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**ZYRA KOMBËTARE E AUDITIMIT
NACIONALNA KANCELARIJA REVIZIJE**

NATIONAL AUDIT OFFICE

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AUDIT REPORT
ON THE ANNUAL FINANCIAL REPORT OF PRIZREN
MUNICIPALITY FOR
THE YEAR ENDED 31 DECEMBER 2016

Prishtina, June 2017

The National Audit Office of the Republic of Kosovo is the highest institution of economic and financial control, which according to the Constitution and domestic laws, enjoys functional, financial and operational independence. The National Audit Office undertakes regularity and performance audits and is accountable to the Assembly of Kosovo.

Our Mission is to contribute to sound financial management in the public administration. We perform audits in line with internationally recognized public sector auditing standards and good European practices.

The reports of the National Audit Office directly promote accountability of public institutions as they provide a base for holding managers' of individual budget organisations to account. We are thus building confidence in the spending of public funds and playing an active role in securing taxpayers' and other stakeholders' interests in enhancing public accountability.

The Auditor General has decided on the audit opinion on the Annual Financial Statements of the Municipality of Prizren in consultation with the Assistant Auditor General, Qerkin Morina, who supervised the audit.

The opinion and report issued are a result of the audit carried out by Lavdim Maxhuni (Team Leader) Ernes Beka and Fetah Osmani under the management of the Audit Director Florim Beqiri.

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Executive Summary

Introduction

This report summarises the key issues arising from our audit of the 2016 Annual Financial Report of the Municipality, which determines the Opinion given by the Auditor General. The examination of the 2016 financial statements was undertaken in accordance with the International Standards on Supreme Audit Institutions. Our approach included such tests and procedures, as we deemed necessary to arrive at an opinion on the financial statements. The applied audit approach is set out in our External Audit Plan¹ dated 15.11.2016.

Our audit focus (detailed in Annex 1) has been on:



For more details, see Annex 1.

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

Opinion of the Auditor General

Unmodified Opinion with Emphasis of Matter

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

Emphasis of Matter

As emphasis of matter, we would like to draw your attention to the fact that €2,227,559 were misclassified from the category of Capital Investments for Goods and Services and Subsidies and Transfers. In addition, the register of assets under €1,000 was incomplete.

For more, please refer to Section 1.1 of this report.

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

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

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

Key Conclusions and Recommendations

Based on the details presented in each section of this report our overall conclusion is that:

Based on the issues raised in the report our general conclusion is that the internal control system established by the Municipality does operate but not at the appropriate level, as there are weaknesses in some key governance areas.

Our main conclusions and recommendations are:



Management's response to 2016 audit

The Mayor considered and agreed with all audit findings and committed himself to address recommendations given.

We take it for granted the fact that the Mayor:

- Table the Audit Report for discussion in the Local Assembly; and
- During January/February 2018 initiate a discussion in the Local Assembly regarding the implementation of the Action Plan on audit recommendations, before AFS 2017 are submitted to Ministry of Finance.

1 Annual Financial Statements and other External Reporting Obligations

Introduction

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

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

1.1 Audit Opinion

Unmodified Opinion with Emphasis of Matter

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

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

Basis for the opinion

We conducted the audit in accordance with International Standards of Supreme Audit Institutions (ISSAIs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the AFS section of our report. We believe that the obtained audit evidence is sufficient and appropriate to provide a basis for the opinion.

Emphasis of Matter

We draw your attention to the fact that expenditures were classified in incorrect codes. From the payments tested we noticed that the Municipality had paid €2,227,559 out of the category of Capital Investments, which were goods and services and subsidies and transfers. The most important ones are: waste collection and management (€1,079,132), summer and winter maintenance of roads (€474,955), subsidy for the football club Liria (€100,000), teacher

transportation (€48,770), supply with wheat grain, corn, plastic foil (€102,122), etc. This amount was approved with budget tables of 2016 as capital investments, but projects presented in tables do not meet the conditions to be treated as capital projects. Errors relate to initial planning by the Municipality and inadequate approvals by the MoF.

