



REPUBLIC OF KOSOVA
OFFICE OF THE AUDITOR GENERAL

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**AUDIT REPORT ON THE FINANCIAL STATEMENTS OF THE
MUNICIPALITY OF PRIZREN 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 Prizren Municipality in consultation with the Assistant Auditor General, Qerkin Morina, who supervised the audit.

The opinion and report issued are a result of the audit carried out under the management of the Audit Director, Faruk Rrahmani, supported by Florim Maliqi (Team Leader), Agim Sogojeva and Nebojsa Ristiq.

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Executive Summary

Introduction

This report summarises the key findings from our audit of the 2013 Annual Financial Statements for Prizren 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 01.10.2013.

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 Prizren Municipality (including budget execution and management).

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:

Unmodified Opinion with an Emphasis of Matter

In our opinion the financial statements *present a true and fair view* in all material aspects.

Emphasis of Matter

We would like to draw your attention to the fact that records and information disclosed for fixed assets were not complete and accurate. The Asset Register did not include a vehicle received as donation from the Ministry of Public Administration and eight IT equipments were not recorded with purchase value.

(ISSAI 200 Unmodified Opinion with an Emphasis of Matter)

Overall Conclusion

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

- The current systems of internal controls do not provide sufficient assurance for the Management to successfully meet all its objectives. When it comes to the situation of Financial Management and Control, 16 recommendations were given in previous year report, out of which, the Municipality addressed only three, whilst others were either in process of addressing or were not addressed at all. This fact is an indication that the Municipality's management did not pay sufficient attention to adjustment of existing shortcomings;
- Although 2013 Annual Financial Statements were better prepared than in 2012, they still were not complete and accurate. Some of the errors were adjusted in the final version, but the Management failed to adjust all items. The unadjusted matter remains unfair presentation of the outstanding liabilities at the end of 2013, and incomplete presentation of assets;
- Revenue Management seems to be the key problem of the Municipality. During 2013, there was a lower turnout within Own Source Revenues of €319,352 or 7% compared with the previous year whilst receivables have exceeded over €11.6 million. The Management should have high priority focus for addressing this problem;
- Another important problem which continues repeating from year to year relates to increase of liabilities. Outstanding liabilities in the end of the year were €4,572,000. This amount included around 45% of the contingent liabilities;
- We noticed an exceeded number of employees in Education And Health Sector, and as a result, difficulties were faced when it comes to paying their salaries due to budget constraints;
- Systematic weaknesses were noticed in procurement starting from committing funds, following procurement procedures up to contract management. Contract management process was followed by inadequate controls, reports did not have any

clear specifications and there was a lack of technical acceptance for the works completed; and

- The Municipality made progress in asset recording, compared with the previous year, but what is up to the Management to do, is to record and evaluate assets by the end of 2014. In this context, Assets Register should be updated with all required information.

Although we managed to obtain assurance from controls in several areas of the financial statements, our considerations for Financial Management and Control highlighted significant weaknesses in some important areas of activity. This occurred especially in the area of Procurement, Budget execution according to cash flow, collection of revenues, Subsidies and Transfers as well as recording non-financial assets.

Auditor General's key recommendations are as follows.

The Mayor should ensure that:

- A revised action plan clearly sets out a timetable for addressing the recommendations made by the Auditor General with accountable staff members identified and with initial focus on those of greatest significance;
- The 2014 Annual Financial Statements production plan formally includes management review of the draft account with specific focus on high risk areas where errors have been identified in previous years;
- A detailed analysis of 2013 revenues is made ensuring completeness of receipts and that a robust process is in place in order to determine potential revenue flows in the coming years;
- Appropriate mechanisms for revenue collection, granting Subsidies and assets recording are activated with complete and accurate information with aim to further improve these areas where management shortcomings were noticed;
- An analysis is made why contracts were signed without sufficient funds being committed, especially in three last months of 2013 and that controls exist or were applied to ensure that procurement procedures were carried out only when funds are available; and
- The Findings and Recommendations in the draft report are considered, discussed and addressed at all levels of management; aimed at strengthening Financial Management and Control within the Municipality.

