



REPUBLIC OF KOSOVO
OFFICE OF THE AUDITOR GENERAL

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

Prishtina, June 2014

The Office of the Auditor General undertakes both Regularity and Performance Audits. The Auditor General Lage Olofsson, is the head of the Office of the Auditor General which employs around 145 staff. The Auditor General and the Office of the Auditor General 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 Office of the Auditor General 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 Peja 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, Faruk Rrahmani, supported by Faik Thaqi (Team Leader), Enver Ramadani and Milosh Petroviq.

TABLE OF CONTENTS

| | |
|--|----|
| Executive Summary | 4 |
| 1 Audit Scope and methodology | 7 |
| 2 Annual Financial Statements and Other External Reporting Obligations | 8 |
| 3 Prior Year Recommendations | 12 |
| 4 Financial Management and Control..... | 13 |
| Annex I: Explanation of the different types of opinion applied by the OAG..... | 29 |
| Annex II: Prior year recommendations..... | 32 |

Executive Summary

Introduction

This report summarises the key findings from our audit of the 2013 Annual Financial Statements for the Municipality of Peja 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 issued by INTOSAI. 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 Planning Memorandum dated 29.10.2013.

Our audit focus has been on:

- 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 management and execution).

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 Office of the Auditor General.

The Auditor General's opinion is:

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

Emphasis of Matter

We would also like to draw your attention to the fact that the information disclosed on fixed assets was incomplete and incorrect because the assets of Family Health Care Centres were not presented in the 2013 Annual Financial Statements.

(ISSAI 200: Unmodified Opinion with an Emphasis of Matter).

Overall Conclusion

Our overall conclusion, based on the detailed sections of this report, is that, Municipality management designed the internal control system, but these controls did not operate in some key areas of financial management. Areas with shortcomings are presented as follows:

- Incomplete presentation of non financial assets in the Annual Financial Statements leads to the conclusion that there are deficiencies in the controls applied by the management to confirm the completeness and accuracy of assets;
- A number of 2012 and earlier recommendations have not been implemented yet. This will result in weak controls / poor value for money;
- Systematic weaknesses in the procurement procedures, granting of subsidies and collection of revenues are indicators that improvements in key areas are slow;
- Although we managed to obtain assurance from effective management controls in some areas of accounts, our assessment of Financial Management and Control has identified that significant weaknesses exist in some important areas of activity; and
- This particularly applied in procurement, where contracts have been poorly managed; contracts were signed without the committed funds, delays in work executions etc. Despite the fact that revenues collection was higher compared to the plan, we found that the invoicing value within a year was not included in the planning and that a clear strategy for the collection of receivables was lacking.

The Auditor General's key recommendations are as follows.

The Mayor should ensure that:

- The 2014 Annual Financial Statements production process formally incorporates management review of draft accounts with specific focus on areas considered of high risk of errors and/or areas where errors have been identified in previous years;
- A revised action plan clearly sets out a timetable for addressing the recommendations given by the Auditor General, with accountable staff identified and initial focus on those areas of greatest importance;
- A Strategic Plan on the collection of receivables and the management of this process is put in place. A preliminary assessment should be made, given the known complexity of the existing operations, and a way of increasing own source revenues collection level should be found;
- A detailed assessment of the procurement process and controls is implemented in order to determine why weaknesses continue to occur and to identify actions to be implemented to address these weaknesses; and
- Funds from the category of Subsidies and Transfers are used in accordance with internal regulation on subsidies and that means allocated from this category have reached the intended purpose.

Management's response - 2013 audit

Management has agreed with our audit findings and has committed itself to address our recommendations.

1 Audit Scope and methodology

It is the responsibility of 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 Auditor General's (AG) opinion 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

Overall Conclusion

Our review of the AFS considers both compliance with the reporting framework, and the accuracy and quality 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

Unmodified Opinion¹ with Emphasis on Matter

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

Emphasis of Matter

We would also like to draw your attention to the fact that the information disclosed on fixed assets was incomplete and incorrect because the assets of Family Health Care Centres were not presented in the 2013 Annual Financial Statements.

(ISSAI 200: Unmodified Opinion with an Emphasis of Matter).

¹ The term "unmodified opinion" is equivalent to the term "unqualified opinion" used in our previous year's reports. The new wording is in accordance with the new INTOSAI audit standards (ISSAI 200). For more information refer to Annex 1.

