



**REPUBLIC OF KOSOVA
OFFICE OF THE AUDITOR GENERAL**

Document No: 22.13.1-2014-08

**AUDIT REPORT
ON THE FINANCIAL STATEMENTS OF THE MUNICIPALITY OF
RAHOVEC FOR
THE YEAR ENDED 31 DECEMBER 2014**

Prishtina, June 2015

The Office of the Auditor General undertakes both Regularity and Performance Audits. The Acting Auditor General 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 Acting Auditor General has decided on the audit opinion and report on the Annual Financial Statements of the Municipality of Rahovec in consultation with the Assistant Auditor General, Qerkin Morina, who supervised the audit.

The opinion and report issued are a result of the audit carried out under the management of the Audit Director, Florim Beqiri, supported by Mehmet Muçaj (Team Leader), Faik Thaqi and Elvir Krasniqi (team members).

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Executive Summary

Introduction

This report summarises the key findings from our audit of the 2014 Annual Financial Statements of the Municipality of Rahovec, 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 2014 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 01.12.2014.

Our audit focus has been on:



The level of work undertaken by the Office of the Auditor General to complete the 2014 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, except for the following cases:

The Municipality made a wrong classification of expenditures, thus paying from Capital Investments category for Goods and Services and Subsidies, the amount €191,613. The Capital investments are overestimated with €191,613 and the misclassification of the same in the Goods and Services and Subsidies and Transfers are underestimated with the same sum.

In article 13, Budget Execution Report – the cash inflow and the cash outflow revenues (in the final budget column), are understated with €67,554. Furthermore, the donations are presented in the amount of €30,000 at the execution column, while it should be €15,844.

Emphasis of Matter

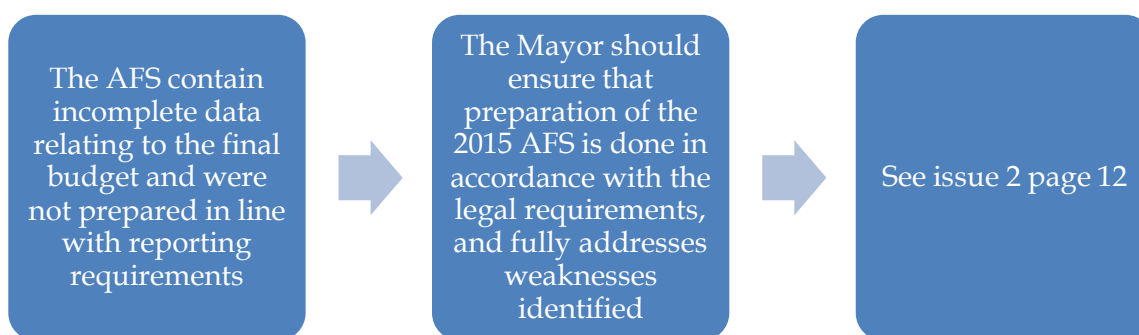
We would like to draw your attention to the fact that the disclosure of Fixed Assets is not complete since the accounting register does not contain 28 municipal vehicles.

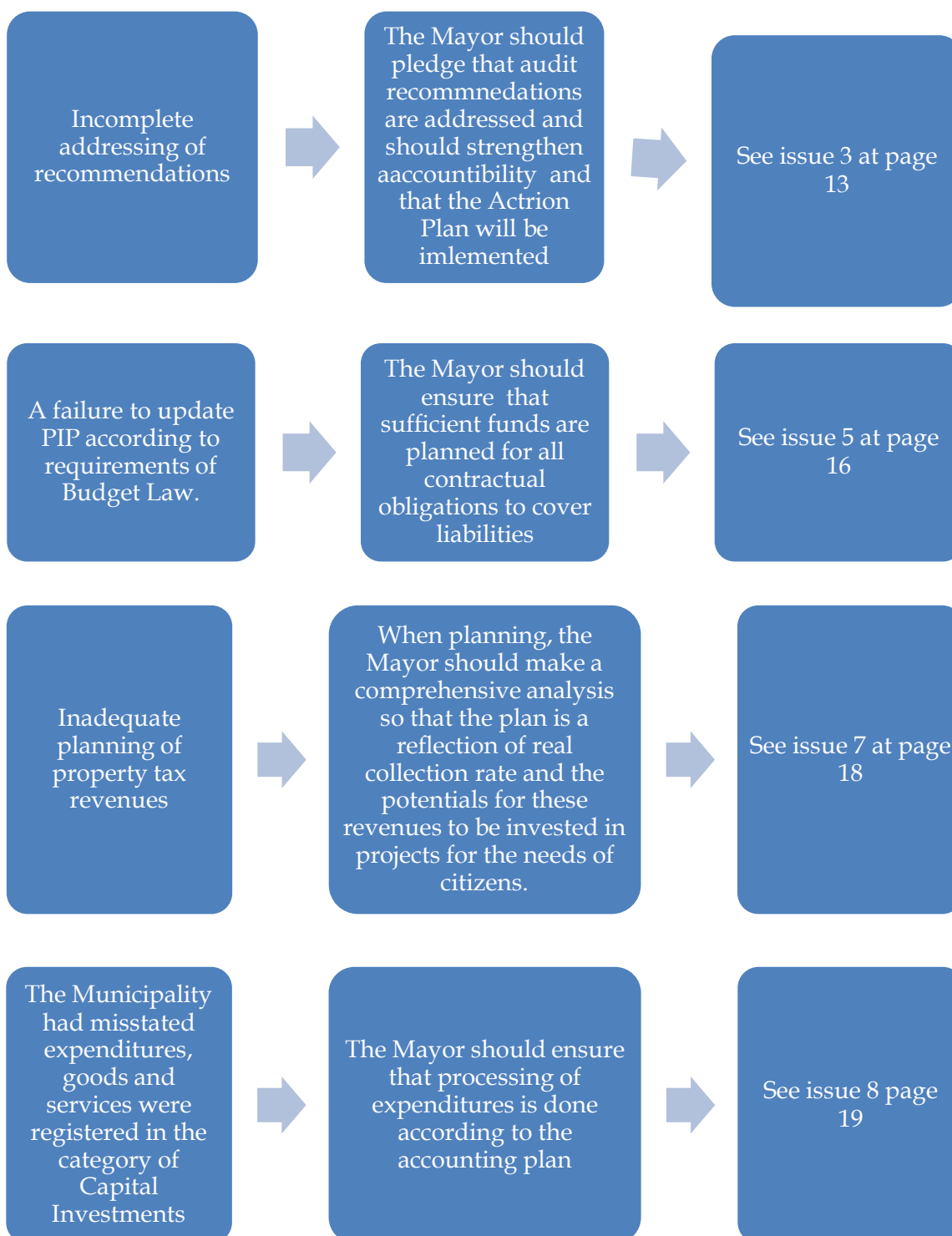
(ISSAI 200/1705: Qualified Opinion with Emphasis of Matter).