In addition, the register of financial assets under €1,000 is not complete as therein are not included assets of schools, Main Family Medicine Centre, and the Directorate for Social Welfare.

Responsibility of Management and Those Charged with Governance and AFS

The Mayor is responsible for the preparation and fair presentation of financial statements in accordance with International Public Sector Accounting Standards – Financial Reporting under the Modified Cash based Accounting and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error. This includes the application of Law number 03/L-048 on Public Finance Management and Accountability (as amended and supplemented).

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

Auditor General's Responsibility for the Audit of the AFS

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

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

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

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

1.2 Compliance with AFS and other reporting requirements

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

- Compliance with MoF Regulation no. 01/2017 on the Annual Financial Reporting of Budget Organisations;
- Requirements of LPFMA no. 03/L-048, as amended and supplemented with Law no.03/L-221, Law no. 04/L-116 and Law no. 04/L-194;
- Compliance with Financial Rule no.01/2013;
- Compliance with Financial Rule no.02/2013;
- Action Plan on implementation of recommendations;
- Requirements of Financial Management and Control (FMC) procedures;
- Nine month financial statements; and
- Draft and final procurement plan on time.

When it comes to abovementioned requirements, the Municipality had handled them in accordance with reporting framework.

In the context of quality, a number of financial adjustments were required to the draft AFS as they contained some errors and shortcomings that related to information. They have been corrected, with the exception of issues on assets and misclassification for which issues we have emphasised the opinion. For more, see subchapter 1.1 Audit Opinion.

DECLARATION BY MANAGEMENT

Given the above - the Declaration made by the Chief Administrative Officer and Chief Financial Officer when the draft AFS are submitted to the Ministry of Finance can be considered to be correct given that were not identified material errors except for issues identified in the audit opinion.

1.3 Recommendations for the first part of the report

Recommendation 1 The Mayor should ensure that an analysis is undertaken to determine the causes of the emphasis of matter and establish effective processes to confirm that the draft AFS plan for 2017 addresses all weaknesses related to AFS.

2 Governance

Introduction

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

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

The remainder of our review of governance arrangements reflects a consideration of:

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

Overall Governance Conclusion

There is a number of governance weaknesses within Municipality particularly related to accountability, risk management and the quality of management reporting. The self-assessment checklist completed by Municipality only partially recognises this situation with some positive comments about existing arrangements not evidence based. Other arrangements that would support governance development such as an effective response to audit recommendations.

A key tool that supports effective governance is implementation of audit recommendations. The Municipality has not managed to implement previous year's recommendations to a sufficient degree, as only six out of 20 were fully implemented.

The Municipality had not drafted a strategic plan and had not drafted the list of risks that the Municipality faces.

Budget planning seems to be weak as only 66% of own source revenues planned were collected, and only 88% of the budget for capital investments was spent. Due to improper management of liabilities, the Treasury under Article 39.2 had executed the payment of €443,416 out of the category of capital investments, and out of goods and services €213,940.

In terms of compliance with legislation, as a result of not implementing relevant regulations, our audit has revealed existence of some weaknesses that include procurement, revenues, assets and receivables.

2.1 Progress in the Implementation of Prior Year Recommendations

Our audit report on 2015 AFS resulted in 20 recommendations, 18 of which were of high priority and two of medium priority. The Management had prepared an Action Plan showing how all recommendations will be implemented. Last year's audit report was not discussed at the municipal assembly.

By the end of our audit for 2016, six recommendations were implemented (four of high priority and two of medium priority), five high priority recommendations are in the process of implementation and nine high priority recommendations have not been implemented. For a more thorough description of recommendations and how they are addressed, see Annex III.

Issue 1 - Addressing Prior Year Audit Recommendations - High Priority

Finding Nine out of 18 high priority recommendations were not addressed at all, as the Municipality has not followed any formal processes to manage and monitor the manner in which Auditor General's recommendations are implemented. As such, in this audit report issues were raised again in order to improve certain activities.

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

- Inadequate governance which reduces management's ability to take timely actions against financial challenges that can potentially result in financial losses;
- Inadequate budget planning;
- Inadequate management of revenues from renting of municipal property; and
- Continuous organisational inefficiency and poor value for money in procurement practices.

