



REPUBLIC OF KOSOVA
OFFICE OF THE AUDITOR GENERAL

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AUDIT REPORT
ON THE FINANCIAL STATEMENTS OF THE MUNICIPALITY OF
LIPJAN
FOR THE YEAR ENDED 31 DECEMBER 2013

Prishtina, June 2014

The Office of the Auditor General (OAG) undertakes both Regularity and Performance Audits. The Auditor General Lage Olofsson, is the head of the OAG which employs around 145 staff. The Auditor General and the OAG shall be independent and certifies around 90 Annual Financial Statements each year, while undertaking other forms of audits.

Our Mission is to “Contribute to sound financial management in public administration”. We shall perform quality audits in line with internationally recognized public sector auditing standards and good European practices. We shall build confidence in the spending of public funds. We shall play an active role in securing taxpayers’ and other stakeholders’ interests in enhancing public accountability’

The reports produced by the OAG directly promote accountability as they provide a base for holding managers’ of individual budget organisations to account.

The Auditor General has decided on the audit opinion and report on the Annual Financial Statements of the Municipality of Lipjan 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 under the management of the Audit Director, Florim Beqiri, supported by Lavdim Maxhuni (Team Leader), Sabile Musa, Mexhit Ferati and Shpresa Zenelaj.

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Executive Summary

Introduction

This report summarises the key findings from our audit of the 2013 Annual Financial Statements of Lipjan Municipality which determine the Opinion given by the Auditor General. I would like to thank the Mayor and his team for their assistance during the audit process.

The examination of the 2013 Annual Financial Statements was undertaken in accordance with the internationally recognised Public Sector auditing standards. Our approach included such tests and procedures as we deemed necessary to arrive at an opinion on the financial statements. The approach taken is set out in our Audit Planning Memorandum dated 12.12.2013.

Our audit focus has been on:

- The compliance with the reporting framework and the significant risks to the Annual Financial Statements highlighted in the Audit Planning Memorandum;
- The response to our 2012 and earlier recommendations; and
- The Financial Management and Internal Control of the Municipality (including budget execution and Internal Audit).

The level of work undertaken by the Office of the Auditor General to complete the 2013 audit is a direct reflection of the quality of the internal controls implemented by management.

Opinion

Annex I explains the different types of Opinions applied by the OAG.

The AG's opinion is:

In our opinion the Annual Financial Statements *present a true and fair view* in all material aspects, with the exception of:

In the Statement of Cash Receipts and Payments – Third Party Payments, the Municipality did not accurately present the amount of €1,588,153. This amount is not accurate as the co-financings from line Ministries in the amount of €1,162,937 are also included in the total of these payments.

In the budget execution report, the Municipality presented the amount of €1,949,000 as budget appropriation, while according to the Free Balance this amount should have been €1,700,000. The difference is €249,000.

Emphasis of Matter

In addition, we would like to draw your attention to the fact that records and information regarding the disclosure of outstanding liabilities and assets were not accurate. Inaccuracies are:

The invoices of January 2014 in the amount of €83,196 were also included in the total of outstanding liabilities presented of €1,246,034.

In the summary of Non-Financial Capital Assets, assets above €1,000 presented in the AFS were in the amount of €173,655,000. These assets are not complete and accurate as there were assets not recorded in the accounting register and not presented in the AFS.

Capital Investments were overstated by €53,281 as this amount was spent on Wages and Salaries.

(ISSAI 200 Qualified Opinion with an Emphasis of Matter).

Overall Conclusion

Our overall conclusion based on the detailed sections of this report is that:

The management of Municipality designed the internal control system, but these controls were not sufficiently effective in some key areas of financial management. In particular, we have identified:

- Although the Financial Statements addressed most of presentational requirements, the Annual Financial Statements presented for audit had a number of omissions and inaccuracies. Some were amended in the final version of the Annual Financial Statements, but the management chose to leave some items unadjusted.
- Significant risks that materialised were incorrect reporting of third party payments in the amount of €1,588,153. The total of these payments included payments (co-finances) for various projects implemented by the MLGA, MEST, and the Ministry of Infrastructure in the amount of €1,162,937. Another significant risk in the AFS relates to incorrect recording of assets, because the Committee identified assets which were not recorded in the Asset Registers;
- The prior year recommendations were implemented at a low level. Out of 21 recommendations, the Municipality implemented only five. This resulted in some of the weaknesses to be repeated at even more significant forms;

- Although the final budget execution in total is 92%, Capital Investment funds were spent at a relatively low level of 86%, while the budget for Goods and Services was spent only by 68%. This was due to the failure in collecting Own Source Revenues in line with the plan;
- We have noticed that control weaknesses in the high management level are serious. Problems relate to communication and information nature. There is a lack of regular reporting on the progress of Municipality's day-to-day operations.
- The abnormal trend of revenue collection increases the need for better planning of own financial resources. The revenues collected in 2013 were 8% higher than those in 2012, but 30% lower than those in 2011. It seems that the Municipality does not have any consistency in planning and as a result, the collection of revenues from property tax was lower than planned. Poor management of revenues is also noticed in collecting rent from public properties. Nearly €80,000 were accumulated from rent as Receivables;
- Procurement was also followed by serious shortcomings. Besides shortcomings in administrating procedures, the Municipality entered into contracts by 5,9 million, while only 1.7 million were committed;
- Due to failures of management's controls, outstanding liabilities presented by the Municipality for Wages and Salaries at the end of the year were in the amount of €288,474, this is because a number of Education employees were left out off the payroll list. Irregularities were also identified in payments carried out for maternity leave;
- Poor management of Subsidies was reflected with payments carried out without a legal basis, by not applying of established criteria and by carrying out payments for Goods and Services from Subsidies; and
- Poor addressing of internal audit recommendations resulted in repeating of same recommendations, systematic weaknesses and shortcomings.