2.2 Significant risks to the Annual Financial Statements

Our Audit Planning Memorandum identified two significant risks related to the registration of all assets affecting the AFS and the presentation of Third Party Payments.

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

The identified risk of material misstatements related to the recording and presentation of assets occurred because the management did not undertake actions to address these risks. Whilst, the Third Party Payments risk did not occur.

Risk Identified but did not occur

The risk of misstatement that we identified at the planning stage relating to the disclosure and presentation of Third Party Payments did not occur. Municipality's various projects with considerable value have been financed by the Ministry of Youth, Culture and Sports, Donators (USAID, IOM, EU). Municipality's management has fairly handled this risk and managed to present those payments in the AFS and thus provided appropriate disclosures.

Audit response

We have reviewed the Municipality information relating to Third Party Payments and concluded that this information has been presented in AFS.

Identified Risk

Issue 1 - Owned assets are not registered

Finding

The assets owned by the Municipality have not been identified and registered in the assets register resulting in a material misstatement in the assets notes in the AFS. Failure to register all assets will result in material understatement of assets values in the AFS. It has been established that this risk exists and municipality has not managed to address it yet, as required under the Treasury rules.

In our interim audit memorandum, we provided advices to the management on the action required to ensure that the assets figure in AFS was correct. However, the risk identified has materialised because the management has been unable to implement the necessary improvements in internal control and we have confirmed that assets values recorded in the AFS are materially incorrect.

At the final audit stage, we were not provided with any report from the Assets Stocktaking Commission to confirm the complete and timely registration of all municipality's assets.

Recommendation 1 - High Priority - The Mayor should identify the right action to address these control weaknesses in order to enable a true and fair presentation of assets in 2014.

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 no. 03/2013;
- Requirements of Law no. 03/ L-048 on Public Financial Management and Accountability;
- AFS were signed by CAO (Mayor) and CFO;
- AFS were prepared within the time period and are submitted to the Ministry of Finance (MoF) in Albanian and Serbian;
- AFS were prepared in hard copy and in soft copy; and
- Municipality prepared and submitted regular quarterly reports to the Municipal Assembly and to Minister of MoF during 2013.

We have no issues to raise on these matters because issues raised in our interim audit memorandum related to the reporting framework have been addressed by the management.

2.4 Compliance with other external reporting requirements

Description

Other than producing AFS, the Municipality is required to address external reporting obligations such as:

- Budget request for funding capital projects;
- Quarterly reports including nine month financial statements;
- Self-assessment report according to FMC rules;
- Draft and final procurement plan;
- Reports on debts; and
- Action plan for implementation of recommendations;

We have no issues to raise on these matters since the Municipality has complied with all external reporting obligations. In addition, these requests were of good quality and in line with the timetable required.

3 Prior Year Recommendations

Overall Conclusion

The Municipality management prepared an action plan in time and has made progress in addressing our prior year recommendations. However, the other recommendations need to be implemented as well in order to avoid the repetition of same weaknesses from previous year. For a full description of recommendations and how they were addressed, see Annex II.

Description

Our Audit Report on the 2012 AFS resulted in 20 key recommendations. At the end of our audit, we found that eight recommendations have been fully addressed, four have been under the process of addressing, whilst eight have not been addressed at all.

Issue 2 - Addressing Prior Year Audit Recommendations - High Priority

Finding Almost half of the prior year recommendations were not addressed and this increases the risk that they are repeated in 2013. The management has not implemented any formal process to manage and monitor the way the AG's recommendations are implemented.

Risk Failure to address recommendations will result in incomplete AFS, continued poor management, poor management of revenues procurements and subsidies. This will result in poor quality services and poor value for money and ineffectiveness in operational activities.

Recommendation 2 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.

4 Financial Management and Control

Overall Conclusion

Our audit approach is focused on understanding and evaluating the actions taken by management to secure effective Financial Management and Control. For individual financial systems, we seek to identify the level at which actual controls operate. This may, for example, be monitoring activity undertaken by senior management or lower level operational controls.

We consider that controls are well designed, but they have not been implemented as planned and do not operate 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 found that controls over revenue are not being implemented effectively. Controls over a range of expenditure areas require further enhancement to prevent the municipality from suffering financial loss, poor value for money and ineffective project management. The main areas where most improvements are required are: Procurement, Revenues, Subsidies and Asset Management.