Management's Response - 2013 audit

The Management agreed with all 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 Auditor General's (AG) opinion on the AFS.

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

In our opinion the financial statements *present a true and fair view* in all material aspects.

Emphasis of Matter

We would like to draw your attention to the fact that records and information disclosed for fixed assets were not complete and accurate. The Asset Register did not include a vehicle received as donation from the Ministry of Public Administration, and eight IT equipments were not recorded with purchase value.

(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

Description

Our Audit Planning Memorandum, identified two significant risk(s) to the AFS related to the completeness of assets and completeness of third party payments. These are risks of material misstatement that may result in a modified opinion including an Emphasis of Matter.

The risk of material misstatement relating to the completeness of assets and third party payments occurred because no management action was taken to address the highlighted risk.

Identified Risk

Issue 1 - Incomplete reporting on assets

Assets owned by the Municipality over €1,000 were not completely recorded in the asset register, resulting in material misstatement within AFS notes.

Finding

During our interim audit, we have given advices to the Management for actions needed to be undertaken to ensure that the figures of assets within AFS are correct. However, risk identified is materialised given that the Management did not manage to apply required adjustments in internal control and we have confirmed that the asset value in AFS was not accurate.

Recommendation 1 High Priority - The Mayor should identify the appropriate actions in addressing these control weaknesses in order to allow a fair and true presentation of assets for 2014.

Issue 2 - Third Party Payments

The risk is identified but did not occur

The risk of material misstatement that we identified relating to the disclosure and presentation of Third Party Payments did not occur.

Audit Response

The payments made by the Ministries to the Municipality are clarified under the new Treasury Rule no. 03/2013 dated 31.12.2013, and they are not handled as Third Party payments given that they are payments from the Treasury Single Account.

We have reviewed the information of Municipality on Third Party Payments and we may conclude that the information is presented in a fair view.

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 Law on Public Financial Management and Accountability no. 03/L-048;
- AFS have been signed by CAO (Mayor) and CFO;
- AFS have been prepared within the required timeframe and submitted to MoF in Albanian and Serbian language;
- AFS have been prepared in hard and electronic copy; and
- The Municipality prepared and submitted regular quarterly reports to the Municipal Assembly and a copy to Minister of the Ministry of Finance during 2013.

We have noticed several shortcomings in the initial draft Annual Financial Statements which should be adjusted given that they were not in compliance with Financial Rule no.03/2013.

However, despite our persistence, even after some adjustments made, there are still some reporting issues which remain unchanged.

Issue 3 - Presentation of Annual Financial Statements - High Priority

Finding Note 28: Disclosure of liabilities at the end of the period, the Municipality failed to disclose the accurate situation of unpaid liabilities especially for category of Salaries. Liabilities in AFS were presented in the amount of €213,000, although they should have been €211,933; and

Article 30: The Statement of non-financial assets was incomplete, given that the assets register was not updated with information in terms of the value of assets received as a donation. This case relates to receiving a Mitsubishi type vehicle as a donation from by the Ministry of Public Administration. Further on, the purchase value for eight monitors was missing in IT equipment register.

Risk Shortcomings identified within assets and liabilities lead to a risk of incorrect reporting regarding 2013 AFS, having an impact in not meeting AFS statutory requirements.

Recommendation 2 The Mayor should ensure that the 2014 AFS production plan formally addresses all compliance requirements in terms of their preparation, i.e. Financial Rule 03/2013 and secure that there is a reporting line in place and managerial staff is responsible when reporting financial data drafted by CFO.

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 requests for financing capital projects to MoF;
- Quarterly reports including nine month financial statements in time; and
- Reports on debt submitted to MoF.

The self-assessment report for Financial Management and Control (FMC) rules and Annual Performance Report were not prepared.