The Auditor General's key recommendations are as follows:

The Mayor should ensure that:

- 2014 AFS Production Process formally incorporates management review of the draft account with specific focus on areas considered of high risk of error and/or areas where errors have been identified in previous years. The staff responsible for preparation of the Annual Financial Statements should have adequate professional competence, or attend additional training in this area;
- A revised action plan clearly sets out a timetable for addressing the recommendations made by the Auditor General with accountable staff members identified and initial focus on areas of greatest significance.

- The budget preparation process is followed by a rigorous assessment fully reflecting all relevant information, including expenditures against revenues during the previous year and the changes expected during the year etc. Effective monitoring should be implemented during the year and appropriate actions taken to address variances against the expenditures planned;
- Prompt measures are taken and that an appropriate governance structure is implemented, through which the senior management is informed on control deficiencies and actively manages them;
- A systematic review is carried out and obstacles determined, in order to increase Own Source Revenues, reduce the level of historical debts, and identify possibilities for improving the current situation. The Municipality should refer to other similar Municipalities and implement their effective practices if they can be applied under the same conditions;
- A detailed assessment of procurement process and controls is made to determine why weaknesses continue to occur and identify actions which need to be taken to address these weaknesses;
- The possibility how these liabilities could be covered is discussed with the Ministry of Finance and the Government.
- Employment contracts are approved only if there is sufficient budget for vacant positions, and review the cases of non-payments to staff are identified. In addition, urgent measures should be taken to draft a regulation on subsidies, review irregular payments and determine why the existing criteria were not applied, and establish additional controls to ensure that such cases are not repeated in the future; and
- All management levels take into account the advice and recommendations made by the Internal Audit, and occasionally monitor whether the Internal Audit process is having an impact.

Management's response – audit for 2013

The management has agreed to all our audit findings and committed themselves to address our recommendations.

1 Audit Scope and methodology

It is the responsibility of the Municipality to prepare Annual Financial Statements (AFS) under the International Public Sector Accounting Standards (IPSAS) for 'Financial Reporting under the Cash Basis for Accounting' and other specific requirements. The Office of the Auditor General (OAG) is responsible for carrying out a Regularity Audit which involves the examination and evaluation of the AFS and other financial records and expression of opinions on:

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

We have considered 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 opinion of the Auditor General (AG) and the focus of our audit.

The following sections provide a more detailed summary of our audit finding with emphasis on observations and recommendations in each area of review.

For completeness we have included issues identified at the interim audit where they remain relevant. Our findings are defined as:

High Priority - issues which 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 improvements to the efficiency and effectiveness of internal controls.

Our procedures included a review of the internal controls and accounting systems and procedures 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.

Findings considered low priority will be reported separately to finance staff.

2 Annual Financial Statements and Other External Reporting Obligations

Our review of the AFS considers both compliance with the reporting framework and the accuracy of the information recorded in the financial statements. We also consider the Declaration made by the Chief Administrative Officer (CAO) and Chief Financial Officer (CFO) when the draft AFS are submitted to the Government.

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 financial statements. A number of the declarations are intended to provide assurance to the Government that all relevant information has been provided to ensure that a comprehensive audit can be undertaken.

2.1 Audit opinion

Qualified Opinion with an Emphasis of Matter

In our opinion the Annual Financial Statements *present a true and fair view* in all material aspects, with the exception of:

In the Statement of Cash Receipts and Payments – Third Party Payments, the Municipality did not accurately present the amount of €1,588,153. This amount is not accurate as the co-financings from line Ministries in the amount of €1,162,937 are also included in the total of these payments.

In the budget execution report, the Municipality presented the amount of €1,949,000 as budget appropriation, while according to the Free Balance this amount should have been €1,700,000. The difference is €249,000.

Emphasis of Matter

In addition, we would like to draw your attention to the fact that records and information regarding the disclosure of outstanding liabilities and assets were not accurate. Inaccuracies are:

The invoices of January 2014 in the amount of €83,196 were also included in the total of outstanding liabilities presented of €1,246,034.

In the summary of Non-Financial Capital Assets, assets above €1,000 presented in the AFS were in the amount of €173,655,000. These assets are not complete and accurate as there were assets not recorded in the accounting register and not presented in the AFS.

Capital Investments were overstated by €53,281 as this amount was spent on Wages and Salaries.

(ISSAI 200 Qualified Opinion with an Emphasis of Matter).

2.2 Significant risks to the Annual Financial Statements

Description

Our Audit Planning Memorandum dated 12.12.2013 were identified two significant risks that relate to assets recording and disclosure of Third Party Payments.

These are risks of material misstatement which may result in a modified opinion including an Emphasis of Matter.

The risks of material misstatements that we have identified relate to the recording of assets and presentation, identification of third party payments and their presentation in the AFS has occurred because no management actions were taken to address the highlighted risks.

Identified Risk

Issue 1 – Incorrect presentation of third party payments

Finding

During the examination of AFS we noticed that in the column of third party payments, the Municipality recorded the amount of €1,588,153. This amount is not correct as in the total of these payments, the co-financings in the amount of €1,162,937 from various projects by the MLGA, MEST, and the Ministry of Infrastructure are also included.

