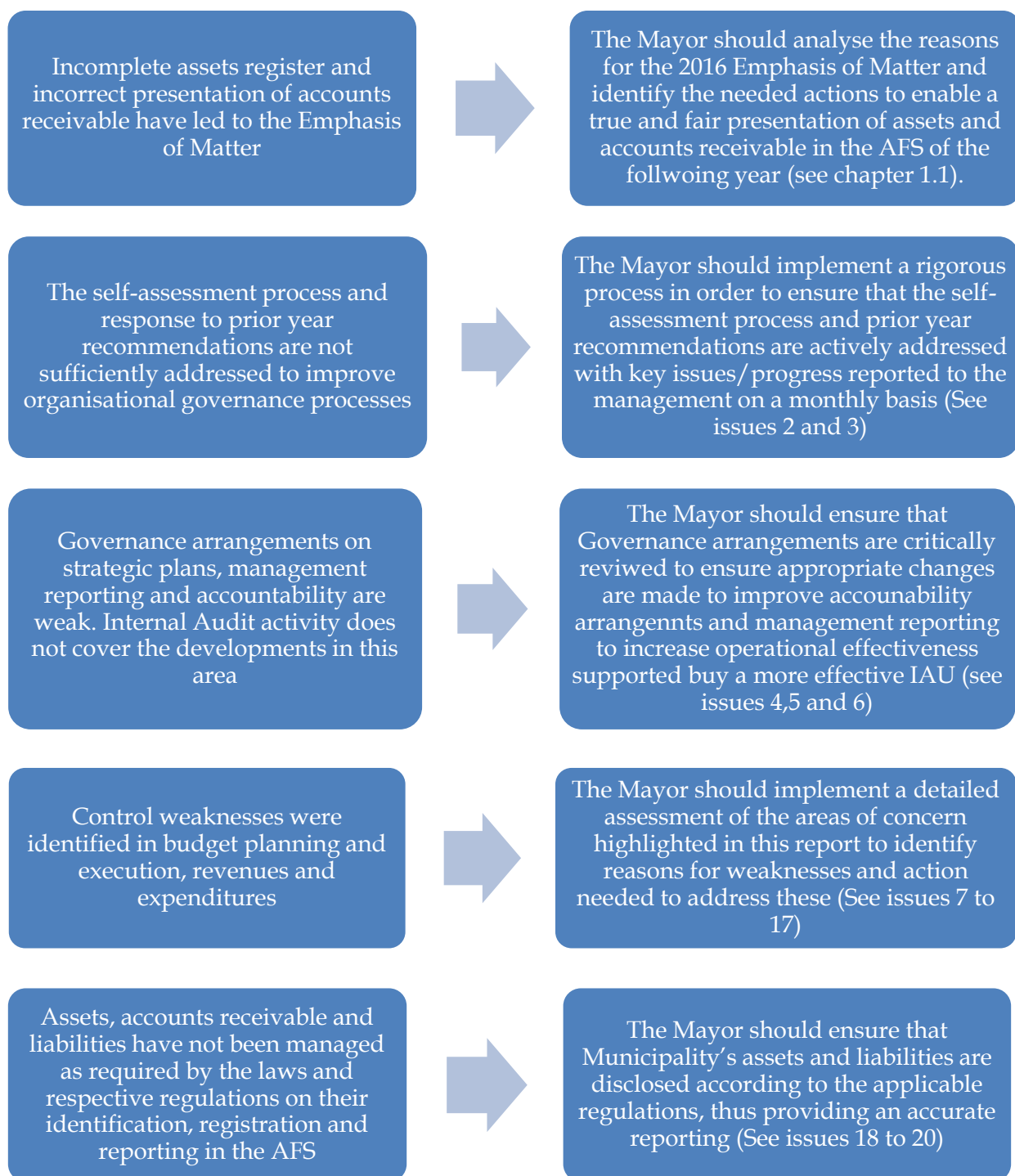
For more details, see Section 1.1 of this report.

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

We would like to thank the Mayor and his staff for the cooperation during the audit process.

¹ The term External Audit Plan replaces the term Audit Planning Memorandum

Key Conclusions and Recommendations



Mayor's Response

The Mayor has considered the detailed audit findings and conclusions in this report and has committed to address all given recommendations. In addition, the Mayor is committed to:

- discuss the audit report in the Municipal Assembly; and
- by the end of January 2018, he shall discuss in the Municipal Assembly about the progress in the implementation of audit recommendations Action Plan before the annual financial statements of 2017 are submitted to the Ministry of Finance

1 Annual Financial Statements and other External Reporting Obligations

Introduction

Our review of the Annual Financial Statements (AFS) considers both compliance with the reporting framework and the quality and accuracy of information recorded in the AFS. We also consider the Declaration made by the Chief Administrative Officer and Chief Financial Officer when the draft AFS are submitted to the Ministry of Finance.

The declaration regarding presentation of the AFS incorporates a number of assertions relating to compliance with the reporting framework and the quality of information within the AFS. These declarations are intended to provide the Government with the assurance that all relevant information has been provided to ensure that a comprehensive audit can be undertaken.

1.1 Audit Opinion

Unmodified Opinion with Emphasis of Matter

We have audited the AFS of the Peja Municipality for the year ended on 31st December 2016, which comprise of the Statement of Cash Receipts and Payments, Budget Execution Statement and the Explanatory Notes of the Financial Statements.