Recommendation 3 Medium priority – the Mayor should ensure that external reporting requirements are fully met in order to achieve an effective reporting by the Municipality, in line with external reporting framework.

3 Prior Year Recommendations

Overall Conclusion

Our 2012 audit for the Municipality resulted in 16 key recommendations. Despite implementing an Action Plan for addressing 2012 recommendations, a number of significant issues remain to be addressed. However, the Management made efforts to address our recommendations. For a more thorough description of the recommendations and how they are addressed, see Annex II.

Issue 4 - Addressing Prior Year Recommendations - High Priority

Finding Only three prior year recommendations were fully implemented, nine were in process, whilst four have not been implemented by the time of our audit. The Management failed to apply a formal process for managing and monitoring the way AG's recommendations are being implemented. It is worth mentioning that the Management did not submit prior year audit report to the Municipal Assembly for discussion.

Risk Lack of a formal process for managing the implementation of the recommendations results in the inefficiency of the organisation. Consequently, the same shortcomings are being repeated from year to year. The continued weaknesses of internal controls in key financial systems resulted in:

- Ongoing organisational inefficiency and poor value for money; and
- Non-improvement of controls related to Own Source Revenues.

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

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 and the results of this action. 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 whether controls are well designed, have been implemented as planned and operate effectively. This requires an assessment of structures, processes and accountability lines introduced by the Management.

We also noticed that the Municipality did not consider self assessment in the context of PFM both in terms of PEFA and PIFC self assessment.

We found that controls over a range of expenditure areas require further enhancement to prevent the Municipality suffering financial loss, poor value for money and ineffective project management. The main areas where most improvements are required are Wages and Salaries, Procurement, Subsidies and Transfers and Own Source Revenues.

4.1 Good Governance

Description

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

Issue 5 - Weaknesses in High Level Management Controls

Finding We reviewed forms of the management controls applied within Municipality in terms of Revenues and Expenditures. The format of management reports does not provide explanations for variances against budget and budget forecasts are not updated on a monthly basis. The fact that during 2013, invoices from prior years were paid, as a result of non-timely reporting of liabilities refers to the fact that the reporting line did not operate as intended.

Risk Poor quality financial reporting to senior management reduces management's ability to actively monitor the Organisation's activities. Lack of proper reporting for all expenditures, i.e. unpaid invoices when they occurred increases the risk that the current year projects may not be executed.

Recommendation 5 The Mayor should review reporting aspect of respective directorates to determine the format of financial reporting which allows the Management to have proper and timely decision-making when it comes to progress and monitoring of processes.

4.2 Budget Planning and Execution

Description

We have considered the source of budgetary funds for the Municipality, 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 ²	2013 Outturn	2012 Outturn	2011 Outturn
Sources of Funds	33,628,746	35,157,505	31,780,415	30,274,489	32,018,274
Government Grant - Budget	27,509,666	27,614,666	27,324,442	25,683,770	26,073,953
Carried forward from previous year ³ -	0	1,114,900	887,220	976,455	1,436,952
Own Source Revenues ⁴	6,119,080	6,119,080	3,364,987	3,317,382	3,892,448
Domestic Donations	0	219,777	153,878	125,610	167,400
External Donations	0	89,082	49,888	171,272	447,521

The final budget, compared with the initial budget was higher by €1,528,759. This increase is a result of External and Domestic Donations totalling to €308,859 and revenues carried forward from the previous year, totalling to €1,114,900. The other part of €105,000 is increased in line with Government decisions.

The budget is spent 90% on the overall level. The main impact on this low percentage of execution relates to the poor collection level of Own Source Revenues, only 65% when compared with budget planning.