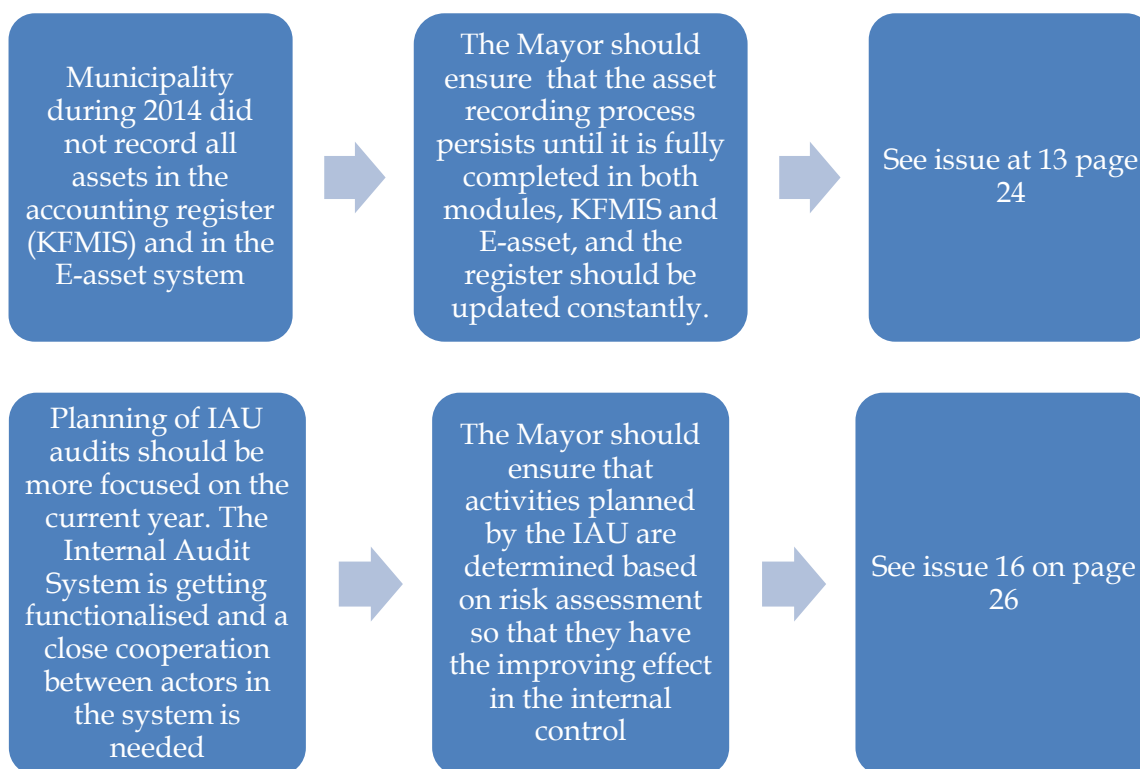
Overall Conclusion

Municipality management has designed internal control system at a satisfactory level, although the system needs for an enhanced monitoring, to ensure that internal controls act effectively and efficiently.

Our key conclusions and recommendations are:







Management's Response – 2014 audit

The detailed audit findings and conclusions in this report have been considered by the Municipality. The Management's responses where we have not reached a common position are detailed in Annex III.

We take it for granted that the Mayor:

- Table the Audit Report for discussion in the Local Assembly; and
- During January/February 2016 initiate a discussion in the Local Assembly regarding the implementation of the Action Plan on audit recommendations, before AFS 2015 are submitted to Ministry of Finance.