In our opinion, the Annual Financial Statements for the year ended on 31st of December 2016 present a true and fair view in all material respects in accordance with International Public Sector Accounting Standards (cash based Accounting), Law no.03/L-048 on Public Finance Management and Accountability (as amended and supplemented) and Regulation no.01/2017 on Annual Financial Reporting of Budget Organisations issued by the Ministry of Finance.

Basis for the opinion

We conducted the audit 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. We believe that the obtained audit evidence is sufficient and appropriate to provide a basis for the opinion.

Emphasis of Matter

We draw your attention to the fact that:

Municipality's assets over €1,000 acquired during 2015 were not fully recorded in the assets accounting register. The value declared by the Municipality, not recorded in KFMIS, was €3,981,660.

While testing capital investment payments for 2016, we found that 42 payments totalling €1,272,540 were not recorded in the Assets Register (KFMIS). The municipal administration building, schools and health facilities were not included in the asset register because they have no financial value. The Municipality did not evaluate these assets through the evaluation commission.

The closing balance of property tax accounts receivable in the 2016 AFS was €8,963,320 whilst according to datas from department of property tax Protax the value of accounts receivable for 2016 was €8,417,691. This shows that property tax accounts receivable presented in the AFS were overstated by €545,629.

Based to the Law no.05/L-043 on Public Debt Forgiveness, the Municipality has forgiven business organisations for the debts they have been charged from 2002-2008 provided that they pay off their debts for the years 2009-2012. The forgiven amount of debts for 2016 was €209,520. The law does not foresee the forgiveness of debts from business tax. This has also resulted in the understatement of accounts receivable for the same amount.

Responsibility of Management and Those Charged with Governance and AFS

The Mayor of the Peja Municipality is responsible for the preparation and fair presentation of financial statements in accordance with International Public Sector Accounting Standards – Financial Reporting under the Modified Cash based 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 number 03/L-048 on Public Finance Management and Accountability (as amended and supplemented).

The Mayor is responsible to ensure oversight the Municipality's financial reporting process.

Auditor General's Responsibility for the Audit of the AFS

Our responsibility is to express an opinion on the AFS based on our audit. We conducted our audit in accordance with ISSAIs. These standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could influence the decisions taken on the basis of these AFS.

An audit involves performing procedures to obtain evidence about the financial records and disclosures in the AFS. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement in the AFS, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial statements in order to design audit procedures that are appropriate in the entity's circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Management, as well as evaluating the presentation of the financial statements.

1.2 Compliance with AFS and other reporting requirements

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

- Compliance with MoF Regulation no.01/2017 on the Annual Financial Reporting of Budget Organisations;
- Requirements of LPFMA no.03/L-048, as amended and supplemented;
- Compliance with Financial Rule no.01/2013;
- Compliance with Financial Rule no.02/2013;
- Action Plan on implementation of recommendations;
- Requirements of Financial Management and Control (FMC) procedures;
- Submission of regular quarterly reports to the Municipal Assembly; and
- Draft and Final Procurement Plans in time..

Issues raised in the Memorandum of Understanding dated 29.11.2016 regarding the reporting framework were partially addressed by the Management.

A number of financial adjustments were required to the draft AFS of 2016 and we made suggestions to improve them. The Management has considered our suggestions and improved the final AFS, except for the issues presented in sub-chapter 1.1 Audit Opinion. In the context of the AFS we have no issues to raise regarding the reporting framework, except for the issue regarding the CFO who did not report on physical progress of capital investments because the recorded data were not saved by the PIP system.

DECLARATION BY THE MUNICIPALITY MANAGAMENT

Given the above, the Declaration made by the Chief Executive Officer and Chief Financial Officer when the draft AFS are submitted to the Ministry of Finance can be considered to be incorrect when it comes to the disclosure of assets and accounts receivables.

1.3 Recommendations for the first part of the report

In the regard to the issues presented above, the following recommendation is given:

Recommendation 1 The Mayor should ensure that an analysis is undertaken to determine the causes of the Emphasis of Matter. Actions should be taken to address the underlying causes in a systematic manner to record all capital assets and to ensure the correct presentation of accounts receivables. The declaration made by CAO and CFO should not be submitted unless all necessary checks are applied to the draft AFS.

2 Governance

Introduction

Effective governance arrangements are fundamental to the Municipality for successfully managing the challenges it faces and ensuring that service delivery is optimised for the benefit of taxpayers and other service users.

A key tool supporting effective Governance is the implementation of audit recommendations as this demonstrates that Management are seeking to develop existing processes and controls. Similarly, the self-assessment checklist provides a framework for developing enhanced Governance arrangements. It is important that the answers provided by the Municipality are supported by appropriate evidence.

The rest of the review of governance arrangements reflects a consideration of:

- those areas of governance arrangements where significant improvements are required and where we believe that our recommendations can generate positive improvements including consideration of the Internal Audit system; and
- areas of Financial Management and Control identified through our audit work including specific work directed at compliance issues in key income and expenditure systems (these areas are considered in Section 3 of this report)

Overall Governance Conclusion

There is a number of control weaknesses in municipality governance, particularly related to accountability, risk management and quality of management reporting. The self-assessment checklist completed by the Municipality only partially reflects this situation with some positive comments on existing non-evidence based arrangements.

A key tool supporting effective governance is the implementation of audit recommendations. Implementation of prior year recommendations was not at a satisfactory level. Only four (4) out of 18 given recommendations were fully implemented.