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	33,628,746	35,157,505	31,780,415	30,274,489	32,018,274
Wages and Salaries	14,925,000	15,151,374	15,139,595	14,856,794	14,403,387
Goods and Services	3,051,116	3,156,268	2,585,716	2,082,843	2,133,269
Utilities	841,861	841,861	804,029	802,795	638,218
Subsidies and Transfers	535,979	535,979	504,157	350,288	351,636
Capital Investments	14,274,790	15,472,023	12,746,918	12,181,769	14,491,764

Explanations for changes in budget categories are given below:

- The final budget compared with the initial budget for Capital Investments was increased under budget review by €1,197,233, whilst the expenditures rate for this category was 82% of the budget. This budget was planned to be spent on ongoing and new projects;
- The budget increase for Wages and Salaries by €226,374 as well as Goods and Services by €105,152 was a result of payments made for night-shifts within Main Family Health Centre;
- The budget increase for Goods and Services was made in order to cover the remaining debt from the previous year. Despite this, the level of debt at the end of the year for this category was €283,000. Budget for Utilities was not subject to any change compared with the initial budget, but €37,832 remained unspent within this category, whilst outstanding liabilities at the end of year for this category were €135,000;
- The Municipality also received Grants from Domestic and External Donors in the amount of €308,859, which were allocated for Capital Investments in order to co-finance the project for construction of road infrastructure, whereas €203,766 were spent; and
- Each year Own Source Revenues are under spent as a direct result of budget under spending given that Own Source Revenues are the last source of funding used. In 2014, the carried forward value of own source revenues is €883,066.

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

Description	Initial Budget	Final Budget	2013 Receipts	2012 Receipts	2011 Receipts
Own source revenues	6,119,080	6,119,080	4,020,374	4,339,726	4,999,000

As seen from Table 3, during 2013, the revenues declined by 7% compared with 2012 or 20% from 2011. Planning of revenues was poor, given that collection rate was only 66%. This led to failure of many financing planned from Own Source Revenues.

4.3 Revenues (including Own Source Revenues)

Description

The Municipality collects revenues from different sources such as: property tax, vehicle registration fees, business fees, construction licenses, revenues from rent, etc. Smaller sources of revenues include recording of births and deaths.

Issue 6 - Planned revenues - High Priority

Finding Planned revenues for 2013 were €6,119,080 whilst the amount collected was €4,020,374. Revenues collected during 2013 were lower by €319,352 than in the previous year.

Risk Whilst revenues in 2012 and 2011 had a normal flow, we have a significant decline in 2013 when it comes to the collection of revenues. The ongoing decline of revenues threatens the failure of municipality's projects, planned to be financed from Own Source Revenues.

Recommendation 6 The Mayor should comprehensively analyse the issue of revenues, in terms of planning as well as the establishing effective mechanisms for executing planned parameters. The Management should initiate a reassessment process, where all accounts are analysed in terms of age, significant amounts, realistic possibilities of collection and exercising administrative measures (if necessary).

Issue 7 Lack of mechanisms for collection of revenues - High Priority

Finding The Municipality planned to collect €1,370,000 for 2013 whilst it collected €1,479,900 or 108 % of planned revenues.

We analysed the aspect of invoicing for Property Tax in order to assess the planning issue. Invoiced value for 2013 was €2,096,919, whilst the Municipality planned to collect only €1,370,000. Planning of revenues from property tax was not either based on invoicing of the current year. Receivables from property tax until the end of the year were €6,399,000.

We tested 13 samples from the property tax in the amount of €49,606. We did not find any material irregularities from testing, but the Municipality still has problems collecting debts accumulated from year to year.

According to the municipal accounting register, revenues planned for business fees for 2013 were €630,000, whilst the total amount collected was €140,914 or around 22%. Although a decision was issued in 2012 for settlement of 2/3 of the debts when paying 1/3 of the debts, information on previous years' debts for business fees show that debts were collected in the amount of €4,343,000. Municipal inspectors failed to have an impact either through on-site visits or decisions, in collecting revenues from business fees.