4.1 Budget Planning and Execution

Description

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

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

| Description | Initial Budget | Final Budget ² | 2013 Outturn | 2012 Outturn | 2011 Outturn |
|---|----------------|---------------------------|--------------|--------------|--------------|
| Sources of Funds | 19,652,317 | 20,952,752 | 20,263,384 | 18,970,438 | 18,738,853 |
| Government Grant - Budget | 16,752,317 | 17,068,317 | 16,980,919 | 15,930,094 | 15,690,539 |
| Carried forward from previous year ³ - | 0 | 769,957 | 650,615 | 668,228 | 765,294 |
| Own Source Revenues ⁴ | 2,900,000 | 2,900,000 | 2,456,879 | 2,121,449 | 1,880,030 |
| Domestic Donations | 0 | 29,417 | 4,500 | 6,560 | 4,800 |
| External Donations | 0 | 185,061 | 170,469 | 244,107 | 398,190 |

The final budget, compared to the initial budget, was higher by €1,300,435. This increase is a result of External and Domestic Donations and revenues carried forward from the previous year.

In general, 97% of the budget was spent, the same percentage of the prior year. We may conclude that the Municipality had a high budget performance for both years.

² Final budget - the budget approved by the assembly which was subsequently adjusted for by the Ministry of Finance.

³ Own Source Revenues unspent in previous year carried forward into the current year.

⁴ Municipality own source revenues planned and collected in current year..

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 | 19,652,317 | 20,952,752 | 20,263,384 | 18,970,438 | 18,738,853 |
| Wages and Salaries | 10,512,912 | 10,535,499 | 10,482,665 | 10,378,157 | 10,023,108 |
| Goods and Services | 2,343,763 | 2,739,363 | 2,705,611 | 2,686,923 | 2,009,956 |
| Utilities | 591,914 | 601,914 | 597,009 | 557,083 | 500,349 |
| Subsidies and Transfers | 350,000 | 601,007 | 599,233 | 473,692 | 328,432 |
| Capital Investments | 5,853,728 | 6,474,970 | 5,878,865 | 4,874,583 | 5,877,008 |

As noticed from table 2, all economic categories had a high spending efficiency compared to budget allocations.

The final budget, compared to the initial one, was increased in the amount of €1,300,435. This was as result of budget review. An emphasised increase is noticed in Capital Investments by €621,242, Goods and Services by €395,600 and Subsidies and Transfers by €251,007.

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 carried forward value of revenues is €665,510.

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

| Description | Initial Budget | Final Budget | 2013 Outturn | 2012 Outturn | 2011 Outturn |
|---------------------|----------------|--------------|--------------|--------------|--------------|
| Own source revenues | 2,900,000 | 2,900,000 | 3,003,047 | 2,72,7094 | 2,613,910 |

As noticed from table 3, the planned Own Source Revenues for 2013 were €2,900,000, whilst €3,003,047 were collected. The revenues collection trend over the last three years has been positive as we witness a constant growth.

4.2 Revenues (including Own Source Revenues)

Description

The municipality has a positive trend of Own Source Revenue collection compared to previous year and to the current year's plan. Controls over revenues collection and reporting have been established, however, some processes need to be further improved in order to support the complete revenue collection. Weaknesses identified in the Own Source Revenue category are the following.

Issue 3 - Property tax - High Priority

Finding In 2013, the Municipality planned to collect €900,000 from property tax, whilst €1,083,998 were collected. We analysed the invoicing of property tax in order to assess the planning issue. The invoiced amount was €1,737,074 for 2013. When comparing the collected amount with invoiced one, it appears that the Municipality managed to collect 62% of the property tax invoiced amount. The uncollected accounts from property tax are increasing every year amounting to €8,016,674.

Risk Poor collection policies have led to the increase of uncollectable accounts in over €8,016,674. The increase of property tax debt from year to year may result in the reduction of the municipality's revenues and may reduce the possibility of delivering many self-financed projects.

Recommendation 3 The Mayor should ensure that a Strategic Plan on the collection of receivables and the management of this process is put in place. A preliminary assessment should be made, (given the known complexity of the existing operations), and a way of increasing own source revenues collection level should be found.

Issue 4 – Non reconciliation of revenues from municipal departments – Medium Priority

Finding The revenue officer conducts monthly, quarterly and nine month reconciliations with Treasury and municipality’s revenue generating departments. However, we have found that two departments (Department of education and inspection) did not conduct monthly reconciliations with the revenues recording chief officer.