These spent amounts are recorded as expenditures in the accounting records of these ministries, and since they were made from Treasury Single Account they cannot be handled as third party payments. Material misstatement regarding these payments may lead to modification of the opinion.

Recommendation 1 High Priority – The Mayor should analyse the reasons for misstatements concerning the third party payments, and ensure that third party payments are fully and accurately reported in the AFS 2014.

Identified Risk

Issue 2 – Assets owned by Municipality are not identified and recorded properly resulting in material misstatements in the assets note to the AFS.

Finding

We have assessed the controls implemented by the management to prove whether or not the assets owned by the Municipality are recorded in Asset Register. In our interim memorandum, we provided advice to management on the actions required to ensure that the assets figure in the AFS was correct. However, the risk identified has materialised

because the management has not managed to apply necessary improvements in internal control and we have confirmed that assets values recorded in the AFS are incorrect, as the committee identified assets that were not recorded in the assets registers.

Recommendation 2 High Priority - The Mayor should analyse the reasons why these assets were not recorded and identify the actions required to address these controls weaknesses in order to enable a true and fair presentation of assets in the 2014 AFS.

2.3 Compliance with AFS reporting requirements

Description

The AFS are required to comply with a specified reporting framework. We considered:

- Compliance with Financial Rule (FR) no. 03/2013;
- Requirements of LPFMA no. 03/ L-048;
- AFS have been prepared within the timeframe and submitted to the Ministry of Finance (MoF);
- AFS have been signed by the CAO (Mayor) and the CFO;
- AFS have been submitted in Albanian and Serbian;
- AFS have been prepared in hard and electronic copy; and
- The Municipality prepared and submitted regular quarterly reports to the Municipal Assembly and one copy to the Minister of MoF during 2013.

We have identified the following discrepancies:

A number of financial adjustments were required to the draft AFS and we have also made a number of other suggestions to improve these inaccuracies, nevertheless, appropriate adjustments were not made. Given the above - the Declaration made by the CAO and CFO when the draft AFS are submitted to the Government can be considered to be incomplete related to the third party payments, budget execution, outstanding liabilities and assets.

Issue 3 – AFS production process – High Priority

Finding

In Article 12, Statement of Cash Receipts and Payments – column of Third Party Payments, the Municipality did not accurately present the amount of €1,588,153. For more information, see Chapter 2.2 of this report.

In Article 13 - Budget Execution Report, Note 16, Final Budget column, the Municipality presented the amount of €1,949,000 as budget appropriation while according to the Free Balance this amount should have been €1,700,000 i.e. a difference of €249,000.

Capital investments were overstated by €53,281 as this amount was spent on Wages and Salaries.

Note 31 - Statement of Outstanding Liabilities - in the total amount of €1,246,034 invoices of January 2014 in the amount of €83,196 were also included as outstanding liabilities.

In Note 30 - Summary of Non-Financial Capital Assets in value above €1,000 presented in the AFS was €173,655,000. These assets were not complete and accurate, as the Municipal Committee found assets which were not recorded in the accounting register nor presented in the AFS,

Risk

Annual Financial Statements were not complete, especially in terms of Third Party Payments, reporting of expenditures and assets. Accounting records are insufficient to support management decision-making processes and wider budget considerations.

Recommendation 3 The Mayor should ensure that the requirement from the draft plan for AFS 2014 for the review of draft account is applied by the management, with special focus on areas where statements were deficient. The statement made by the CAO and the CFO regarding the accuracy of AFS should not be submitted unless all relevant controls over the AFS have been applied.

2.4 Compliance with other external reporting requirements

Description

The Municipality is required to address the following external reporting obligations other than producing AFS such as:

- Budget request for financing capital projects to the MoF;
- Quarterly reports including nine month financial statements in time;
- Self-assessment report in accordance with Financial Management and Control (FMC) rules;
- Draft and final procurement plan in time;
- Action plan on addressing of recommendations; and
- Reports on debts submitted to the MoF.

We have no issues to raise on these matters, as the Municipality met all external reporting obligations. Furthermore, the requirements met were of good quality and in line with reporting deadlines.

Recommendations

We have no recommendations in this area.

3 Prior Year Recommendations

Overall Conclusion

The management of Municipality prepared an Action Plan on implementation of recommendations, although we found that most of previous year recommendations were not addressed. For a more thorough description of the recommendations and how they are addressed, see Annex II.

Description

Our Audit Report on the 2012 AFS resulted in 21 recommendations.

At the end of our audit, we noticed that five recommendations have been fully addressed; three were partially addressed or are in the process of being addressed; and 13 have not been addressed yet.

Issue 4 – Poor addressing of Prior Year Audit Recommendations – High Priority

Finding Only a portion of prior year recommendations has been implemented because the management has not implemented any formal process to manage and monitor the way that the AG's recommendations are implemented.

Risk The continued weakness of internal controls in key financial systems such as Financial Management and Control has resulted in:

- Improper budget management;
- Lack of sufficient controls over planning and collection of revenues;
- Continuous organisational inefficiency and poor value for money in procurement practices;
- Irregular payment of invoices and subsidies; and
- Entry into contracts without commitment of funds, and recruitment of staff above the approved budget etc.

Recommendation 4 The Mayor should ensure that a revised action plan clearly sets out a timetable for addressing the recommendations made by the AG with accountable staff members identified and with initial focus on those of greatest significance. The implementation of this plan should be reviewed by the Mayor on a monthly basis.