1 Audit Scope and Methodology

It is the responsibility of the Municipality management 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:

- 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. Management activity also determines the focus of our compliance audit and good governance audit which do not directly impact on the opinion.

Our audit approach to governance is focused on evaluating the actions taken by management to secure effective financial management and control and the results of this action in efficiently delivering high quality operational outputs. 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 management including the role undertaken by Internal Audit and Audit Committees as well as inbuilt system controls.

The following sections provide a more detailed summary of our audit finding with emphasis on observations and recommendations in each area of review. An assessment of how the Management have addressed recommendations made in the report on 2013 may be found in Annex II.

For completeness we have included issues identified at the interim audit where they remain relevant. At the interim audit stage we provide advice to enable relevant action to be taken in advance of the AFS production and final audit.

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.

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

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

2 Annual Financial Statements and other External Reporting Obligations

Introduction

Our review of the AFS considers both compliance with the reporting framework, and the quality and accuracy of the information recorded in the financial statements. We also consider the Declaration made by the Mayor 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.

Overall Conclusion

Our overall conclusion relating to AFS is that a number of errors have been identified with the presentation of final budget, misclassification of expenditures, inaccurate asset recording, while relating to reporting requirements they were met.

2.1 Audit Opinion

In our opinion the Annual Financial Statements *present a true and fair view* in all material aspects, except for the following cases:

The Municipality made a wrong classification of expenditures, thus paying from Capital Investments category for Goods and Services and Subsidies, the amount €191,613. The Capital investments are overestimated with €191,613 and the misclassification of the same in the Goods and Services and Subsidies and Transfers are underestimated with the same sum.

In article 13, Budget Execution Report – the cash inflow and the cash outflow revenues (in the final budget column), are understated with €67,554. Furthermore, the donations are presented in the amount of €30,000 at the execution column, while it should be €15,844.

Emphasis of Matter

We would like to draw your attention to the fact that the disclosure of Fixed Assets is not complete since the accounting register does not contain 28 municipal vehicles.

(ISSAI 200/1705: Qualified Opinion with Emphasis of Matter)

2.2 Significant Risks to the Annual Financial Statements

Description

Our Audit Planning Memorandum dated 01.12.2014 identified only one significant risk related to the completeness of assets and their presentation to AFS. At the interim audit stage, we provide advice that assets should be recorded in the accounting register and at the subsequent audit stage, we found that municipality had still not taken actions required to record all assets in the accounting register.

Identified Risk

Issue 1 - A failure to record all assets in KFMIS owned by Municipality will result in material underestimation of the AFS assets values

Audit response and Findings

We have assessed the controls implemented by management to prove the completeness of asset records. In our interim audit memorandum, we provide advice to management on the action required to ensure that the assets figure in the AFS was correct and complete. However the risk identified has materialised because management has been unable to implement the necessary improvements in internal control, despite the actions taken. We have confirmed that assets values recorded in the AFS are incomplete, because 28 vehicles were not recorded in KFMIS and some municipality properties.

Recommendation 1 High Priority - The Mayor should establish a commission represented by municipality key sectors, which we also suggest to include an officer from Cadastre Municipal Department, and complete the recording of all properties not recorded. This commission should prepare a summarised report, reporting on all registration results and eventual challenges, and should be presented to management. A key role in this process should be played by the assets officer, to make recording provided by this commission in KFMIS. A systematic monitoring of this process needs to be done directly by the Mayor.

2.3 Compliance with AFS and other reporting requirements

Description

Municipality is required to comply with a specified reporting framework and other reporting requirements. It has met the following reporting requirements:

- Compliance with Financial Rule no. 03/2013;
- Requirements of LPFMA no. 03/ L-048;
- Whether AFS are submitted to Ministry of Finance (MoF) within the time framework;
- Whether AFS are signed by CEO and CFO;
- Whether AFS are received in Albanian; and
- Submission of regular quarterly reports to Municipal Assembly and to Minister of the Ministry of Finance (MoF) during 2014.

The Municipality prepared the AFS within the legal time period, modified them on 19.03.2015, and submitted them to MoF.

Issue 2 - AFS preparation process - High Priority

In article 13, of the budget execution report - the cash inflow, in the final budget column, the revenues were represented less by €67,554. The value presented was €950,000, while it should be €1,017,554;

In article 13, the cash outflow in the final budget column, presented the amount of €10,839,000, while the final budget should be €10,907,411. Thus, a mismatch of €68,411;

At the execution column, the donations are presented in the amount of €30,000 while it should be €15,844; and

There were expenditure misclassifications made, where Goods and Services, and Subsidies in the amount of € 191,613 were paid from Capital Investments category.

Risk

Declaration of the Mayor and CFO on AFS 2014 is not fully reliable. Inaccurate presentation of data in AFS and errors identified in the amounts recorded lead to a misunderstanding of financial position of municipality. The budget amount presented inaccurate and the misclassification of expenditures have resulted in the Modification of Opinion.

Recommendation 2

The Mayor should identify reasons behind misstatements made in AFS and ensure that the final review processes by management are improved when 2015 AFS are submitted. The Mayor and CFO should not sign statements without being ensured that errors are identified and adjusted prior to AFS being submitted to Government.