Peja Municipality has a three year development strategy (2015-2017) in place but responsibilities for the coordination and implementation of this strategic plan were not clearly stated and its implementation costs were not calculated either.

Internal Audit has provided a clear overview of the internal controls assurance level and has given recommendations to improve them.

In 2016, the Municipality used 94% of the final budget, an improvement of 20% compared to the previous year. This shows a positive trend of budget management.

2.1 Progress in Implementing Prior Year Recommendations

Our Audit Report on the 2015 AFS resulted in 18 recommendations. The Municipality prepared an Action Plan stating how all recommendations will be implemented. By the end of the 2016 audit period, four (4) recommendations were implemented, eight (8) were under implementation and six (6) have not been addressed yet. The audit report of 2015 AFS was discussed in the Municipal Assembly.

For a more thorough description of the recommendations and how they are addressed, see Annex III.

Issue 2 – Implementation of Prior Year Audit Recommendations – High Priority

Finding Only a proportion of prior year recommendations have been addressed because Peja Municipality has not implemented any formal process to manage and monitor the way AG’s recommendations are implemented.

Risk The continued weaknesses of management and other controls in key financial systems have resulted in:

- Incomplete assets register;
- Weaknesses in overall governance; and
- Over/under statement of accounts disclosed in the statements.

Risk Continued weaknesses of management controls over key financial systems and in other areas of activity have resulted in failure to fully implement prior year recommendations. The municipal management may thus not be able to meet its organisational objectives with quality, which would have an impact on the quality of services to the citizens.

Recommendation 2 The Mayor should ensure that a strengthened process of accountability is applied towards the staff in charge with the implementation of recommendations within timeline and priorities set in the action plan. Implementation progress should be monitored systematically and where setbacks are identified adequate measures should be taken.

2.2 Self-Assessment Checklist of FMC components

The Ministry of Finance has produced a detailed self-assessment checklist for Budget Organisations to support effective governance arrangements. We have tested the quality of FMC self-assessment submissions made to the Ministry by assessing one key question in each component of the checklist. We have summarised our findings for the Municipality. Our considerations are not intended to give a commentary on the quality of the whole self-assessment questionnaire submission but will provide a 'snapshot' across a number of key questions to support the Ministry of Finance in its attempts to increase the effectiveness of the process and develop the FMC system as a whole.

Issue 3 - Self Assessment Checklist - High Priority

Finding	<p>As part of our audit we have considered key questions related to the five components of the self-assessment checklist. For the questions considered we found that:</p> <ol style="list-style-type: none">1. The Self-Assessment questionnaire completed by Peja Municipality acknowledged that required risk management systems were not yet operational. This situation has arisen because the Municipality did not produce the list of risks;2. Peja Municipality has a three (3) year development strategy (2015-2017) in place but responsibilities for the coordination and implementation of this strategic plan were not clearly stated and its implementation costs were not calculated. Issues related to strategic plans are presented in details in sub-chapter 2.3.1;3. Links between the procurement plan and budget and the production of adequate reports on a timely basis are considered in place by the Municipality and the evidence we were provided with support this conclusion although weaknesses were identified in the procurement plan which did not include all purchases made from Goods and Services. Moreover, reports were not always produced on a timely basis;4. Internal Audit did not highlight the above issues. Furthermore, the action taken to address issues identified in the 2016 self-assessment checklist is limited. This situation has occurred because of a lack of clarity within the Municipality regarding both the importance of this checklist and who is the responsible officer for using it to support operational improvements.
Risk	<p>Poor governance arrangements weaken strategic and operational processes and reduce the quality of services provided to citizens through inefficient and ineffective activities.</p>

Recommendation 3 The Mayor should ensure that a review of the quality and completeness of the self-assessment checklist is implemented and that areas of weaknesses are proactively addressed. A mechanism to confirm the accuracy of the return and to ensure supporting documentation should be applied.

2.3 Specific Governance Reviews

Our work on specific areas of governance arrangements has been informed by our audit planning which considered the context within which the Municipality of Peja operates and the challenges that it faces.

2.3.1 Setting of Strategic Objectives

All Budget Organisations are obliged to prepare and submit organisation level strategic plans. The Municipality owns some of these documents such as: Municipal Governance and Development Strategy for 2015-2017, Strategic Spatial Plans and Strategic Urban and Regulatory Plans.

Issue 4 – Challenges in drafting, approval and implementation of strategic plans – High Priority

Finding Upon USAID initiative, an emergency operational draft plan was drafted for the 2015-2017 period, but it was not sent yet to the Municipal Assembly for approval;

The Regional Development Strategy was produced but it covered the 2010-2013 period. It was not updated.

The Anti-Corruption Strategic Plan was not prepared but it was included as an integral part of the produced Integrity Plan for 2017-2020; and

The Municipality has a three year development strategy (2015-2017) in place but responsibilities for the coordination and implementation of this strategic plan were not clearly stated and its implementation costs were not calculated. The strategy monitoring and assessment plan was not implemented either.

Risk Lack of strategic plans and failure to have them approved by the Municipal Assembly undermines the prioritisation of issues vital to development and the welfare of its citizens. Failure to appoint the persons responsible for the coordination and implementation of the strategic plan makes the follow up on objectives' achievement impossible in the light of the Municipality's vision, as one of the essential requisites of good governance.

Recommendation 4 The Mayor should initiate drafting strategic plans with clear strategic objectives set and propose them to the Municipal Assembly for approval. He should also ensure the oversight and measurement of implementation of such objectives.