4 Financial Management and Control

4.1 Overall Conclusion

Our audit approach is focused on understanding and evaluating the actions taken by management to secure effective financial management and control and the results of this action. For individual financial systems we seek to identify the level at which actual controls operate. We consider that controls are well designed but have not been implemented as planned and are not operating effectively. This requires an assessment of structures, processes, and accountability lines introduced by management including the role undertaken by Internal Audit and Audit Committee.

We also considered Municipality's self-assessment undertaken in the context of PFM both in terms of PEFA assessments and PIFC self-assessment.

We found that significant improvement of controls is required in all the areas to prevent the Municipality from suffering financial losses, poor value for money and ineffective management of operational activities. The main areas where most improvements are required are Wages and Salaries, Procurement, Revenues, Subsidies, Assets Management and Outstanding Liabilities.

4.2 Good Governance

Description

The management implemented a range of internal controls to ensure that financial systems operate properly. It is important that they include appropriate reporting to the management to enable effective and timely responses to operational problems identified.

Issue 5 – Weaknesses in high level management controls - High Priority

Finding Our review of managerial controls implemented in the Municipality's main financial system highlighted that control weaknesses in the high management level are serious. Problems relate to communication and information nature. Lack of regular reporting on the progress of Municipality's day-to-day operations caused significant management weaknesses resulting in the irregularities identified in the summary of this report.

Risk Poor quality of financial reporting to the senior management reduces the ability of management to manage actively Municipality's activities and impairs effective budgetary control. This may result in unplanned deficit or surplus and delay necessary actions to address them. In addition, there is a continuous potential risk for irregularities.

Recommendation 5 The Mayor should take prompt measures and ensure that an appropriate governance structure is implemented, through which the senior management is informed on control deficiencies and actively manages them.

4.3 Budget Planning and Execution

Description

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

Table 1 Sources of budgetary Funds - outturn against the budget (in €)

Description	Initial Budget	Final Budget ¹	2013 Outturn	2012 Outturn	2011 Outturn
Sources of Funds	11,993,341	12,305,133	11,269,304	11,351,262	11,665,699
Government Grant - Budget	10,293,341	10,293,341	10,156,396	10,140,584	9,874,397
Carried forward from previous year ² -		248,562	232,968	313,996	479,741
Own Source Revenues ³	1,700,000	1,700,000	822,940	880,766	1,280,050
Domestic Donations		5,848	0	10,000	0
External Donations		57,382	57,000	5,916	31,511

The final budget, compared with the initial budget was higher by €311,792. This increase is a result of External and Domestic Donations and Revenues carried forward from the previous year.

In 2013, the Municipality used 83% of the final budget or €11,269,304, while in 2012 the budget was spent at the level of 95%, which can be considered a good budget performance.

¹ Final budget - the budget approved by the assembly which was subsequently adjusted for by the Ministry of Finance.

² Own Source Revenues unspent in previous year carried forward into the current year.

³ Municipality own source revenues planned and collected in the current year which was used by the entity for financing its own budget.

Table 2 Spending of funds by economic categories - outturn against the budget (in €)

Description	Initial Budget	Final Budget	2013 Outturn	2012 Outturn	2011 Outturn
Spending of funds broken down by economic categories	11,993,341	12,305,134	11,269,304	11,351,262	11,665,699
Wages and Salaries	6,780,898	6,789,328	6,738,235	6,744,399	6,580,682
Goods and Services	1,199,710	1,193,056	815,574	742,386	752,815
Utilities	256,500	256,594	204,747	119,972	130,708
Subsidies and Transfers	150,000	184,866	179,550	138,064	88,273
Capital Investments	3,606,233	3,881,290	3,331,198	3,606,441	4,113,221

Explanations for changes in budget categories are given below:

- The increase of Capital Investments budget was done partly from the revenues carried forward in the amount of €212,000, and from the donors in the amount of €63,000. The budget in this category was spent at the level of 86%. Failure to collect revenues in the amount of €500,000 planned from Own source revenues had a direct impact in executing capital projects. The table shows that the Municipality was much more effective in two prior years when it comes to executing capital projects.
- The budget for Goods and Services was reduced by €6,654. Notwithstanding the reduction in this category, only 68% of the budget was spent during the year. This budget surplus resulted because the Municipality did not make accurate calculations of funds required for this expenditure category.
- With the review, the budget of Subsidies and Transfers category increased by €35,000. This increase was due to a transfer of funds from the category of Goods and Services and Revenues carried forward from the previous year.
- Each year Own Source Revenues are underspent as a direct result of budget underspending given that Own Source Revenues are the last source of funding used. In 2014, the value of revenues carried forward was €395,000.

Table 3 Municipality's own source revenues budgeted and collected in 2013 (in €)

Description	Initial Budget	Final Budget	2012 Receipts	2011 Receipts	2010 Receipts
Own Source Revenues	1,700,000	1,700,000	1,202,414	1,111,359	1,570,134

As seen from the table, planned revenues for 2013 were in the amount of €1,700,000, while revenues collected were in the amount of €1,202,414 or 71%, including court fines and police tickets. The main part of revenues was from property tax (41%). Percentage of revenue collection is relatively low. Variances of revenue collection amounts in the past three years are obvious. There is an increase compared with 2012, but a significant decline compared with 2011.

On the other hand, debts to the Municipality exceeded the value of 3.4 million, which is a significant amount. The balance of receivables is steadily increasing.