3 Prior Year Recommendations

Overall Conclusion

The Municipality submitted in time the plan for addressing prior year recommendations. However, some prior year recommendations were not addressed, and still some time is needed to for complete implementation.

Description

Our Audit Report on the 2013 AFS of Municipality resulted in 16 key recommendations. At the end of our 2014 audit, five (5) recommendations have were fully addressed; six (6) were partially addressed; and five (5) have not been addressed yet. For a more thorough description of the recommendations and how they are addressed, see Annex II.

Issue 3 - Addressing Prior Year Audit Recommendations - High Priority

Finding Municipality did not addressed a number of recommendations. The Municipality management has not implemented a formal process to monitor how recommendations are implemented. As some of the issued raised in the previous year audit were not handled properly, some prior year errors and weaknesses have repeated this year.

Risk A failure to implement recommendations has resulted in continued weaknesses in internal control systems. This resulted in: inaccurate AFS; a failure to comply in full with the regulation on subsidy awarding, poor assets management and insufficient benefit from internal audit.

Recommendation 3 The Mayor should ensure that an action plan is not produced only to meet a formal requirement, but should be a practical guide for the implementation of all recommendations. The document as such should clearly sets out a timetable and accountable staff members for implementation of activities, with initial focus on those of greatest significance. The implementation of this plan should be monitored by the Mayor on regular basis.

4 Governance

Overall Conclusion

Strong governance supports effective planning, implementation and monitoring of municipality activities. Significant weaknesses have been identified in the governance aspect. Budget planning procedures are weak and due to this, the Municipality of Rahovec for 2014 did not approve the budget at the Municipal Assembly in time. The budget from the municipal assembly was approved on 26.02.2014. Budget for 2014 was the same as the budget for 2013. A failure for the budget to be approved at the Municipal Assembly in time increases the risk for capital projects not to be included in the subsequent budget and the funds foreseen according to budget categories are not in line with real needs.

Municipality has made no FMC self-assessment and has not drafted any plan for risk management.

We found that while controls over budget planning process and revenue are not good and have not been consistently analysed. Controls over a range of expenditure areas require further enhancement to prevent Municipality suffering financial loss, poor value for money and ineffective project management.

4.1 Budget Planning and Execution

Description

We have considered the sources of budgetary funds for the Municipality of Rahovec, spending of funds by economic categories and revenues collected. For more, this is highlighted in the following tables:

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

Description	Initial Budget	Final Budget ¹	2014 Outturn	2013 Outturn	2012 Outturn
Sources of Funds	9,774,525	10,907,411	10,463,701	10,067,841	10,276,518
Government Grant -Budget	8,824,525	9,691,929	9,530,093	9,148,202	9,061,614
Carried forward from previous year ² -	0	168,163	166,113	188,362	333,620
Own Source Revenues ³	950,000	1,017,555	737,857	680,000	615,107
External Donations	0	29,764	29,638	51,277	266,177

The final budget is higher than the initial budget by €1,132,886. This increase is a result of External Donations (€29,764), own source revenues collected (€67,555) more than planned, revenues carried forward from previous year (€168,163) and increase of Government grant due to the raise of salaries (€867,404). The final budget for 2014 was executed at the level of 96% of the plan, which in an execution aspect presents a very effective performance.

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

Description	Initial Budget	Final Budget	2014 Outturn	2013 Outturn	2012 Outturn
Spending of funds broken down by economic categories	9,774,525	10,907,411	10,463,701	10,067,841	10,276,518
Wages and Salaries	5,365,372	6,254,282	6,228,063	5,330,305	5,361,722
Goods and Services	733,893	770,391	634,577	693,593	939,328
Utilities	257,260	257,260	226,174	271,208	292,565
Subsidies and Transfers	100,000	106,128	105,951	93,845	94,141
Capital Investments	3,318,000	3,519,350	3,268,936	3,678,890	3,588,762

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

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

³ Own source revenues budgeted and spent.

Explanations for changes in budget categories are given below:

- The biggest difference occurred within the category of Wages and Salaries. The Government of Kosovo from April 2014 took a decision to raise salaries by 25% for all public sector categories;
- Budget execution for Goods and Services was only 82% because MoF has not allocated 15% budget for Goods and Services; and
- A lower budget execution rate is found within Capital investments, where at the end of the year, funds not used recorded by 7% (about €250,000).

Table 3 Own Source Revenues collected – outturn against budget (in €)

Description	Initial Budget	Final Budget	2014 Outturn	2013 Outturn	2012 Outturn
Own source revenues	950,000	1,017,555	1,017,555	842,364	800,404

Since municipality budget for 2014 was not approved at the Municipal Assembly, MoF allocated the same amount as 2013 (€950,000) as the budget planned for the collection of own source revenues. During 2014, this amount was exceeded by €67,000 and as is seen in the table, the amount collected was €1,017,555.

Issue 4 – Payments according to court decisions and Article 39.2 of LMFMA – High Priority

Finding Based on court decisions, Treasury executed direct payments in the amount of €36,008 and 323,550 during the year 2014 from the budget account of the Municipality of Rahovec, according to Article 39.2 of LMFMA 323. These funds were spent to pay the obligations of previous years, forwarded in 2014.