2.3.2 Management Reporting and Accountability

A range of internal controls are applied by Management to ensure that financial systems and operational activities operate as intended. It is important that these include appropriate reporting to management to enable an effective and timely response to identified operational problems.

Issue 5 – Weaknesses in Management Controls – High Priority

Finding Our review of the management controls applied to the Municipality’s key financial system highlighted poor financial reporting of expenditure and revenue to senior management and incomplete analyses on service delivery. Internal reporting process has resulted in a number of weaknesses which limit the effective management. Responsibilities are limited and not implemented as intended.

Risk Poor quality of financial and activity reporting to senior management has reduced the management’s ability to proactively manage the operations of the Municipality and undermines effective budgetary control. This can result in unplanned over or under spending and delay necessary actions to address these. It may also result in revenues not collected as expected. Similarly, it may result in poor quality service delivery.

Recommendation 5 The Mayor should ensure that a review is implemented to determine the format of financial and operational reporting to senior management which is required to provide effective business management. Budget developments should be continuously monitored in order to prevent any underspending at the yearend and increase the collection level.

2.4 Internal Audit System

In 2016, the Internal Audit Unit (IAU) planned 11 audits and has fully implemented its annual plan. just two audits for 2016. IAU has given 51 recommendations out of which 35 were implemented, five (5) were partially implemented and 11 were not implemented at all. The impact of IA output should be judged by the importance that management places on addressing recommendations and the support and challenge provided by an effective Audit Committee. In this regard, the Municipality has implemented most of the recommendations in a disciplined manner.

However, there are some issues that need to be addressed in order to further strengthen internal audit function, these are the following:

Issue 6 - Poor functioning of Audit Committee - High Priority

Finding During 2016, the Audit Committee held four meetings, but two of the members did not attend them. The Chairman of the Audit Committee missed the third and fourth meetings. The AC discussed about the internal audit reports, but it did not ask the management to implement the IAU recommendations. The Management did not prepare the plans on the implementation of IAU recommendations.

Risk The Audit Committee's work with limited capacities may reduce the IAU's oversight ability and undermines further strengthening of internal audit's role.

Recommendation 6 The Mayor should ensure that the IAU and Audit Committee operate in full capacities in order to gain maximum benefits of internal audit services.

3 Financial Management and Control

Introduction

Our work on Financial Management and Control (FMC) outside of the Governance areas referred to above reflects the detailed work undertaken on Revenue and Expenditure Systems. As part of this, we consider Budget management, Procurement and Human Resources issues, and Assets and Liabilities.

Financial Management and Control Conclusion

Procurement still remains the Municipality's major concern because regulations have not been sufficiently enforced with resultant poor value for money being achieved and delays in project implementation. In the context of financial systems, controls over revenues are generally not sufficiently effective and not properly applied. Controls over other areas of expenditures require further enhancement to prevent shortcomings and to add value for money.

3.1 Budget Planning and Execution

We have considered the sources of budgetary funds, spending of funds by economic categories and collected revenues. This is highlighted in the following tables:

Table 1. Own source revenues(in €)

Description	Initial Budget	Final Budget	2016 Receipts	2015 Receipts	2014 Receipts
Own Source Revenues	3,452,687	3,452,687	3,470,858	3,337,518	3,271,418
Total	3,452,687	3,452,687	3,470,858	3,337,518	3,271,418

In 2016, planned revenues were approximately the same as the executed ones. Receipts include revenues of €454,057² from traffic fines and court penalties collected from central institutions.

Own source revenues of €3,452,687 were allocated to cover expenditures for the Municipality's needs. Out of this amount, €2,841,727 were spent, whilst the remaining of €175,075 were carried forward to 2017. The total of unspent own source revenues was €630,228. Collection of revenues for 2016 reflects an increase of €133,340 or around 4% compared to the previous year.

² Traffic fines of €150,108.5 from Kosovo Police and penalties of €303,948 from Courts.

Table 2. Sources of budgetary Funds (in €)

Description	Initial Budget	Final Budget ³	2016 Outturn	2015 Outturn	2014 Outturn
Sources of Funds	20,717,792	23,384,361	22,047,434	21,146,160	20,536,683
Government Grant - Budget	17,265,105	17,498,949	17,496,799	17,984,147	17,232,343
Carried forward from previous year ⁴ -	0	1,183,637	728,484	648,492	659,067
Own Source Revenues ⁵	3,452,687	3,452,686	2,841,727	2,217,268	2,566,106
Domestic Donations	0	684,790	472,244	50,640	0
External Donations	0	564,299	508,180	245,613	79,167

The final budget was higher than the initial budget by €2,666,569 as a result of the Government grant of €233,843, own source revenues of €1,183,637 carried forward from previous year, internal donations of €684,790 and external donations of €564,299.

In 2016, the Municipality used 94% of the final budget or €22,047,434, an improvement of 4% compared to 2015. However, the budget execution in Capital Investments remains at an unsatisfactory level and explanations for the current position are detailed below.