Issue 6 - Budget Planning and execution - High Priority

Finding The budget for Capital Investments and Goods and Services was not planned properly and was not based on the trend of expenditures made in previous years. Planning was not good also when it comes to allocation of funds throughout the year. Around 52% of the Capital Investments budget was spent in the last quarter.

Risk There is a high discrepancy between the plan and expenditures. Inadequate planning and execution of the budget in the abovementioned categories may result in failure to meet organisational objectives (planned expenditures) and funding of current year obligations with the next year budget.

Recommendation 6 The Mayor should ensure that the budget process is followed by a thorough analysis and critical evaluation of all categories, with particular focus on capital projects. The Mayor should monitor the budget performance on a periodic basis and address obstacles arising during the execution process of capital projects, in order to ensure that projects are executed and objectives met.

4.4 Revenues (including Own Source Revenues)

Description

Revenues generated in 2013 totalled €1,202,414. The main items comprising amounts collected are revenues from property tax, other business fees etc.

Issue 7 - Property tax - High Priority

Finding The Municipality for 2013 invoiced 18,925 property taxpayers in the value of €1,009,798, while it collected €493,668 or half of the invoiced amount. We have tested 13 samples amounted to €58,361, where the Municipality signed agreements with taxpayers to pay obligations with instalments, and noticed that these taxpayers only paid the first instalment in the amount of €16,036. The Municipality did not address this issue in a systematic manner and payments arranged were not carried out.

Risk Since the property tax is Municipality's main revenue source, failure to collect as planned has direct impact in executing capital projects and other funding foreseen from this source.

Recommendation 7 The Mayor should review existing systems to confirm whether the mechanisms established by the Municipality over revenue collection are operating effectively, and if not, take additional actions to ensure that taxes are collected at the foreseen levels.

Issue 8 – Construction licenses - High Priority

Finding

The Municipality planned to collect the amount of €150,000 from construction licenses, and it collected €17,744 or 12%. In our discussions with responsible persons, we were told that the Ministry of Finance increased the revenue planning for 2013. Therefore, it resulted in unsatisfactory collection from this category.

Based on the inspectorate report, 27 cases of illegal constructions were identified during 2013, but inspectors failed to issue decisions to demolish these buildings and collect construction fees.

We noticed that the apartment building “Dino Sh.P.K” did not have a construction license, where according to the decision it did not meet construction conditions, while according to inspection report, the construction was completed without a construction license with floors (B+P+7). In addition, in one case a natural person applied for a construction license of an apartment building with floors (B+P+6 and P+1). No license was issued for the building, as it did not meet construction conditions, while according to the inspectorate, the works have already been completed.

Risk

Illegal construction of buildings has adverse effects on Municipality’s spatial and development planning. In addition, avoiding to pay fees for construction licenses results in low collection of revenues, as well as financing other supporting infrastructure projects for these buildings.

Recommendation 8

The Mayor should ensure that prompt actions are taken for addressing this problem with a priority. Such cases should be handled separately, and assess which of these building could be legalised and which should be demolished. It is also necessary that regulatory plans are discussed and approved, in order that investors avoid constructions without licences. Administrative measures should be taken as needed.

Issue 9 - Revenues from rented out properties - High Priority

Finding Planning of revenues from rent was in the amount of €71,000 whilst €48,138 was collected. Out of these, 69% were collected only in December.

The Municipality signed 62 contracts for renting out land and business premises. 51 lessors had accumulated and outstanding debts in the amount of €79,029. The Municipality terminated the contracts for 19 cases, but no steps are taken yet to collect the debts from others.

Risk The Municipality has weak controls over its properties. Lack of timely action in collecting monthly rents and in updating contracts for municipal properties, increases the risk that financial obligations against the Municipality are not met by the users of these properties, and these debts become uncollectable or turn into bad debts.

Recommendation 9 The Mayor should raise the issue of contracts expired in the Municipal Assembly, and where they deemed necessary, to extend the contracts. On the contrary, users who do not possess valid contracts should be stopped from using public property.

4.5 Expenditures

4.5.1 Procurement

Description

Although the Municipality designed formal controls over expenditures, our testing has shown that they do not operate properly. Signing contracts without sufficient commitment of funds, rewarding ineligible bidders, are only few cases describing the failure of controls.

Expenditures made through procurement procedures for 2013 were in the amount of €3,681,096.

We have analysed whether capital investment projects were recorded in the Public Investment Program (PIP) and the Medium Term Expenditure Framework. Furthermore, we also reviewed whether any changes have taken place regarding the projects foreseen to be implemented during the year. We have evaluated that the PIP system was not completely followed, as there were cases where contracts signed for 2013 were foreseen under the PIP, but budget was not planned for these contracts for the following years (2014 and 2015), as is the case with 19 following contracts:

Issue 10 - Entry into obligations without the availability of funds, without sufficient commitment of funds and rewarding ineligible bidders - High Priority

Finding

In the contract “Construction of school in Bujari” in the amount of €392,844 the statement of availability of funds is missing. The commitment of funds for this contract was only in the amount of €3,035. The budget foreseen for this project for 2013 was in the amount of €50,000, while for 2014 and 2015 there is no budget planned for executing this contract.

In addition, the Municipality during 2013 signed 19 contracts for Capital Investments in the amount of €5,926,545 without having sufficient funds. The total amount foreseen and committed for these contracts was €1,656,867. The difference between the contracts and amounts committed is €4,269,678.

In the contract “Servicing and Maintenance of Vehicles of Municipal Institutions” in the amount of €129,559, one of the criteria foreseen under contract notice was that Economic Operator (EO) should have contracts of employees and taxes paid for these employees for the last three months. The Dossier of the winning company did not contain evidence that tax obligations for employees were met.