Risk The amounts of payments executed according to court decisions and Article 39.2 of LMFMA are significant for the municipality budget and impact on the misbalance of budget. Such payments increase the risk that projects planned is not carried out and may also have effects in the activities of municipality.

Recommendation 4 The Mayor should ensure to make a sound budget planning, strengthen financial discipline for the execution of payments in time and should review all overdue obligations in order to eliminate such budget disorders.

Issue 5 – Public Investment Programme (PIP) – High Priority

Finding Municipality does not maintain and update the Public Investment Programme (PIP). In 12 cases, we found that Municipality had not updated projects in PIP, as is required under Article 7.2 of the Budget Law. Law foresees that no later than 30 (thirty) days after the issuance of full appropriations for the 2014 fiscal year, budget organisation should make necessary budget changes to meet the unpaid financial obligations from the previous year related to multi annual capital projects. Such a thing was not done by municipality.

Risk Municipality has got a poor management of this programme. A failure to plan sufficient financial funds for capital projects for which Municipality has contracts, increases the risk for Municipality to make compulsory budget cuts during the year in other approved projects by Assembly, and potentially increases the risk for subject to indictments.

Recommendation 5 The Mayor should ensure that budget is planned consistently for all multi annual projects and that the PIP system is used as intended.

4.2 Revenues (including own source revenues)

Description

The Municipality has no sufficient controls established relating to the collection of own source revenues. There is a need for improvement of some processes to support the collection of revenues. At the interim audit stage, we provided advice that revenues should be recorded in adequate codes and we consider that Municipality has taken measures to address this advice. Despite this, we identified the following issues:

Issue 6 – A failure to collect rents for municipal properties – High Priority

Finding The Municipality in 2014 undertook no concrete actions over users who failed to meet financial obligations for municipal properties which were under short term use. We identified two cases, where contracts for giving municipal preemies on rent, were on expired terms, while the user continued to use these premises. In four cases, we identified that users of municipal premises had not met financial obligations against municipality. The annual charge for four (4) cases was €24,536 while accumulated debts during the previous years were €94,227.

Risk Controls applied over rent revenues are ineffective. Continuing to use municipal properties in absence of valid contracts is in contradiction with Law. Moreover, legally, the municipality has not right to collect rents and this increases the risk that these financial taxpayers may reject their obligation and revenues may not be collected at all.

Recommendation 6 The Mayor should ensure that the agreed terms of contracts with lessees are strictly adhered to. For cases assessed that rents cannot be collected, contracts should be terminated and public auction procedures initiated for giving properties for use.

Issue 7 – Inadequate property tax revenue planning– Medium Priority

Finding The Municipality planned property tax revenues in the amount of €220,000 while the invoicing for 2014 was €323,229. The collection of these revenues was in the amount of €301,698. The planning process was not subject to any sustainable analysis. There are huge discrepancies between planning, invoicing and collection.

Risk Due to poor analysis in the planning process, the amounts collected from property tax have exceeded the plan by 37%. This has not occurred due to municipality's efficiency in tax collection, but rather, due to unrealistic forecast / underestimation of plan. Such a situation makes also difficult the project planning to be financed by own source revenues.

Recommendation 7 When planning property tax budget, the Mayor should ensure that the planning process is preceded by an analysis of trends achieved during previous years, with specific focus on the level of invoicing. In addition, municipality should implement more effective processes in tax collection.

4.3 Expenditures

4.3.1 Procurement

Description

The Municipality in 2014 spent €4,129,688 for the category of Capital Investments and Goods and Services. We tested 66 payments in the amount of €1,045,116 or 25% of expenditures for Goods and Capital Investments and 10 samples for the procurement activities in the amount of €1,594,232.

Our review has identified the following weaknesses:

Issue 8 – Systematic Weaknesses in Procurement – High Priority

Finding

The Municipality in 2014 entered into contractual obligations bigger than the allocated funds in the Law on Appropriations. We identified three cases “Asphalting of the road Pastasel-Kaznik”, “Construction of the primary school in Opertushë”, “Construction of joint residential building for families in need”. The amount of budget allocations in cases mentioned above for three years was €475,400, while the value of contracts entered into for three projects was €1,265,863. The deficit of funds in relation to the contracts entered into was €790,463;

The Municipality during 2014 did not notify in writing eliminated or unsuccessful Economic Operators (EO) from tenders. We identified three cases in which Municipality did not notify EOs in writing.

In three procurement procedures (for framework contracts) we identified that the Municipality has not foreseen the forecasted amount of supplies in the tender dossier, as is foreseen by Law on Public Procurement; and

In 19 cases (payments), the Municipality made misclassification of expenditures in the total amount of €191,613. Payments were recorded in the Capital Investment category, while the nature of expenditures was Subsidies, respectively Goods and Services.

Risk

Entering into contracts by municipality without commitment of sufficient prior funds, not foreseen under the Midterm Budget Framework, increases the risk that such projects are delayed, or not completed at all. Half-finished projects, also bear the real risk to be damaged by atmospheric conditions and then repaired before given for use. A failure to foresee approximate quantity increases the risk for EOs to provide a quantity of unnecessary items and disorienting prices. Misclassification of expenditures impacts on the presentation of Capital Investments over values which in reality are spent in this category.