Risk Failure to carry out periodic reconciliations may lead to incorrect reporting of collected revenues and this may also be reflected in AFS.

Recommendation 4 The Mayor should ensure that the municipal departments and the Revenues Officer reconcile revenues on a regular basis in order to provide completeness and accuracy of revenues.

Issue 5 – Business operation tax – Medium Priority

Finding Since 2002, there are 7677 businesses registered in the municipality, some of which are active and some are passive. Pursuant to the Law on Local Government Finance, the municipality collected revenues from business operation tax. The business liabilities towards the municipality by the end of 2012 amounted to €6,360,180.

On 17.12.2012 the Mayor issued a decision to exempt businesses from the business operation tax for 2013. But, prior year liabilities were not handled in this decision and the amount of debts towards the municipality remained at the same level.

Risk If taken decisions does not foresee the way and the timetable these accounts receivable are planned to be collected, there is the risk that the Municipality will hardly collect the accumulated receivables.

Recommendation 5 The Mayor should, as soon as possible, plan how to handle the account receivables from business operation tax accumulated over the years.

Issue 6 – Revenues from secondary education – Medium Priority

Finding In 2013, the Municipality planned to collect revenues from secondary education co-payments in the amount of €70,000, whilst €89,956 was collected, thus exceeding the annual plan. Despite controls established over the revenues of Education Department, we found that €24,780 was received at the cash register. The amount of revenues received was over €10 and, according to financial rules, they should have been paid at the Municipality's account authorised by the Director of Treasury.

Risk Receipt of cash when there is an open account thus neglecting the Treasury rules leads to the risk that cash is misused or lost.

Recommendation 6 During the interim period, we have advised the management to stop receiving cash of over €10 (out of the bank account). At the final stage, we obtained assurance that the advice given had already started to be implemented. We do encourage the management to continue carry on with such practice.

Issue 7 – Revenues from Health co-payments – Medium Priority

Finding In 2013, the Municipality planned to collect revenues from health co-payments in the amount of €110,000, whilst €99,928 was collected. Despite the controls established over the revenues from Health Directorate, we have found that amounts over €10 were received in the cash registers, which should have been paid through the municipality bank account authorised by the Director of Treasury.

Risk Receipt of cash when there already is an open account of municipality thus neglecting the Treasury rules leads to the risk that cash is misused or lost.

Recommendation 7 The Mayor should take measures as soon as possible to ensure that amounts over €10 are paid into municipality's bank account authorised by the Director of Treasury.

Issue 8 – Revenues from leased out premises – Medium Priority

Finding In 2013, the municipality planned to collect revenues from leased out premises in the amount of €11,000, whilst €6,300 was collected. In one case, the municipality leased out the municipal area based on a one-year contract dated 10.06.2009, with a monthly price of €500. The Municipality did neither collect revenues from the rent nor terminate the contract with the lessee.

In addition, there was one case of leased out premise with the rent of €200 per month where collection of instalments was delayed for one year.

Risk Lack of complete records on charges to and payments from all lessees may lead to the under payment of the rent and the reduction of revenue funds.

Recommendation 8 The Mayor should implement a registration process of all properties and associated charges, which should be reviewed regularly.

4.3 Expenditures

4.3.1 Procurement

Description

There are some aspects of procurement where controls have not been applied effectively. Procurement processes were not fully managed according to procurement rules, from the preparatory stage up to the contract termination.

Capital Investments planned for 2013 were €5,374,728. Following the budget review, the value of Capital Investments was increased to €6,474,970. During 2013, €5,878,865 or 91% was spent. In total, we tested 31 samples or 60% of capital expenditures in the amount of €3,907,959.

Our audit has disclosed the following shortcomings:

Issue 9 – Systematic Weaknesses in Procurement – High Priority

Finding

In the contract “Construction of a dressing room in the football stadium” in the amount of €39,964 the dynamic plan has foreseen the completion of works in 41 days. Works were completed with a delay of 55 days and the municipality did not apply penalties.

In the tender “Paving of roads in asphalt” the operator was awarded the contract without meeting technical and professional criteria required in the Tender Dossier, such as: diploma of the project manager and the list of employees reported to Tax Administration of Kosovo.