Risk Entering into contracts without appropriate commitments of funds and failure to plan budget adequately for projects lasting more than one year risks the execution of projects, and causes financial difficulties for the Municipality, as well as the possibility to face legal disputes. In addition, lack of statement of availability of funds and deviation from established criteria shows shortcomings when administrating procedures.

Recommendation 10 The Mayor should conduct an internal review to determine why specific procurement requirements were not addressed in the abovementioned cases, and to establish additional controls in order that all identified weaknesses are addressed effectively.

Issue 11 – Improper tender evaluation - High Priority

Finding In the contract for asphaltting of the road “Albania and Haradin Bajrami” in the amount of €2,888,108, the Municipality eliminated the EO who offered the lowest price reasoning that the EO was ineligible. The bid of Eskavatori and Bascom was in the amount of €2,289,197 or €598,911 cheaper than the winning bid. The EO with the lowest price filed a complaint to the PRB, whereby the PRB review panel on 16.07.2013 reviewed the complaint and decided to return the case for revaluation under the justification that the eliminated operator with the lowest price was eligible regarding the criteria for which he was eliminated. The Municipality once again evaluated the tender and the same EO with the cheapest price was eliminated under the justification that he does not meet the same criteria as the first time. Again the EO with the lowest price complains to the PRB and the PRB review expert of on 28.08.2013 gives his opinion that the case should go back for revaluation. The Municipality did not take into account the expert’s opinion, and on 13.09.2013 signed a contract with the company that bid the highest price.

Risk Failure by the CA to evaluate in accordance with criteria established in the Tender Dossier increases the risk of awarding the highest price bid, and cause financial losses to the Municipality.

Recommendation 11 The Mayor should analyse the reasons why the PRB decisions for this case are not considered, to increase controls over the tender evaluation process in order to have equal treatment of EOs upon evaluation of tenders, and to ensure that such cases are not repeated.

Issue 12 – Weak controls in the procurement process - High Priority

Finding In the contract “Repair of sewage system in Konjuh village” in the amount of €90,220, we noticed that the following documents were missing: the statement on availability of funds, decision on establishment of Bid Evaluation Committee, standard forms on notification of eliminated EOs. The evaluation report is deficient given that the part where the Committee recommends the winning company is missing including the signature of Procurement Manager.

Risk Failure to consistently follow procurement procedures and relevant guidelines resulted in entry into irregular contracts.

Recommendation 12 The Mayor should ensure a more effective monitoring of procurement processes through Procurement Manager, in order that such cases are not repeated in the future.

4.5.2 Remunerations (Wages and Salaries)

Description

Wages and Salaries are paid through a centralised system. Controls operated locally by Municipality relate to a) monthly checking of payments by signing the payroll list, b) verifying possible changes that may occur through forms, c) revising of budget for this category and are done monthly reconciliations with the Treasury.

In this category, we tested 65 samples by reviewing the compliance with the payroll list and the payroll system in the Ministry of Public Administration (MPA). Furthermore, we also reviewed whether the positions of officials and multipliers are in accordance with the form of payroll system and the payroll list, and ascertained that matters mentioned are in accordance with legal requirements. Our tests in this category have identified the following issues:

**Issue 13 - Employees outside the payroll, and weak controls over processing of payments
- High - Priority**

Finding The number of Education employees left outside the payroll list increased from 66 in 2012 to 71 in 2013. Outstanding liabilities not paid to employees for Salaries according to the AFS were in the amount of €287,032.

On 01.09.2012 three technical Employees in the vocational school Adam Gllavica with monthly basic salary of €216, were paid with Professor's salary grade of €353 per month. Two of them were paid until February 2013, and one of them until the end of 2013, which is not in line with signed contracts.

In three out of 15 reviewed cases of maternity leave related to Education employees, the payments were not withheld, as required under the labour law. In two cases, the Municipality paid 100% of the salary for the first six months, while it should have paid only 70% of the basic salary. A similar case was paying an Education employee by 100% of basic salary, who went on leave in September 2012, and no changes were made to the payroll.

Risk Failure to pay employees for their contributions creates financial difficulties for employed staff and increases the risk for lawsuits. This may result in financial cost to the Municipality, thus affecting the budget and recruitment processes in the future. For the following cases, the Personnel Office did not update the personnel files and as a result, incorrect payments were carried out.

Recommendation 13 The Mayor should ensure that employment contracts are approved only if there is sufficient budget and vacant positions. Within a specified period, a systematic review of personnel files should be undertaken to ensure that all necessary documentation is included and payments are supported by valid documentation.

4.5.3 Subsidies and Transfers

Description

Planned expenditures for Subsidies and Transfers during 2013 were in the amount of €184,866, while €179,550 have incurred. For testing, we have selected 20 samples in the amount of €96,794, or approximately 54%.

Issue 14 - Lack of legal framework and reporting by subsidy beneficiaries - High Priority

Finding The Municipality during 2013 did not have a written regulation on Subsidies and Transfers.

With the decision of the Mayor on 19.02.2013 funds for the Trade Union in the amount of €28,500 were allocated to cover the liabilities created by the Trade Union for organising a two-day trip in Durres in September 2012, and the financial assistance for New Year's holidays due to the difficult economic situation.