According to the data from Treasury, revenues collected for construction licenses in 2013, were €373,822. Responsible officials were unable to provide complete records of all applications for construction licenses, including records on the number of applications approved and rejected.

Risk Poor planning for revenue collection will increase the potential for non-payment of invoices issued and lack of effective strategy to collect historic debt will reduce the Municipality's ability to have other self-financed projects and meet other expenditure plans.

Recommendation 7 The Mayor should ensure that the planning of revenues is based on realistic parameters in order to foster collection of revenues as much as possible. Further on, it should apply a systematic review in order to determine obstacles for increasing the current level of revenue collection and reducing the level of historic debts (including debts for business fees) and identify the options for improving the situation.

4.4 Expenditures

4.4.1 Procurement

Description

According to analytical review, expenditures for Capital Investments during 2013 were €12,746,918, whilst expenditures for Goods and Services were €2,595,716.

For testing purposes, we have taken 55 payments for Capital Investments in the amount of €5,248,788 or approximately 41% of the value of contracts and 17 payments from the category of Goods and Services in the amount of €893,512 or around 26%.

Issue 8 - Systematic Weaknesses in Procurement - High Priority

Finding In the Contract "Construction of City stadium" in the amount of €193,623, the amount committed for this project was only €20,000. We found cases of entering into contracts without sufficient funds being committed in 23 samples tested. CFO had no comment for such cases;

The contract "Paving the road "Pirana-Reti" amounted to €167,137- according to dynamic plan the project was foreseen to be completed for 50 days. We have noticed that this term was not adhered to. By the time of the audit, this delay reached 250 calendar days. According to the Management's claim, lack of funds for this project resulted in works being stopped and as such not finalised in time. We found such delays almost in every project examined.

Risk Entering into contracts without providing sufficient funding results in failure of the works, on one hand, and increases the risk for the Municipality to enter into obligations without having funds available and therefore it may be subject to certain penalties. Lack of funds causes project stagnation and also due to lack of funding, the Municipality cannot apply penalties for delayed days.

Recommendation 8 The Mayor should consider the Financial Rules and establish stronger controls on Procurement and Finance Department to prevent entering into obligations without having funds available. Besides securing funds beforehand, the Management should also strengthen controls on the monitoring of contracts.

Issue 9 - Non- systematic procurement weaknesses - High Priority

Finding

In the contract "Construction of road Krusha e vogel - Pirana" in the amount of €74,855 we found that the winner of the tender offered contract's performance security for 40 days shorter than the dynamic plan of works. The works were not completed within the performance security period, whilst the Municipality did not request a renewal of performance security. Performance security covered the period from 29.04.2013 to 08.06.2013 in the amount of €7,405.

In the case "Supply with industrial salt for winter road maintenance" a contract was signed in the amount of €19,920. We have analysed the content of the contract and noticed that Contracting Authority (CA) did not properly explain the matter of supply with salt for road maintenance in winter. The Municipality paid €15,000 to Economic Operator (EO) for supply with salt, but it failed to specify what will happen if there is no snowfall and no need for salt or who the owner of the salt is. We have not found that the salt is placed in the Municipality's warehouse. Thus, goods were not delivered in the Municipality's warehouse instead they were left in the EO's warehouse.

Risk

The performance security is an important instrument ensuring timely implementation of the contract and with good quality. In absence of performance security, CA does not have the chance to oblige the EO to act in line with the contract and it risks that the contract is not finalised.

Failure to clearly specify the terms of the contract, may cause unnecessary costs and damage the Municipality's funds.

Recommendation 9

The Mayor should ensure that the Procurement Department implements all the requirements stemming out from Tender Dossier, securing that it obliges an EO to adhere to all the terms of the contract through performance security. Further on, it should ensure that the Municipality establishes clear objectives before entering into any contractual agreement with EO, and ensure that the contract terms are favourable and justify the value for money spent.

4.4.2 Non Procurement Expenditure

Description

There are some aspects of other expenditure process where controls were not effectively applied.