Table 3. Spending of funds by economic categories - (in €)

Description	Initial Budget	Final Budget	2016 Outturn	2015 Outturn	2014 Outturn
Spending of funds by economic categories	20,717,792	23,384,361	22,047,434	21,146,160	20,536,653
Wages and Salaries	12,965,868	13,235,378	13,213,466	13,002,566	11,925,237
Goods and Services	2,420,000	2,572,602	2,559,607	2,262,418	2,260,801
Utilities	671,924	671,707	664,499	606,154	528,460
Subsidies and Transfers	250,000	257,628	248,570	359,212	428,300
Capital Investments	4,410,000	6,647,046	5,361,292	4,915,810	5,393,855

Explanations on changes in budget categories are the following:

- The budget of Wages and Salaries increased by €269,510 as a result of Government's decision;

³ Final budget - the budget approved by the assembly which was subsequently adjusted for by the Ministry of Finance.

⁴ Own Source Revenues unspent in previous year carried forward into the current year.

⁵ Receipts used by the entity for financing its own budget.

-
- The budget in Goods and Services increased by €152,602 as a result of own source revenues of €112,012 and donors grants of €40,590;
 - The budget of Subsidies and Transfers increased by €7,628 as a result of own source revenues; and
 - The budget for Capital Investments increased by €2,237,046 as a result of Government's decision by €16,731, own source revenues by €1,036,696 and donors grants by €1,183,619.
-

Issue 7 - Budget Execution - High Priority

Finding Budget execution was generally at the expected level, except for the Capital Investments where around 19% of funds were underspent at the yearend. While this budget was carried forward as underspending, the Municipality could have paid off liabilities of €292,890 presented in the AFS rather than burdening the future year's budget with such liabilities on capital investments.

Based on courts decisions and Treasury direct payments, €371,312 were paid from the Capital Investments category. Municipal officers were not able to provide us with evidence on what these payments had been made for.

Risk Underspending of funds from Capital Investments at the yearend may result in failure to achieve organisational objectives, i.e. in failure to implement planned projects and having them implemented the following year. Payments executed through court decisions may undermine the budget balance and increase the risk that planned projects are not implemented.

Recommendation 7 The Mayor should ensure that budget performance is systematically monitored on a monthly basis and that this review identifies and addresses barriers to planned levels of budget execution, and also ensure that liabilities carried forward to the following year are reduced as much as possible.

3.1.1 Revenues

Revenues generated by the Municipality in 2016 totalled €3,470,858. These are mainly collected from property tax, construction permits, rental, administrative fee and other. A range of processes and controls related to planning and collection of revenues need to be improved in order to increase revenues and provide for accuracy and completeness of reporting.

Issue 8 – Shortcomings in Planning and Reporting of Revenues – High Priority

Finding The Municipality’s planning did not include revenues from construction permits, vehicles registration tax and licences. The value of unplanned collection was €381,000.

According to property tax data, the Municipality has recorded 31,703 properties. In 2016, they checked 578 existing properties, i.e. only 2% of them rather than 1/3 as stipulated in the Administrative Instruction no.03/2011.

Risk Failure to plan revenues makes the planning and spending process difficult and may result in liabilities carried forward to next periods. Failure to verify 1/3 of properties may result in incomplete information on the current taxable property.

Recommendation 8 The Mayor should ensure that initial budget planning includes all revenues by type and approximate amount expected to be collected, he should also ensure that 1/3 of properties are checked.

Issue 9 – Failure to Enforce the Regulation on Municipal Fees and Fines – High Priority

Finding While testing revenues from the administrative fee and tax licences, we found that in nine (9) cases citizens were charged incorrectly. In six (6) cases the old regulation was used whilst in three (3) ones the current regulation was used, but fees were incorrectly applied. The payment made for these fees was €117, whilst according to the applicable regulation it should have been €182.

Risk Failure to implement the applicable regulation leads to incorrect fees being applied for the citizens which may result in over or under payment than stipulated in the regulation. This will consequently affect the Municipality’s budget.

Recommendation 9 The Mayor should strengthen accountability measures towards the officers applying such fees to the citizens and ensure that the enforced regulation is applied with correct municipal fees and fines.

Issue 10 – Failure to Reconcile Revenues in the Protax System – Medium Priority

Finding According to the Protax program managed by the Ministry of Finance, property tax revenues collected during 2016 were €1,524,625, whilst according to Free-Balance they were €1,562,511, a difference of €37,886.

Risk Failure to reconcile property tax revenues between these two systems leads to the risk that the liability paid by citizens will not be deducted in the Protax system and that citizens will be burdened with such liability already paid.

Recommendation 10 The Mayor should ensure that citizens are not re-burdened with taxes already paid and should try together with officials of the Ministry of Finance to find the reasons behind such differences and eliminated them.

Issue 11 – Delays in Collection of Rent – Medium Priority

Finding The Municipality had entered into a contract agreeing with the tenant that the whole annual rental would be paid at the beginning of the calendar year. The tenant did not honour the terms of the contract for this payment. The Directorate for Property-Legal Affairs issued a decision in contradiction to the contract for the payment to be made in four instalments.

In another rental case, the contract stipulated for the tenant to pay the rent within five (5) days after the year begins. But, the payment of €4,260 for having rented the administration building was made five (5) months in delay.

Risk Weak management of rental contracts and unwillingness to undertake efficient measures to collect revenues increases the risk that revenues plan will not be met and capital projects planned to be financed by own source revenues will not be implemented.

Recommendation 11 The Mayor should ensure effective management of rental contracts and put in place mechanisms to collect revenues according to the contracted terms, i.e. meeting of deadlines for collection of rent.

3.1.2 Wages and Salaries

Wages and Salaries are paid through a centralised system. The key controls that confirm accuracy and completeness of payments are payroll lists signed by the heads of units. Expenditures on wages and salaries for 2016 were €13,213,466 or 100% of the planned budget.