Recommendation 8 The Mayor should initiate better control of contract procedures and legal requirements securing that contractual obligations are not entered into before budget funds are committed. Long-term commitments should be harmonised with project dynamics and should be planned with the Midterm Budget Framework (MTBF). Further, procurement requesting units should conduct approximate assessments for purposes of supply/purchases in cases of framework type contracts, and expenditures processing should be done according to accounting plan.

Issue 9 – Non systematic procurement weaknesses – High Priority

Finding Municipality did not conduct procurement procedures for insuring municipal vehicles. We identified that Municipality paid €2,803 for the insurance of 12 municipal vehicles. Payments without procurement procedures are in contradiction with Treasury Financial Rule 01/2013 and Law on Public Procurement.

Risk Avoiding procurement procedures increases the risk for municipality to pay more expensive services than the market price.

Recommendation 9 The Mayor should ensure that procurement procedures are used in all cases when this is applicable.

Issue 10 – Change of positions of contract in the process of execution of works – High priority

Finding On 02.09.2013, the Municipality entered a contract for the construction of a drainage channel for agriculture lands in the village Celinë in the amount of €437,858. This project, according to contract is foreseen to be finished within three years. We identified that during the contract execution, substantial changes were made in the contract positions without the prior municipality management approval in writing, but only with the consent of the oversight body. According to the contract, the channel was supposed to be open made of concrete. It is being constructed as a closed channel with concrete tubes. Payments made so far were €80,000. Due to huge changes in contract, we were unable to arrive at an assurance whether works done to date in the project are equivalent to the counter value of the money spent.

Risk Change of contract terms (positions) led to the change of project. Such situation brings other bidders at an unequal situation, because after the change of positions of works, the prices they offered with could have been different to the ones initially given. This increases the potential that the price for new works is higher than the competition price. The potential risk is that this may threaten achievement of the project purpose. We are not certain whether the value for money is achieved, and this may cause financial losses to Municipality.

Recommendation 10 The Mayor should review the contract and analyse in detail reasons behind the change of positions and should undertake immediate measures in order for the project to meet the intended purposes. Eventual amendments in contracts are decided on the foreseen level.

4.3.2 Other expenditures

Issue 11 – Payments through Memorandum of Cooperation – High Priority

Finding

The Municipality during 2014 signed some Memorandum of Cooperation. We reviewed the contents of Memoranda and we found the following issues:

On 25.04.2014, municipality entered into a Memorandum of Cooperation with Caritas Kosova for increasing the quality of home and outpatient clinic health services for the citizens of Rahovec Municipality and rural areas. The value of this project was €70,000. The Municipality, according to agreement, participates with €55,000. Caritas Kosova within this project would provide a vehicle with eight (8) seats for the needs of the transporting persons under dialysis regime. Caritas Kosova did not provide this vehicle and did not conduct such services laid out in the agreement. Municipality paid the total amount in the Caritas account according to the agreement from Capital Investment category, as follows: €30,000 (12.05.2014); €10,000 (22.07.2014); €1,781 (13.10.2014) and €13,219 (04.12.2014). The Municipality money was used by Caritas Kosova for covering the expenditures for 28 health sector employees (5 dentists, 7 physicians and 16 nurses). These employees according to Medical Family Health Centre (MFHC) data were engaged in MFHC, Family Health Centre (FHC) and Outpatient Care (OC) in rural areas. Payments made by municipality for Caritas Kosova had only one invoice attached, and the invoice description states payment to be allowed according to memorandum.

On 09.12.2014, Municipality entered into an annex contract for sketching a conceptual project which aims at regulating the halls for haemodialysis services and carry out the process in full for disinfection, disinsection and deratisation of health and municipal premises in Rahovec. The value of this annex was €20,000. Municipality participates with €16,782, while the contribution of Caritas Kosova will be €3,218 for special beds for the haemodialysis ward, invalid wheelchairs, etc. On 10.12.2014, the Municipality paid the amount of €16,781 in the bank account of Caritas Kosova. An invoice was attached stating that the payment based on annex agreement. The Municipality has no information whether or not Caritas has defined its part of the annexed agreement.

On 26.12.2013, the Municipality entered into an agreement with CDF (Community Development Fund) for the central heating system in the school premises in the village Xërxe. The agreement foresaw that Municipality will participate with 17% or €8,213. According to the agreement, Municipality will transfer to the account of CDF, funds prior to signing the contract. On 06.02.2014, Municipality paid the amount of €8,213 based on the agreement. According to a report, works for this project were completed on 03.03.2014.

Risk Around €79,000 was up front paid under these agreements. It is not clear to what extent services / works foreseen in the agreement are completed by partners. Payments made by municipality prior to services or work completed increase the risk for not achieving the value for money and projects may not be finished according to agreements, and are with poor quality.

Recommendation 11 The Mayor, prior to signing agreements in the future, should ensure that payment agreements are revisited ensuring transparent reporting during and after the finalization of the projects as basis for monitoring and evaluations of value for money.

4.3.3 Remunerations (Wages and Salaries)

Description

Budget for the category of Wages and Salaries was €6,245,282, while the expenditures for 2014 were €6,228,063 or 99.7%.

Wages and Salaries are paid through a centralised system. The key controls operated at the local level from municipality deal with a) monthly payment control by signing the salary list, b) verification of potential changes that may be presented through forms, c) budget review for this category and reconciliations with Treasury.