In four contracts “Renovation and reconstruction of the Family Health Care Centre”, “Construction of water supply in the village Dugajevë”, “Renovation of theatre – Istref Begolli, third phase” and “Construction of the facility for Local Public Enterprises Ambienti” the amount of committed funds was lower, than of the amount of contracts.

In two contracts “Paving of road in asphalt in the village Nobergjan” and “Construction of Local Public Enterprise Ambienti” the tender winner provided a Tender Performance Security of 30 days shorter than the works dynamic plan.

Risk

Entering into contracts without sufficient funds committed, failure to adhere to criteria when selecting the winner, and delays in the contracts implementation indicate the shortcomings in the procurement process. All these shortcomings lead the municipality to the risk of not achieving value for money. The identified shortcomings damage the competition, process transparency and increase the risk of financial losses.

Recommendation 9 The Mayor should analyse why procurement requirements were not addressed in these cases and ensure that enhanced controls are implemented to ensure that such situations are not repeated.

Issue 10 – Control weaknesses in the implementation of contracts - High Priority

Finding We tested the execution of contract for municipality vehicles servicing entered into on 06.09.2012 in the amount of €225,078. In testing the payments, we found that, for some items, the contract prices were not adhered to when invoicing and the municipality accepted and paid them. Cases when prices in the invoice were higher than in the contract are presented as follows:

- 1) Engine oil price in the contract was €8/litre, whilst it was invoiced with a price of €15.
- 2) In four cases, the working hour was €30 according to the contract, whilst it was invoiced €34.80 after VAT was calculated.
- 3) In another case, the price for engine change module for the vehicle Opel Vectra was €245 per piece according to the contract, whilst it was invoiced €1,100 per piece.

Finding Requests from the Municipality for firewood supply were 3,694.75m³, whereas the winning Economic Operator (EO) provided a confirmation from Kosovo Forests Agency for only 720m³ of firewood. Therefore, the quantity the EO had the license for was insufficient in relation to the Municipality's needs.

Finding The Municipality paid the amount of €3,000 to the local TV Dukagjini for broadcasting the municipal assembly sessions. The evidence confirming the coverage of the sessions was missing in the payment certification. Therefore, it is not known whether broadcasting occurred, as there is no CD or a confirmation report.

Finding In one case, the purchase of water tubes was supposed to be with a dimension φ ,300. We found that they received tubes φ , 250, whereas the price was invoiced and paid as for the tubes φ , 300. Therefore, the price paid does not reflect the counter value of what was received.

Risk Failing to follow the appropriate procurement procedures and underlying guidance has resulted in potentially incorrect payments and financial loss for the municipality. There is a further risk that poor value for money spent was achieved in these contracts.

Recommendation 10 The Mayor should ensure an effective control system on the whole procurement process up to the complete contracts implementation. Proactive actions should be undertaken to prevent departures from contract terms when goods are received and goods prices are paid.

Issue 11 - Vehicle management - Medium Priority

Finding According Article 6 of the Administrative Instruction no. 03/2008, every employee that needs to use the official vehicle should first fill out the form - request for driving services, signed by his supervisor. We have identified that Municipality officers did not filled out any form (request signed by their supervisor) on the use of official vehicles. Requests for official trips were not filled out by the vehicle users.

Risk Internal control over vehicle management process is insufficient and increases the risk for their misuse. Lack of requests on the use of vehicles causes a lack of information on the purpose of using official vehicles.

Recommendation 11 The Mayor should put effective controls over this area in place as soon as possible in order that vehicles are used after the request for driving services has been filled out and approved.

4.3.2 Remunerations (wages and salaries)

Description

The budget planned for the category of wages and salaries was €10,534,294, whilst expenses for 2013 were €10,482,665, or 99%.

Wages and salaries are paid through a centralised system (payroll). Controls operating at a local level in the municipality relate to a) control of monthly payments by signing the payroll lists, b) verification of possible changes that may appear through forms, c) review of budget for this category and reconciliations with the Treasury.

We tested 54 samples for this category and reviewed compliance of payroll lists with the payroll system in the Ministry of Public Administration. In addition, we have reviewed whether or not officers positions and multipliers are in compliance with the payroll system form and payroll list.

Issue 12 – Incomplete personnel records – Medium Priority

Finding We tested personnel records to verify if they were complete. Out of 54 samples, we found that eight files of Education Department were incomplete. Employment contracts were missing in the records.