We have no recommendations in this area

3.1.3 Goods and Services and Utilities

The final budget of Goods and Services in 2016 was €3,244,309. Out of which €3,224,106, or 99% of budget were spent. Those mainly relate to expenditures for utilities, travel, telecommunication, services, purchase of mobile phones and equipment, fuel, insurance and registration services, maintenance and other.

Issue 12 – Contracts not foreseen in the Procurement Plan – High Priority

Finding Contracts Supply of Dental Materials; Maintenance and Servicing of the Air Conditioning System; Supply with Stationery and Food; Bus Transport; and Supply of Hygienic Materials were not included in the procurement plan sent to CPA. The value of these five (5) contracts was €1,431,670.

Risk Entry into contracts that were not foreseen in the procurement plan undermines the implementation of planned contracts and leads to changed priorities or even entry into obligations without any budget support.

Recommendation 12 The Mayor should ensure that the procurement plan is drafted following a thorough analysis of all units' requests and that it includes all prioritised projects for which budget funds have been provided.

Issue 13 – Criteria not met and inadequate segregation of duties – Medium Priority

Finding In the Contract of €239,634 for Supply with Dental Materials, one of the tender criteria was for the bank turnover of the last three year to be no less than €150,000 and for the warehouse not located in longer distance than 15km from Peja city. We found no evidence that the contract winner had met this criterion.

The Chairman of Tender Evaluation Commission for the tender Supply with Stationery worth €69,706 was assigned as the Contract Manager for this contract. This is in contradiction to the Public Procurement Rules and Operation Guidelines issued by PPRC⁶.

Risk Awarding contracts outside the defined criteria is in contradiction to the law and leads to risk that the winning will not implement the contract due to insufficient capacities. Inadequate segregation of duties and responsibilities as well as engagement of the same officer in the tender evaluation and as contract manager increases the risk of conflict of interest.

Recommendation 13 The Mayor should ensure that no contracts are awarded to EO unless they meet all the criteria required in the Tender Dossier. He should also ensure that segregation of duties on certain activities is made according to the applicable legislation in order to prevent conflict of interest.

⁶ Article 62.3.7.

3.1.4 Subsidies and Transfers

The final budget of Subsidies and Transfers was €257,628, out of which €248,570 or 96% were spent in 2016. These mainly relate to support culture and sport activities or ad-hoc support.

Issue 14 - Weaknesses in Controls over Subsidies - Medium Priority

Finding The Mayor approved an individual request for financial aid of €2,500 on the grounds that the funds would be used as a financial support for the material to finalize the house built for a serious social case. While reporting on the funds spent, the mediator who took over the financial assistance did not provide reliable and relevant evidence that the funds were spent for the above purpose.

The subsidy of €7,500 on behalf of the public beneficiary was provided with about seven (7) months delay. The decision was taken on 22.02.2016, whilst the funds had been transferred to the beneficiary on 25.10.2016. Article 14.2 of the Regulation on Subsidies stipulates that the subsidy shall be payable no later than 30 days after the date of approval.

Risk Insufficient evidence and delays in paying subsidies may result in poor value for money and in payments not made in line with the regulation.

Recommendation 14 The Mayor should ensure that legal requirements regarding subsidies are adhered to and that relevant evidence is provided to justify the purpose of the subsidy.

3.1.5 Capital Investments

The final budget of Capital Investments was €6,647,046, out of which €5,361,291 were spent in 2016. These relate to expenditures on rehabilitation of infrastructure, construction of schools, expropriations, equipment and different improvements of capital assets.

Issue 15 - No Dates on the Acceptance Reports - High Priority

Finding In eight (8) cases we found that progress payments received from the supervisory body had not dates. It is therefore impossible to know whether works have been executed according to the contracted deadlines.

Risk Supervisory Body's failure to put dates on the executed works increases the risk that the Municipality will not have evidence on whether or not works are executed according to the contracted deadlines.

Recommendation 15 The Mayor should ensure that the project management implements all regularity and validity checks of the documentation and does not accept reports with no dates and required information from the supervisory body.

Issue 16 - Misclassification in the economic categories - High Priority

Finding The payment of €9,980 made on 29.08.2016 was incorrectly classified as expenditure for investment maintenance, but according to the Contact "Stay for the weekend, enjoy Peja" the invoiced stages related to services.

Risk Payments made from inadequate economic categories will affect accurate presentation in the AFS. Where the misclassified amounts are material they may result in qualification of the opinion.

Recommendation 16 The Mayor should ensure that expenditures are classified under the adequate economic categories as set forth in the accounting plan in order to enable a true presentation of expenditures in the AFS.

3.2 Assets

3.2.1 Capital and Non-Capital Assets

The Municipality of Peja did not make much improvements regarding the registration of municipal assets according to the recommendation given last year. Incomplete asset registration is detailed under sub-chapter 1.1.

Issue 17 - Weaknesses in Assets Management - High Priority

Finding The stocktaking commission finished the inventory with 12 days in delay and did not compare the inventory balance with the balance in the non-financial assets register. This is a requirement in the regulation on the management of non-financial assets in the budget organisations.

E-assets register is not accurate because purchases made from Health and Education were not recorded in this register.

Finding Incomplete assets recording and failure to compare the assets register to the current balance makes the confirmation of assets existence difficult and increases the risk that they will be misused, lost or alienated.