Regarding the category of Wages and Salaries we reviewed the compliance of employment contracts with Ministry of Public Administration (MPA) payroll system.

Recommendations

We have no recommendations in this area.

4.3.4 Subsidies and Transfers

Description

The Municipality for 2014 had a final budget for Subsidies in the amount of €106,128, which was almost spent in full (€105,951).

We reviewed the process of subsidy granting. After testing a sample unit selected out of nine (9) cases in the amount of €13,800, we identified the following issues:

Issue 12 – Weaknesses in the implementation of Regulation on Subsidies - High Priority

Finding Municipality has not complied with the internal regulation on subsidy granting in full. In 2014. The Municipality subsidised the football club “Rahoveci” in the amount of €11,300 without meeting the criteria set forth in the internal municipal regulation;

Municipality supported SH.K.A “Anadrinia” with €3,500 for organising a traditional festival. According to internal municipal regulation, subsidies over €2,000 should be approved by the Municipal Assembly, while they were approved by the Mayor; and

Risk Subsidy granting without complying with criteria set forth in the internal municipal regulation presents a risk that internal controls are not complied with and subsidies do not achieve objectives intended.

Recommendation 12 The Mayor should ensure that the internal municipal regulation for subsidy granting is implemented properly.

4.4 Assets and Liabilities

4.4.1 Capital and Non Capital Assets

Description

Our audit identified strengthened municipality process in recording assets in KFMIS compared to previous year. In 2013 AFS, the value of assets was €89,129,219, while in 2014, the Municipality value was €43,699,997. The assets were decreased with the value of €45,429,222. The reasons for this was that some assets earlier were overestimated, such as: Primary School “Ardhmëria” in Rahovec was wrongly registered in the amount of €50,920,000 and should have been registered in €509,200; Primary school “Pataqani i Ulët”, €263,900 was registered twice; Primary school in Kramovik was registered twice €182,400; and Primary School “Hamëz Thaqi” in Xërxe was registered twice in the amount of €385,106. These updates were made by Treasury upon the request of Municipality.

At the interim audit stage, we suggested that all municipal assets are recorded in compliance with the regulation on asset management and we found the concrete actions undertaken. There still remains work to be done for the full addressing of recommendations. We identified the following weaknesses:

Issue 13- A failure to record assets and improper assets stocktaking - High Priority

Finding

Th Municipality is still missing a final accurate register of assets. It was unable to establish at the end of the year a stocktaking commission, as required in the Administrative Instruction 02/2013.

Municipality has still not managed to use and record assets under €1,000 in the E-asset programme. In addition, the purchase of eight vehicles Dacio Sandero is recorded as a group with the value of €50,000 and not separately for each vehicle.

Out of 39 vehicles owned by municipality, 28 are not registered in the accounting register.

Risk

A failure to record accurately the municipal assets increases the risk of underestimation of municipality assets and unfair presentation of the assets value. In addition, failure to record assets in the E-asset programme increases the risk of losses, misuse and unauthorised use.

Recommendation 13 The Mayor should ensure that at the end of 2015 stocktaking commission and assessment of assets is established. Final reports for the management and recording results shall be processed in the assets records by the respective officer. The activities of commissions should be systematically supported and monitored by the Mayor.

4.4.2 Handling of Receivables

Description

Accounts receivable of the Municipality at the end of 2014 were €2,345,000. Compared to the previous year (€2,206,507), an increase by €138,493. These receivables result are from: property tax, business tax, giving municipal property for rent, etc.

Issue 14 - Handling of receivables - High Priority

Finding We identified that the municipality has incorrectly presented accounts receivables for rent revenues in public premises. In the AFS of 2014; receivables from premises were €146,000, while according to municipal registers they are €139,641.

Risk Insufficient controls over accounts receivables presents a risk to delete taxpayers obligations from the register and this would impact on the decrease of own source revenues. A failure to collect accounts receivable may impact on the inability to meet the expenditures plan. The inefficient municipality policies to handle accounts receivable have resulted in their increase from one year into the other and this increases the risk to fail in the execution of municipal projects.

Recommendation 14 The Mayor should initiate an assessment process, where all accounts receivable are analysed in terms of aging, real collection potentials and establish a strategic plan for bringing the receivables down.

4.4.3 Handling of Debts

Description

The Municipality in 2014 AFS reported financial obligations in the amount of €731,551. Compared to 2013 (€2,202,988), obligations were decreased by €1,471,437, a positive approach in handling of debts prevails.

Issue 15 – Recording invoices not paid - Medium Priority

Finding Municipality of Rahovec in 2014 kept evidence relating to invoices received and reported obligations in Treasury on monthly basis. However, we tested the evidence keeping and we identified some invoices which were not recorded in the protocol book. The value of invoices which were not recorded in the protocol book was €96,440 (Invoice with no. 23/2014 in the amount €26,440; invoice with no. 08/2012 in the amount of €40,000; invoice with no. 62 in the amount €30,000).

Risk A failure to accurately record the municipal obligations impacts that monthly reporting is incomplete and increases the risk that municipality pays invoices paid earlier.

Recommendation 15 The Mayor should ensure that the finance services implements all legal requirements regarding registration and payment of invoices not paid.