In one case, the Municipality subsidised the football club "Ulpiana" under the decision dated 29.01.2013 in the amount of €17,000. According to the request of club's management dated 15.01.2013, these funds will be used to pay referees, field maintenance, payments to coaches, payments to players, etc. Based on the evidence provided by the club approximately €13,497 were spent for paying debts accumulated in the Tax Administration and the pension trust from August 2009 to April 2013 which is not in line with the request approved.

For two employees of the Municipality, the Mayor allocated financial funds of €1,100 each. The requests made by these employees specified only the amount requested without a specific purpose.

In another case, the Mayor took a decision to allocate funds for a municipality's employee in the amount of €350 for paying Master studies semester at the Faculty of Law without any specific criteria. No evidence was submitted by the beneficiary regarding the payment of these funds for the specified purposes. Identical cases relate to the allocation of funds for two other students for paying semesters in the amount of €300.

On 21.02.2013, the Mayor took a decision to allocate €5,000 as subsidy to the Journalists Association “DEBATE” to purchase equipment for publishing of newspaper “Ulpiana Press”. Under this decision, the beneficiary was required to report in accordance with specification of approved expenditures. No evidence was provided that these funds were designated according to the approved plan. Similar cases are: subsidising the Council for Local Youth Action LIPJAN for the project “Let us celebrate the fifth anniversary of our independence together” in the amount of €1,000, and subsidising the Song and Dance Ensemble LIPJAN for the projects “Preparation of artistic programme for the occasion of fifth anniversary of our independence” in the amount of €1,325, and “Purchases of clothing” in the amount of €2,000.

Risk

Planned expenditures for Subsidies and Transfers have not reached the purpose, and as such are not in line with Financial Rules. Lack of internal policies/regulations results in deficient procedures that should be followed when giving subsidies.

Recommendation 14 The Mayor should immediately adopt a regulation which clearly specifies the criteria and sources of subsidy. In addition, to review the cases mentioned and determine why the controls were not applied and establish additional controls as well as undertake administrative measures in order that such cases are not repeated in the future.

Issue 15 - Subsidies spent for the category of Goods and Services - High Priority

Finding The Municipality paid the amount of €1,660 from the category of Subsidies and Transfers for purchases of invitations, announcements, cups, medals, and inscriptions for the festive program for the occasion of fifth anniversary of our Independence, based on Mayor's decision dated 07.02.2013. In another case, a payment of €900 was made for transportation costs. Paying for Goods and Services from the category of Subsidies and Transfers is not in line with the Treasury Rule 01.

Risk Paying from the category of Subsidies and Transfers for Goods and Services increases the risk of not meeting the objectives planned by the budget.

Recommendation 15 The Mayor should ensure a better planning of expenditures for subsidies, and executing the budget based on initial allocations should be the management's permanent objective. Administrative measures should be taken as needed.

Issue 16 - Subsidies given not in line with criteria - Medium Priority

Finding The Department for Agriculture and Forestry on 07.10.2013 made a public invitation for subsidising Municipality's farmers with 75 milking machines. The total value of subsidies was €18,300. One of the criteria of the advertisement was that "Farmers who have previously benefited from the Municipality or from any other Donor Organisation will not be the beneficiaries". The Municipality subsidised two farmers who received milking machines in the previous advertisement dated 16.01.2013.

Risk The Committee appointed to evaluate applicants avoided the criteria established in the advertisement for giving subsidies to farmers.

Recommendation 16 The Mayor should ensure that criteria established in the advertisement are followed, and that the Evaluation Committee is impartial, fair, and transparent when selecting beneficiaries.

4.6 Assets and liabilities

4.6.1 Capital and non capital assets

Description

Capital assets over €1,000 recorded in 2012 were in the value of €171,261,000, while by the end of 2013 the value of assets recorded was in the value of €173,655,148.

Issue 17 – Incomplete and inaccurate recording of assets - High Priority

Finding

We noticed that the Municipality keeps records of capital and non-capital assets. However, these records were not accurate and updated. We noticed that the Committee established by the management for recording assets did not record the following assets in its report: sports hall building, Serbian School building “Akqiq Brothers”, three ambulances, two vans, one vehicle Golf 4, and one Toyota, and 17 medical beds donated by “Clinique de Joli Mont-Geneva” are not presented in the Asset Register.

When reviewing the register of assets under €1,000, we noticed that the Municipality incorrectly recorded 52 milking machines as municipal property in the amount of €12,688. These machines were given as subsidies to farmers of the Municipality.

Risk

Lack of a complete assets register makes it difficult to identify and confirm assets existence, as well as increases the risk for their misuse, even loss or write-off.

Recommendation 17 The Mayor should ensure that the Committee established by the management evaluates all assets owned by the Municipality. In addition, the management should monitor evaluation results.

4.6.2 Handling of debts

Description

The statement of outstanding liabilities not paid to suppliers at the end of 2013 was in the amount of €1,246,033. These liabilities are carried forward to be paid in 2013. In this amount invoices of 2014 that are in the amount of €83,196 are also included.

The remaining amount of outstanding liabilities is quite significant compared to the total budget of the Municipality and it might have serious implications in meeting 2014 objectives, as these liabilities have to be paid from this year's budget.

Issue 18 – Entry into liabilities above the approved budget - High Priority

Finding At the end of the year, the Municipality presented outstanding liabilities for salaries in the amount of €288,474, due to insufficient budget planning. 77 Education employees were not included in the payroll list.

Risk Failure to plan the budget properly poses a risk for achieving future expenditure plans, due to the need to pay prior year liabilities. Entering into liabilities above budget appropriations may cause financial difficulties for the Municipality, and a possibility to be subject to legal disputes.