Recommendation 17 The Mayor should ensure that assets registers are complete and accurate and that concrete actions are taken for the weaknesses identified during the stocktaking in order to improve them according to the Regulation on Assets Management.

3.2.2 Receivables

The Municipality has failed to correctly present all debts for which it has provided services. The structure of accounts receivable consists mainly of: property tax, rents and business taxes.

Issue 18 - Failure to Reconcile Accounts Receivable - Medium Priority

Finding The Municipality uses the Excel program for charging and collecting the business tax. The responsible officer reported to the Finance Department €8,690,808 of charges, whilst in the Excel program they were €8,665,268, a difference of €25,541. According to officials, the difference was due to mistakes made while charging businesses with this tax, but we were not provided with evidence that validate the difference in these reports.

The value of debt presented in the individual taxpayer's financial records does not correspond to the value of the debt presented in the charge and collection report (wherefrom values were taken to be presented in the AFS). These differences relate to the calculated penalty for the second semester and the interest of December 2016, which are not included in the charge and collection report. These differences exist in all taxpayers whose debt value at the yearend was not zero, thus accounts receivables are understated for these values.

Risk Lack of database assurance for charging and collecting this tax increases the risk that the municipality will reduce the value of business tax without collecting any means. Failure to include interest and penalties in financial reports increases the risk that the Municipality will not have the exact value of the receivables and thus understate them.

Recommendation 18 The Mayor should ensure that existing differences are clarified, that data presented in the financial reports are complete and accurate and include all values that represent the real situation.

3.3 Outstanding Liabilities

The statement of liabilities not paid to suppliers at the end of 2016 was €657,472. These liabilities are carried forward to be paid in 2017.

Issue 19 – Incomplete reporting of liabilities and delays in paying them – High Priority

Finding The Municipality reported to the Ministry of Finance only on unpaid invoices of the previous month, whilst the financial rule on reporting of liabilities require that the monthly report of liabilities include the balance of liabilities of the reporting period including all liabilities, regardless of the period they incurred.

Based on the Financial Rule no.01-2013 on Spending of Public Money, budget organisations should pay any invoice payable for the received goods and services within 30 calendar days from the date the invoice is received. In 16 cases, we found delays in such payments from 7 to 15 months amounting to €343,208.

Risk Incomplete reporting of outstanding invoices and delays in paying debts off increases the risk the lawsuits and may result in additional costs of interests and fines, required by third parties.

Recommendation 19 The Mayor should strengthen controls and ensure that the finance department will record, check, report and pay all liabilities within the set statutory deadlines.

This report is a translation from the Albanian original version. In case of discrepancies, Albanian version shall prevail.

ANNEX I: Audit Approach and Methodology

The responsibilities placed on the Auditor and Those Charged with Governance are detailed in the Opinion set out in Section 1.2 of this report.

While a key output of our work is the audit opinion this report reflects the totality of our work with specific focus also on Governance Issues including Financial Management and Control. The latter is informed by our extensive, risk based, compliance audit programme.

The Executive Summary is intended to highlight the key finding of the audit and the key action that the Mayor should ensure are taken to address identified management/control weaknesses.

The detailed report provides an extensive summary of our audit finding with emphasis on determining the cause audit findings and providing appropriate recommendations to address these. For completeness we have included issues identified at the interim audit where they remain relevant. Our findings are defined as:

High Priority - issues which if not addressed may result in a material weakness in internal control and where action will offer the potential for improvements to the efficiency and effectiveness of internal controls; and

Medium Priority - issues which may not result in a material weakness but where action will also offer the potential for significant improvements to the efficiency and effectiveness of internal controls.

Findings considered low priority were reported separately to finance staff .

Our procedures included a review of the internal controls and accounting systems and associated substantive testing and associated governance arrangements only 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.

Annex II: 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 1705¹⁹ 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 III: Prior Year Recommendations

Audit Component	Recommendation given	Implemented	Under implementation	Not implemented
Financial Statements	The Mayor should ensure that an analysis is undertaken to determine the causes which led to Emphasis of Matter. Adequate actions to address the issues systematically and pragmatically need to be undertaken in order to correct errors in the classification of non-capital expenditures and to ensure that capital assets are correctly recorded and evaluated		There are no visible improvements to influence the emphasis of matter. Misclassifications have improved significantly.	
	The Mayor should ensure that the CFO systematically reports on the physical and financial progress of capital investments in order to have budget requests made based on real needs for investments			There were problems when it comes to recording. Although recording was made the records were not saved.
Prior years recommendations	The Mayor should systematically monitor the implementation of the Action Plan and identify why it has not been implemented. A revised action plan should clearly set out a timetable for the implementation of AG's recommendations with accountable staff members identified and with initial focus on those of greatest significance			Implementation of recommendations is not formally monitored. Some of the recommendations are not implemented

Good Governance	The Mayor should ensure that a review of the processes for completing the self-assessment checklist and proactively addressing areas of weaknesses is implemented. A final review of the Internal Audit may be a supporting tool to enhance quality and confirm the assertions in self-assessment checklist		The self-assessment checklist was prepared but still much remains to be done to improve the quality.	
	The Mayor should ensure that, after having drafted the list of risks with respective levels, immediate responsibility for risk management is delegated to a named director who, in cooperation with the heads of units, will manage and regularly report on the progress of the process			Not implemented
	The Mayor should ensure that the existing accountability and reporting requirements arrangements placed on the municipal directorate are reviewed and that better arrangements for achieving specific objectives and for improving overall governance in the municipality are implemented			Not implemented
Internal Audit	To gain maximum benefit from Internal Audit activity, the Mayor should consider the need to adapt internal audit plans to the requirements for internal audit activities focusing on current year activities and propose immediate improvement measures. In addition, the Audit Committee should be more active in monitoring, building and strengthening the role of internal audit		Efforts have been made but it still remains a challenge. The AC has been more active during 2016 whatsoever.	
Budget	The Mayor should ensure that budget performance is systematically monitored and that barriers to planned levels of budget execution are identified and addressed. Where adjustments to reduce overheads can be made, this should be reviewed in order to focus on capital projects			Not implemented