Issue 10 - Lack of agenda for official travels - High Priority

Finding When examining two payments, one in the amount of €9,983 and the other in the amount of €2,772, we have noticed that payments were made for travels, i.e. visits to Albania. We have found neither the agenda for participation of 67 municipal officials nor the decision reasoning of this trip. The second payment was made for 14 women of the Municipality in honour of 8th of March feast. Officials were not able to prove that the expenditure for this activity was reasonable.

Risk Lack of participation agenda for municipal staff in Albania and failure to justify travel expenses increases the risk that public money is used in a non-justifiable way.

Recommendation 10 The Mayor should enhance controls to similar types of expenditures ensuring that expenditures are in function of operating activities within the Municipality, and as such are grounded and reasonable.

4.4.3 Remunerations (Wages and Salaries)

Description

Wages and Salaries are paid through a centralised system (payroll). Controls operated locally by the Municipality relating to: authorising payroll system, verifying of eventual changes and internal reconciliations.

The budget for Wages and Salaries for 2013 was €15,151,373, whilst € 15,139,594 was spent, or almost entirely. We tested 14 samples for this category, reviewing whether or not the payroll list is in line with the payroll system in the Ministry of Public Administration. We have also tested personnel files in order to verify whether the positions of officials and the multipliers are in accordance with contracts and payroll list.

Issue 11 - Teaching personnel outside the payroll - Medium Priority

Finding While testing the list of employees in Education Sector, we noticed that 21 employees are not paid for their work, although they have an employment contract. These employees were not listed in the payroll register. Teaching personnel does not exercise the right for salary and contributions made.

Risk Engaging staff in the educational process without providing funds for salaries, increases the risk that teaching personnel is not paid in time. This brings teaching personnel into financial difficulties, and besides this, the Municipality may also be subject to legal disputes.

Recommendation 11 The Mayor should ensure that staff recruitment is not made before salaries are secured. Further on, this case should be reviewed and all staff payments are made as soon as possible and such practices are not repeated.

Issue 12 - Unpaid obligations regarding salaries in MFHC and Education Sector - Medium Priority

Risk The information in AFS, the total amount of unpaid liabilities for salaries and remunerations at the end of the year was €213,000. Out of this amount, €175,823 relates to the Education Sector whilst the remaining €35,000 relates to Health Sector. According to the municipal officers, reason for unpaid debts was lack of funds.

Risk Insufficient planning of funds for salaries and other remunerations leads the Municipality to a risk not being able to pay for services rendered and burdens the budget of the coming year with current year debts.

Recommendation 12 The Mayor should ensure that the budget planning process for these two sectors is directly linked to the real needs covering the Wages and Salaries, taking into account previous years experience.

Issue 13 Non-compliance between salaries and contracts – Medium Priority

Finding When testing 14 personnel files, we found that in three contracts, there is a discrepancy between salary under the contract and salary as per payroll system. We have found that two employees for 12 months 2013 were paid more by €576. According to payroll, the third employee was paid more by €364 for 7 months than the contracted salary. We have not found any decision related to changing the salary, i.e. the increase of the multiplier for these three employees.

Risk Personnel Office failed to update personnel file and therefore incorrect payments occurred.

Recommendation 13 The Mayor should resolve this inconsistency, and determine whether these are just isolated cases or a widespread phenomenon. Depending on the situation, controls should be strengthened in order to prevent such cases.

4.4.4 Subsidies and Transfers

Description

According to analytical review, expenditures for subsidies in 2013 were €504,157. For purpose of testing, we have examined one sample unit of payment in the amount of €93,288 or around 19%.

The Municipality has a Regulation for allocation of Subsidies and Transfers, which was approved on 26.04.2013.

Issue 14 - Supplying before signing the contract - High Priority

Finding

The Municipality distributed packages of food for its staff as subsidy. The value of the contract signed with the Municipality to supply food package was €42,900. We found a list with signatures of 436 employees, but we are unable to verify items and supply values for each employee. Selection of EO was made without procurement procedures, and furthermore, a company selected owes the Municipality a rent for land.