4.5 Internal Audit System

Description

The Internal Audit Unit (IAU) is comprised of two auditors. IAU for 2014 planned to carry out seven (7) audit reports, a plan which was executed. The focus of the internal audit reports were activities of 2013.

On 12.02.2015, the Municipality formed the internal audit committee.

Issue 16 - Internal Audit - High Priority

Finding

Our audit identified following issues:

The annual internal audit plan was not based on analysis of risk:

Only a limited number of recommendation given by IA were addressed;

The Internal Audit Committee was not functional during 2014 and has not held any meeting;

The focus of internal audit reports published during 2014 was mainly on 2013 activities.

The recommendation given by the internal audit have not assisted management to understand the level of actions needed for improving the operational and financial activities.

Risk

Lack of focus in pursuing the current year's activities increases the risk that internal controls may not function effectively and management may not be informed on weaknesses and on existing control challenges. This may result in continued weaknesses and increases the risk of financial losses for municipality.

Recommendation 16 The Mayor should ensure that Internal Audit System is getting functionalized. A clear cooperation between actors in the system is needed. The areas for audit should be based on risks and relevant and focused toward the current year. The Mayor should manage internal audit recommendations better.

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
1. Third parties	The Mayor should analyse the reasons for failing to fairly present third party payments in the initial AFS, and identify appropriate actions to address these control weaknesses in order to enable their fair and true presentation in 2014.			Not addressed
2. Assets	The Mayor should analyse the reasons for incomplete and unfair presentation of assets in the AFS for 2013 and identify the action required to address these controls weaknesses to enable a true and fair presentation of Assets in the 2014 AFS.		Partly	
3. AFS preparation process	The Mayor should identify appropriate actions to address these control weaknesses in order to enable a fair and true presentation of data in 2014.		Partly	
4. Addressing recommendations	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.		Partly	
5. Good governance	The Mayor should carry out a review to determine the format of reporting to senior management to support effective business management and introduce appropriate solutions.	Addressed		
6. Budget execution	The Mayor should ensure that the process of budget preparation is followed by a re-assessment of the process, and planning is done based on reasonable and realistic parameters.		Partly	

7. Revenues - planning	The Mayor should ensure that budgeting of revenues is done based on proper planning and realistic parameters. In addition, obstacles regarding revenue collection should be identified and a concrete plan is established which would increase revenue collection. The management should take immediate action regarding the contracts on rented properties and collection of remaining debts, otherwise the contracts should be terminated and use of public property stopped.			Not addressed
8. Construction licences	The Mayor should ensure that all construction license beneficiaries are charged with exact amounts and in accordance with the Law on Construction.	Addressed		
9. Properties given on rent - revenues	The Mayor should ensure that the expired contracts are renewed and invoicing of entities is done on monthly basis. Furthermore, the Municipality should clarify all commercial agreements and terminate contracts which are not favourable for the Municipality.			Not addressed
10. Revenues reporting	The Mayor should ensure that processing of administrative fees is made through the electronic system and monthly reconciliations are made between the relevant departments and revenues officer. This process should be monitored on regular basis.	Addressed		
11. Expenditures - procurement	The Mayor should implement an internal review to determine why procurement requirements are not implemented in all procurement cases, and apply more controls to ensure that systemic weaknesses identified are addressed.	Addressed		
12. Expenditures	The Mayor should review why procurement requirements were not consistently applied in the abovementioned cases and enhance controls ensuring that such situation is not repeated.			Not addressed

13. Subsidies given without supporting documentation	The Mayor should ensure that all subsidies are given based on planning and according to decisions of the competent authorities, as foreseen by the internal regulations. The process should become transparent and subsidies given only based on adequate criteria, followed with a detailed conceptual plan with the intent to diminish the possibility of funds being spent for purposes other than those intended.		Partly	
14. Assets	The Mayor should ensure that the Inventory and Evaluation Committees complete their work and report timely. Assets management officer should record and maintain assets register under the Regulation 02/2013 on Management of Non-Financial Assets.			Not addressed
15. Liabilities	The Mayor should ensure that liabilities of the Municipality are reported on regular monthly basis and in accordance with requirements of Financial Rule on Outstanding Liabilities.	Addressed		
16. Internal audit	The Mayor should ensure that IAU in the future is oriented towards development and implementation of the risk-based audit strategy focused on the current year. This would give assurance to the management on effectiveness of internal control systems. The Audit Committee work should be made operational.		Partly	

Annex III: Management Response to OAG Findings

Findings	Agree	Comments from the institution	OAG view
Finding 2:	No	We have made adjustmetns to AFS and have submitted to the Treasury within the legal deadline 03/19/2015. The treasury has moved those figures while we were not notified for this intervention.	This is just an excuse by the municipality because every budget organization is required to manage its own budget and follow the changes that occur. Our finding and recommendation remains unchanged.
Finding 7:	No	We disagree since the planning has been imposed due to disapproval of the budget by the Municipal Assembly in September 2013, even because of disapproval by the government in April 2014 for political reasons even though the Municipal Assembly has approved the delay.	The issue of the budget approval is handled in the governance chapter, therefore, a special emphasis has been added to own source revenues property tax respectively. Our finding and recommendation remains unchanged