Recommendation 18 The Mayor should discuss how these liabilities could be covered with the Ministry of Finance and the Government.

4.7 Internal Audit System

Description

The IAU for 2013 planned to perform nine audits, and managed to execute the entire plan. Audits covered ongoing activities for 2013.

We have evaluated the work of Internal Audit. The IAU managed to cover risk areas, by preparing reports based on standards and with good quality.

The IAU also prepared quarterly reports and submitted them to Central Harmonisation Unit within the Ministry of Finance. Its recommendations were partially addressed by the management.

Issue 19 - Addressing IAU recommendations - High Priority

Finding We noticed that management did not properly handle recommendations given by the IAU.

In addition, the Municipality did not establish an Audit Committee, which is a requirement under the Administrative Instruction 11/2010.

Risk Due to non-functioning of the Audit Committee and poor addressing of recommendations given by the Internal Audit, many irregularities were not avoided or adjusted in time, and as such, they continue existing.

Recommendation 19 The Mayor should ensure that an action plan is adopted covering timetable for addressing internal audit recommendations and establish the Audit Committee in order to facilitate the addressing of recommendations.

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

(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 II: Prior year recommendations

Audit Component	Recommendation given	Recommendation fully addressed	Partly addressed	Not addressed
2.2 Quality and Accuracy of Information Presented in the Annual Financial Statements	The Mayor should ensure that at the end of each year is established a commission to conduct inventory of remaining stock materials, and present them in the AFS.		Partially	
3 Prior Year Recommendations	The Mayor should ensure that a revised action plan clearly sets out a timetable for addressing audit recommendations made with accountable staff members identified - with initial focus on those areas of greatest significance.			No
4.4 Revenues (including own source revenues)	The Mayor along with his management staff should thoroughly analyse the issue of revenues, in terms of planning as well as in establishing effective mechanisms for achieving planned parameters.			No
4.4 Revenues (including own source revenues)	The Mayor should ensure that all revenues are collected in accordance with the financial regulations, and in no cases will be allowed to collect funds from non-formal education in disagreement with the LPFMA.	Yes		
4.4 Revenues (including own source revenues)	The Mayor should review the existing systems in order to control construction projects, evaluate their effectiveness as well as the legal support provided, and apply required improvements.			No

4.4 Revenues (including own source revenues)	It is the Mayor's responsibility to find appropriate mechanisms and increase controls over all debtors of Municipality, in order to collect and reduce debts owed to the Municipality.			No
4.4 Revenues (including own source revenues)	The Mayor should initiate a process to record all properties and associated charges, which would be reviewed every six months by a senior official.		Partially	
4.5.1 Procurement	The Mayor should ensure that the Municipality has sufficient professional staff to prepare the Bill of Quantity with all the appropriate elements, and that there is proper controls over procurement and management of projects. This manner of contracts management has to be reviewed and request professional responsibilities by the supervision body, which has accepted the works and inoperable devices.			No
4.5.1 Procurement	The Mayor should take into account the financial rules that come from the LPFMA under which the budget organisation should not enter into obligations without having sufficient funds.			No
4.5.1 Procurement	The Mayor should ensure that there are sufficient funds for each project and disallow projects to end without being completed. It is important to understand that efficiency in project implementation is forecasting and sufficient allocation of funds for capital investments.			No
4.5.1 Procurement	The Mayor should ensure that procurement initially conducts a market research prior to initiating price quotation procedures. To receive more bidders with the intention of selecting Economic Operators that offer			No

	lower or more favourable prices.			
4.5.1 Procurement	The Mayor should ensure that such sports activities are reasonable so that public funds are spent and justified with supporting documentation.	Yes		
4.5.2 Other expenditures	The Mayor should take into account that incurred expenditures are paid within the legal deadlines, and in the near future to create a financial discipline so that all payments are carried out on time.			No
4.5.2 Other expenditures	The Mayor should ensure that no payment will be approved before confirming that all legal requirements for certification are met.	Yes		
4.5.3 Remunerations (Wages and Salaries)	The Mayor should ensure that no staffs are recruited before their salaries are secured. In addition, the case has to be reviewed and all payments owed to staff are to be carried out as soon as possible, and such practices are not repeated.			No
4.5.3 Remunerations (Wages and Salaries)	The Mayor should terminate such recruitment practices, and for each position to apply and implement requirements and regulations of the Law on Civil Service, in order demonstrate transparency in the process.	Yes		
4.5.4 Subsidies and Transfers	The Mayor should approve formally a regulation that will specify the criteria and sources of subsidies. Expenditures planned on subsidies and transfers should be spent only in these areas.			No
4.6.1 Capital and non capital assets	The Mayor should ensure that as soon as possible requests from assets officer to confirm existence of all assets in the registry. Committees for evaluation and			No

	inventorying should be established and put to action in order to ensure complete information on assets.			
4.6.2 Handling of receivables	The Mayor should prepare an Action Plan proposing clear guidelines for all relevant Municipality's sectors in order to increase collection. The plan should include priorities, separating debts by maturity date, timetable for actions that need to be taken, the reasons for non-payment, appropriate mechanisms and discussing achievements, at least twice a year.		Partially	
4.7 Handling of debts	The Mayor should ensure a thorough and realistic budget planning and that funds are used based on a clear cash flow plan, by not allowing in any case exceeding the allocated funds to the economic categories.			No
5 Internal Audit System	The Mayor should prepare an implementable Action Plan, detailing responsible officials, and the timetables for carrying out actions.	Yes		