Risk Lack of employment contracts leads to the risk that employees in no employment relation get paid. As such, these payments are illegal.

Recommendation 12 The Mayor should ensure that Human Resources Department will update all personnel records on regular basis, including employment contracts.

4.3.3 Subsidies and Transfers

Description

Initial budget for the category of Subsidies and Transfers was €350,000. After the budget review, the amount of €601,007 was approved. The expenditures for 2013 were €599,233. On 06 March 2013, the Municipal Assembly approved the Regulation on Allocation of Funds for Transfers and Subsidies. We tested 15 samples of €87,388 from the amount spent for subsidies. The weaknesses found are as follows:

Issue 13 – Decisions for subsidies without funds – High Priority

Finding The Mayor approved decisions for different subsidies without having funds to pay. Liabilities presented in 2013 AFS were €18,500. The municipality seems to have taken decisions for subsidizing without coverage.

Risk Taking decisions in lack of an annual budget reflects two different risks. The first risk is that decisions will not to be executed at all due to the lack of funds and the beneficiary will not receive the means. The second risk is that the municipality will enter into liabilities thus putting the upcoming year budget into risk.

Recommendation 13 The Mayor should stop this phenomenon and, in the future, should not take decisions prior have an approved budget. Subsidy should only be granted when funds are available and in line with the Regulation on subsidies.

Issue 14 – Subsidizing public entities - High Priority

Finding

The Municipality subsidised public and non-public entities. In one case, the Municipality subsidised the repair of the city Mosque in the amount of €16,739. The Payment was made in the bank account of a natural person rather than in the bank account of Islamic Community. Article 3 of the Subsidy Agreement sets forth that original documentation on incurred expenditures should be provided 30 days after the project is delivered. The Municipality did not have any feedback on the way funds were spent.

The Municipality subsidised Non-Governmental Organisation “Top Lajm” in the amount of €1,500 to support the project “Ferma Ime”. The Municipality did not receive feedback on the way funds were spent and whether they have achieved the purpose they were intended for.

On 17 December 2012, the Mayor subsidised the football club Arbreshët in the amount of €5,215 in order to announce the best athlete of the year 2012. The agreement has foreseen that project results should be reported 30 days after the selection, which did not occur. Same issues have also occurred when granting subsidies to the theatre projects Rikardi III in the amount of €1,000 and the Arboriculture Association in the amount of €1,000.

The Municipality subsidised NGO “Need Unity” in the amount of €4,000, payment was made on 29.11.2013, and the amount of €7,000 was paid on 05.09.2013. The agreement, according to article 3, has set forth that the Municipality of Peja should report on the means spent and the activities undertaken in writing. Therefore, we had no report on the means spent and the NGO is located out of the Municipality of Peja.

The Film and Theatre House AKT in Prishtinë was subsidised in the amount of €5,000 according to the Mayor’s decision. The agreement signed by the Mayor did not contain any project plan, the NGO is outside of Municipality of Peja and there was no delivery report provided at the end of the project.

In one case, the Municipality subsidised one of its employees in the amount of €2,000 for renovation of the flat. Such subsidy is not foreseen in the Municipality’s Regulation.

In another case, the Municipality subsidised the construction of the road in Lybeniq village in the amount of €7,500 without a project provided for that.

Risk Granting of subsidies by disregarding the regulation approved in the Assembly, lack of projects and lack of receiving feedback information as well as granting of subsidies outside of the municipality's territory leads to the risk of spending public funds out of controls and puts the achievement of objectives into question.

Recommendation 14 The Mayor should ensure that agreements with the beneficiaries are implemented by obliging them to report in accordance with the agreement signed. Municipality's Regulation on Subsidies should be implemented and the municipality should ensure that subsidies have reached the intended purposes.

4.4 Assets and liabilities

4.4.1 Capital and non capital assets

Description

The Municipality has made slight progress in recording assets in the KFMIS compared to the previous year. In 2013, there was €318,891,670 according to AFS, whilst in 2012 it had the recorded amount was €316,318,000.

Issue 15 - Asset recording - Medium priority

Finding The Municipality is still lacking a complete register of assets presented in the AFS. We tested the assets in Family Health Care Centres and found that these assets were not presented in the AFS in 2013.

The Mayor had established the Assets Stocktaking Commission with delay (10 February 2014). By the time we were auditing, the commission had still not started their work.