Based on the Mayor's decision, on 16.10.2013 Football Club "Liria" was funded in the amount of €15,000. Except the payment and the decision issued by Mayor for these funds, the club did not submit any document such as request, pre-invoice, planning of expenditures or club's payroll list.

In one case, we have noticed that €14,799 was paid for wood supply for the families of martyrs and war invalids but the request and register of beneficiaries were not attached.

When testing two payments, one in the amount of €12,239 and the other in the amount of €11,299, we noticed that the payments were made based on supply with construction material for social cases. We were not provided with the register of beneficiaries regarding the construction material.

Risk

Weaknesses identified in the cases above indicate that payments for category of Subsidies and Transfers are not in accordance with the Financial Rules. We could not confirm whether the beneficiaries have received counter values which were charged in the name of Aids. This increases the risk that funds allocated for Subsidies are not spent as intended, with the possibility that in certain cases being misused.

Recommendation 14 The Mayor should ensure that when taking the decision on subsidies, legal grounds are reviewed. Further on, the Mayor should, for subsidies whether for material supplies or transfers of funds, request from relevant departments to maintain all information regarding the beneficiaries of these Subsidies and Transfers.

4.5 Assets and Liabilities

4.5.1 Capital and Non Capital Assets

Description

On 12.12.2013 the Mayor issued a decision for establishing an Evaluation and Inventory Committee for non-financial assets, but this committee did not yet finalise the work in order to ascertain the factual situation for non-financial assets within the Municipality. Section 2.3 contains more details regarding the assets.

Issue 15 - Lack of inventory report - High Priority

Finding An Asset Inventory Committee was appointed under Mayor's decision, at the end of the year. This Committee prepared a report on the physical situation of non-financial assets.

Risk Failure to carry out an evaluation and inventory of assets at the end of the year increases may result in assets records having inaccuracies, given that the existence of assets cannot be confirmed. In such conditions, the assets are exposed to the risk of loss, misuse or write-off. Therefore, the report of assets in the AFS cannot be reliable.

Recommendation 15 The Mayor should ensure that the appointed Assets Inventory Committee, within a certain period of time physically records assets in order to compare them with accounting, and clarify all possible differences. Further on, recording of assets over €1,000 should be an ongoing process until all assets are recorded.

4.5.2 Handling of Receivables

Description

The Municipality reported receivables from property tax in the amount of €6,399,000; other business licenses amounted to €4,343,000, trade receivables of €242,000 and other fees in the amount of €673,000. Therefore, the total value of receivables at the end of 2013 was €11,657,000.

Issue 16 – Collection of receivables - High Priority

Finding When analysing the revenues, it is clear that the receivables have an increasing trend, from year to year, including all categories of assets. The collection rate on all grounds is below average and the Management of the Municipality does not seem to have a strategy how to resolve this problem. The amount of receivables of €11,567,000 is significant for the municipal budget. The decreasing trend of collections over the years is not understandable. For example, municipalities in 2011 from the property tax collected 1 million Euros more than in 2013.

Risk A poor planning of revenues and lower rate of collections has direct impact on meeting the overall objectives of the Municipality, especially the implementation of capital projects from Own Source Revenues.

Recommendation 16 The Mayor should introduce a comprehensive approach when addressing this problem, both in terms of planning and establishing effective mechanisms to reduce these debts to an acceptable level. The Management should initiate a reassessment process, where all accounts are analysed in terms of age, significant amounts, realistic possibilities of collection and exercising administrative measures (if necessary).

4.6 Handling of Debts

Description

The statement of liabilities not paid to suppliers at the end of 2013 was €2,485,000. These liabilities are carried forward to be paid in 2014. However, this only reflects part of the budgetary challenge given that the Municipality had contingent liabilities in the amount of €2,087,000. Municipality's debt at the end of 2013 amounted to a total of €4,572,000.