Procurement Expenditures	The Mayor should review the reasons behind the failures to implement of the contract and propose steps to be followed until the completion of this contract. Moreover, certification controls need to be strengthened and all payments should be made only when progress payments foreseen in the contact are verified	Implemented		
	Identified weaknesses in relation to these supplies should be reviewed and the Mayor should ensure that, during the preparation of the annual procurement plan, a real needs assessment has been made by all requesting units and that all contracts are entered into only for the needed materials and quantities	Implemented		
	The Mayor should strengthen controls over procurement and ensure that procurement processes are implemented fully in compliance with established regulations and respective guideline. The case of the extended contract for Supply with Oil should be reviewed and such practices should not be repeated in the future	Implemented		
	The Mayor should ensure that certifying controls are strengthened and that payments are made following confirmation that all supplies are delivered with clear acceptance reports and in compliance with the contract terms, otherwise payments should not be certified		There was progress on the certification of payments, but improvements should be made in the execution of payments within 30 days and the situations received by the supervisory body contain the date of acceptance.	

Wages and Salaries	The Mayor should undertake concrete measures to ensure regular reporting form departments and summary reports from the HR Department and to provide for a regular staff recruitment and management process in the municipality	Implemented		
Subsidies and Transfers	The Mayor should establish clear criteria regarding approval/refusal of applications for subsidies. He should ensure that, for allocated subsidies, narrative reports are drafted and attached to the invoices and evidences on the reasonability of spending and that activities the subsidies have been allocated for are followed up.		Efforts have been made i following the activities for which the subsidies were allowed but it still complete implementation remains a challenge especially the full compilation of the feedback reports and the establishment of clear criteria.	
Revenues	The Mayor should ensure that enhanced internal controls over collection, reconciliation and reporting of own source revenues are put in place. While reviewing the budget, he should ensure that revenues planning is based on the earlier periods“ collection trends and the complexity of existing operations. In addition, the Property Tax Office should all the property verification resources		Improvements in revenue collection, reconciliation and reporting were noted but further improvements in property verification and full revenue planning are needed	

Assets	The Mayor should establish the commissions for the fair and complete evaluation of all non-financial assets and monitor the evaluation outcomes. The Assets Management Officer as well as officials engaged in receiving municipal assets should effectively communicate in order to prevent regulations requirements from not being implemented and assets value from not being consolidated		Efforts have been made in registration of the assets and in effective communication between the officials in asset registration but fully registration of the all assets remains a challenge.	
Accounts receivable	The Mayor should review the balance of these accounts, analyse the reasons behind the accumulation of such large amounts and undertake effective actions to maximise the collection rate. The process of systematic monitoring of measures and policies for increased collection should also be part of regular management review.			Not implemented
Liabilities	The Mayor should review the balance of outstanding liabilities to determine the measures needed to address the identified issues, and ensure that payments are made within the deadlines set forth in the financial rules. In order to handle contingent liabilities, he should undertake a review of the balance of liabilities in coordination with the municipal Legal Representative in order to avoiding direct payments from MoF and courts.		Outstanding liabilities were treated but fully registration of the payments within deadlines set in financial rules remains a challenge.	

Annex IV: Letter of confirmation

[Put the Municipality's logo]

LETTER OF CONFIRMATION

For having agreed on the Auditor General's findings of 2016 and implementation of recommendations:

To: National Audit Office

Venue and date:

Honoured,

We hereby confirm that:

- We have received the draft audit report of the National Audit Office on the 2016 Annual Financial Statements of the Municipality of Peja, hereinafter referred to as the Report;
- Agree on the findings and recommendations and I have no comment on the content of the Report; and
- Within 30 days from receiving the final report, I will submit the action plan on implementation of recommendations including the deadlines and responsible staff for their implementation.

Mayor:

XXXXXX

KOMUNA E PEJËS



LETËR E KONFIRMIMIT

Për pajtueshmërinë me të gjeturat e Auditorit të Përgjithshëm për vitin 2016 dhe për implementimin e rekomandimeve

Për: Zyrën Kombëtare të Auditimit

Vendi dhe data: 21/04/2017

I nderuar,

Përmes kësaj shkrese, konfirmoj se:

- kam pranuar draft raportin e Zyrës Kombëtare të Auditimit për Auditimin e Pasqyrave Financiare të Komunës së Pejës, për vitin 2016 (në tekstin e mëtejshëm "Raporti");
- pajtohem me të gjeturat dhe rekomandimet dhe nuk kam ndonjë koment për përmbajtjen e Raportit; si dhe
- brenda 30 ditëve nga pranimi i Raportit final, do t'ju dorëzoj një plan të veprimit për implementimin e rekomandimeve, i cili do të përfshijë afatet kohore dhe stafin përgjegjës për implementimin e tyre.

Kryetari:

Gazmend Muhaxheri