Risk Incomplete recording of all assets owned by the Municipality increases the risk of understatement of the municipality assets and unfair presentation of assets in the Annual Financial Statements. It also increases the risk of their loss, misuse and unauthorised use.

Recommendation 15 The Mayor should ensure that concrete actions are taken to enable immediate recording of all assets in the respective registers in accordance with requirements of AI, and that correct and complete assets are reported. In addition, the assets stocktaking should be completed at the year-end in order to prove the physical existence of all assets on the stocktaking day.

4.4.2 Handling of receivables

Description

According to the Law on Local Self-Governance, the Municipality collects different own source revenues. In 2013 AFS, the Municipality presented the amount of €14,208,620 as account receivables. These are from the receivables of property tax and business operation tax.

Issue 16 - Increase of receivables - Medium Priority

Finding The Municipality did not install efficient mechanisms for the collection of account receivables on property tax and tax from businesses. The municipal business tax removal has influenced in keeping accounts receivables at a high level.

Risk In efficient of collection revenues increas the risk that the uncollected amounts from property tax and municipal tax are carried forward from one year to another until they are aged. Another risk is that the receivables collection approach is not adequate. As a consequence, this category of receivables will increase constantly.

Recommendation 16 The Mayor should have a comprehensive approach in handling revenues, both at the planning stage and in putting effective mechanisms in place for the accomplishment of planned parameters. The management should initiate a reassessment process, where all accounts will be analysed in terms of aging, significant amounts, real possibilities for collection and the exercise of administrative measures.

4.5 Handling of debts

Description

The statement of outstanding liabilities towards the suppliers at the end of 2013 was €560,075. These liabilities are carried forward to be paid in 2014. Expenditures from Goods and Services in the amount of €378,729 and Utilities in the amount of €110,971 comprise the largest part of these liabilities.

Issue 17 - Entering into liabilities beyond funds - High Priority

Finding The municipality's outstanding liabilities disclosed in 2013 AFS were €560,075. Based on decisions, the amount of liabilities for subsidies was higher than the one presented in AFS, due to the fact that decisions were taken in lack of funds. The budget for Utilities was €601,914, expenditures for this category were €597,008 and outstanding liabilities for 2013 were €110,971 which leads to conclusion that the municipality has exceeded the approved budget.

Risk Taking decisions to grant subsidies by exceeding the budget approved by the assembly and in lack of funds increases the risk that payments will not be made that decisions taken by the Mayor may lose their validity.

Recommendation 17 The Mayor should ensure that the Municipality will not enter into liabilities by exceeding the budget and by risking the upcoming year's budget.

4.6 Internal Audit System

Description

The Internal Audit Unit (IAU) has three auditors, one of which is the Unit Director. He has prepared the 2013 annual audit plan which was approved by the municipality management. In 2013, the IAU planned to conduct 12 audits.

During 2013, 10 audits were conducted. We were not able to use the work of internal audit due to fact that half of audits conducted covered the last year period, whilst our audit objective relates to 2013.

In addition, IAU prepared quarterly reports and submitted them to the Central Harmonisation Unit in the Ministry of Finance.

The Municipality has established an Audit Committee which held four meetings during the year and assessed internal audit reports and the work of this unit.

Issue 18 - Internal Audit - Medium Priority

Finding Internal Audit Law sets that internal audit director should, by October 31st of each calendar year, plan the audit for the upcoming calendar year, which he did do. But, we found that the half of audits conducted so far were focused on 2012.

Risk Following internal audit issues once events have taken place adds no proper value to the progress of operations and to the functioning of due controls. Internal Audit should function as an errors prevention mechanism.

Recommendation 18 The Mayor should ensure that IAU's audit plan includes current year processes/activities in order to assist the management in taking decisions in time and to prevent eventual errors.