Issue 17 - Entering into obligations above budget appropriations

Finding According to our examination, we noticed that the Municipality entered into obligations above appropriations. Funds allocated for Wages and Salaries were €15,151,373, whilst the remaining obligations were €213,000. Utilities were €804,028 and outstanding liabilities were €97,167 more than appropriations, and expenditures on Subsidies and Transfers exceeded the budget by €43,178. These figures may be even higher based on the fact that during 2013 invoices were paid but not presented in 2012 Annual Financial Statements.

Risk The Municipality failed to handle and manage debts properly and as a result the 2014 budget will be spent for paying the remaining liabilities of 2013. This shows poor planning and no financial discipline.

Recommendation 17 The Mayor should provide a detailed and realistic budget plan and the funds are used based on a clear cash flow plan, not exceeding the funds allocated under the economic category.

4.7 Internal Audit System

Description

The Internal Audit System (IAU) is a key part of internal control and therefore the existence and proper functioning of the IAU is an important part of internal control.

IAU in 2013 planned five audits, four of which covered 2013. Audits were focused in the field of Procurement, Own Source Revenues, Subsidies, the Office for Communities and Return recommended by the Mayor. IAU met 80% of the audit plan and as a result managed to come up with some valuable recommendations for the Management.

Issue 18 - Failure to implement the recommendations - High Priority

Finding

We noticed that the Management did not have any action plan for addressing IAU recommendations. For all audited areas, appropriate recommendations were given for improving processes, but the implementation rate was quite poor.

The Audit Committee held four meetings during 2013 and reviewed the work of the Internal Auditor. From the minutes of Committee's meetings, we noticed that they supported the work of the internal auditor and considered his recommendations. They also took into consideration the recommendations from external audit report for previous year which should be fully addressed. Despite this, the management took into consideration only the previous year recommendations and advices from audit memo, but they were not addressed by the officers responsible for implementation.

Risk

Lack of management's readiness to address the recommendations made by the Internal Audit led to many irregularities which were not avoided or adjusted in time and as such they still continue to be present.

Recommendation 18 The Mayor should address recommendations arising from internal audits, delegating responsibilities to the staff responsible for implementing the recommendations. It should also ensure that in addition to the readiness for addressing the recommendations, this process is also monitored on regularly basis.

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 AFS	AFS preparation for 2013 with all requirements and financial rules.		Partly	
3. addressing prior years recommendations	Drafting an action plan clearly sets out a timetable for addressing the recommendations.	yes		
4.4 Revenues	Ensuring a comprehensive approach on handling revenues, in terms of planning and in terms of establishing mechanisms for effective collection of revenues.		Partly	
	Establish an accurate database on the number of applications filed for licenses, licenses issued and those rejected.		Partly	
	Ensure that all contractual obligations are implemented by leaseholders on regular monthly basis.			No
	Should enhance its activity to increase collection from business fees.		Partly	
4.5 Expenditures	Ensure that in all procurement cases, bids are evaluated objectively.		Partly	
	Ensure that proper controls are in place in order that such situations are not repeated.	yes		

	The needs for supplies are planned better, in order that there is no splitting of tenders.			no
4.5.2 Wages and Salaries	To ensure that personnel files are timely updated		Partly	
4.5.3 Subsidies and Transfers	To approve Regulation on subsidies and transfers	yes		
	Ensure that expenditures for subsidies are made in line with the initial allocations.		Partly	
4.6 Assets	To ensure that assets purchased and received as a donation are registered.		Partly	
	To ensure that asset management is made in line with AI on administrative management.		Partly	
4.7 Handling of debts	To ensure that the Municipality mechanisms should make a detailed and realistic budget planning and budget spending is made according to a cash flow plan by not exceeding funds allocated.			no
5. Internal audit system	To secure an action plan for the recommendations given by the IAU is prepared.			no