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. Annual financial statements | The Mayor is recommended that when preparing AFS he should take into account the legal obligation that AFS should also be prepared in Serbian language. | Yes | | |
| 2.2 Quality and accuracy of information given in annual financial statements | The Mayor should ensure that the systematic plan of drafting of financial statements incorporates the request to include the entire amount of assets. The Mayor needs to monitor the implementation of this request. In the near future, we suggest to the committee established to continue with full evaluation of all fixed assets under the ownership of Municipality. | | | No |
| 3. Prior year recommendations | The Mayor should ensure that the revised action plan clearly sets forth a timeline for the addressing of recommendations with accountable staff members identified with the initial focus in those of a significant importance. | Yes | | |
| 4.4 Revenue (including own source revenues) | The Mayor should ensure that there will be a proper solution developed for software and it is tested during the current financial year in order to meet the management's specified requirements. | | Partly | |
| 4.4.4 Use of land without any criteria | The Mayor should implement a recording process of all properties leased and accompanying charges, which would at least once in six months be reviewed by a senior officer. Criteria should be set and competition implemented. | | Partly | |

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|--|---|-----|--|---|
| 4.4.5 Constructions without permit | The Mayor should ensure that Inspectorate Department applies all controls / mechanisms in order to denounce all investors who do not comply with the criteria to be equipped with construction permit, and observes the decisions issued by the management. | Yes | | |
| 4.4.6 Poor collection of the tax on the exercise of activity | The Mayor should ensure that controls dealing with the collection of these revenues are put in place, in order to ensure that the differences between the plan and collections are reduced. Identification of businesses operating and of those which are inactive should be constantly monitored. | Yes | | |
| 4.4.7 Incomplete evidence on the vehicle registration tax | The Mayor should ensure that the responsible person conducts full and accurate recording of the vehicle registration tax in order to be able to provide reliable reports at any time. | Yes | | |
| 4.4.8 Receipt of payments over €10 from informal education | The Mayor should ensure controls relating to collection of revenues, to ensure that differences between the invoices and receipt of payments in the Treasury are identified in time and procedures to find outstanding amounts are applied. Collections in the amount over €10 should be processed only through bank account. | | | Not yet, amounts over €10 are collected in schools and health |
| 4.5.1 Procurement - annex contract without a proper justification | The Mayor should ensure that technical service has prepared the bill of quantities and measures with all proper analysis in order to avoid the need for additional works. | Yes | | |
| 4.5.1 Procurement - windows priced at €120 are paid at €230 | The Mayor should investigate in detail reasons for these discrepancies and should apply measures for accountability for the persons involved. | Yes | | |

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|---|--|-----|--------|--------------------------------------|
| 4.5.1 Procurement – contract without sufficient commitments and inconsistency in payments | The Mayor should ensure not to enter into contracts without secured funds. The Oversight body should observe the construction dynamics at the site and not from the office, and to certify payments only after works are completed. A clearer report should be put in place between technical services and finances. | | | Lack of commitments in few contracts |
| 4.5.1 Procurement – payment of invoice without description of works | The Mayor should ensure that invoices made are in full accordance with contract conditions and services completed / accepted. | | Partly | |
| 4.5.1 Procurement services are applied without the director approval | The Mayor should ensure that every request is reviewed and approved by responsible management levels in order to decrease the manipulation possibility with the public means. | | | No |
| 4.5.2 Other expenditures – irrationality of advances for official trips | The Mayor should review the above cases and ensure that public means are returned in the budget, and such practices should not be repeated. | Yes | | |
| 4.5.3 Remunerations (wages and salaries) | The Mayor should ensure that a systematic review of Personnel Records is undertaken to ensure that the entire necessary documentation is included within a specified time period. | | | No |
| 4.5.4 Subsidies and transfers | The Mayor should put controls in place that the committee for evaluation of applicants is impartial, fair and transparent in the selection of beneficiaries. | | Partly | |

| | | | | |
|-------------------------------|---|-----|--|----|
| 4.6 Assets | The Mayor should ensure that recording and updating of asset records is done in all sectors of the municipality. | | | No |
| 4.6.2 Handling of receivables | The Mayor should prepare an action plan through which clear instructions will be proposed for all relevant municipality sectors for the increase of collections. The plan should contain priorities, allocations of debts by age, timeline for actions to be undertaken, reasons of non-payment, appropriate mechanism and discussion of achievements, at least twice a year. | | | No |
| 4.7 Handling of debts | The Mayor should ensure a detailed and real budget planning and that the use of funds is done based on a clear plan of cash flow, whereby not exceeding the allocated funds by any means according to economic categories. | Yes | | |
| 5. Internal audit system | The Mayor should ensure that an action plan is implemented, confirming the responsible officers and time for completion of actions. The special focus of internal audit should be the activities of current year with the effect of prevention of action. In addition, the establishment of the committee is recommended to be done in a near future. | | | No |