Recommendation 2 The Mayor should consider the reasons why audit recommendations are not being implemented and apply responsibility measures towards all persons that are charged with the action plan for implementation of recommendations. After the finalisation of this report, the Mayor should prepare the Action Plan with clear deadlines and activities, and determine persons responsible for implementation of this entire plan.

2.2 Self-Assessment Checklist of FMC components

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

Issue 2 - Self Assessment Checklist - High Priority

Finding As part of our audit we have considered key questions related to the five components of the self-assessment checklist. For the questions considered we found that:

1. The completed self-assessment questionnaire has proved that the Municipality has not yet established formal and documented identification procedures and risk management at the level of organisation that would mitigate exposure to risks associated with achievement of objectives;
2. The Municipality does not have a Strategic Development Plan. Furthermore, refer to subsection 2.3.1;
3. The links between the procurement plan and the budget are not always done because the contracts are concluded without sufficient commitment of funds; And
4. Progress on monitoring the objectives is not done regularly and as a result the causes for possible failures are not analysed.

Risk Poor governance arrangements weaken strategic and operational processes and reduce the quality of services provided to citizens through inefficient and ineffective activities.

Recommendation 3 The Mayor should ensure that the list of risks and the strategic development plan will be drafted. Monitoring of strategy should be done on a continuous basis to ensure that strategic objectives are being achieved. The internal audit unit should be engaged to confirm the accuracy of the checklist.

2.3 Specific Governance Reviews

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

2.3.1 Setting of Strategic Objectives

Municipalities are obliged to prepare and submit organisation level strategic plans such as: Urban Plans, Spatial Plans, Emergency Operations Plans, Anti-Corruption Strategic Plans, Regional Development Strategy etc. The Municipality has drafted the municipal strategy for agriculture, strategic document for development of tourism, drafting of emergency response plans, and the spatial urban plan.

Issue 3 – Lack of Strategic Development Plan - High Priority

Finding The Municipality does not have a comprehensive strategic plan with long-term objectives wherein would be described clearly the Vision and Mission which presents orientation and goals of the Municipality in a medium-term development period. In addition, Municipality has not drafted the anti-corruption strategy.

Risk Due to lack of a comprehensive strategic plan are risked priorities of key issues that relate to orientation and development of the Municipality in the long-term. The uncertainty over implementation of the strategy made it impossible to follow-up fulfilment of objectives (from the perspective of Municipality's vision) as one of the essential conditions of good governance.

Recommendation 4 The Mayor should approve an overall strategic plan for the Municipality including the cost of the strategy, establish long-term objectives, and serves as an orientation platform for drafting annual plans. To draft an action plan on monitoring achievement of objectives, by establishing effective oversight functions.

2.3.2 Management Reporting and Accountability

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

Issue 4 - Weaknesses in Management Controls - High Priority

Finding The Municipality has in written form only the minutes that result from meetings of the Board of Directors and the Municipal Assembly, while it does not have weekly and monthly reports in writing prepared by the directors of Directorates for the Mayor, wherein should be described operational and financial activities.

According to the 2016 Budget Law, within three (3) weeks from the end of each three (3) months, the Chief Financial Officer of every Municipality shall submit to the Mayor a detailed report on the progress achieved in the implementation of all capital projects with a value greater than ten thousand (10,000) Euros. A copy of such a report should also be submitted to the Minister of Finance as well, but these reports were not prepared and submitted according to legal requirements.

Risk Irregular reporting to the Mayor reduces management's ability to manage Municipality's activities effectively, to respond to financial challenges in a timely manner and to implement effective budget control.

Recommendation 5 The Mayor should ensure that is carried out a review in order to determine the format of financial reporting to senior management, which is required to support effective business management - and to ensure that an appropriate solution is in place for this. In addition, to take measures so that reporting by the CFO is done in line with legal requirements on physical progress of capital investments.

2.4 Internal Audit System

The Internal Audit Unit (IAU) operates with two members of staff - the Director of IAU and one auditor. An effective audit requires a comprehensive work programme that reflects financial and other risks to the Municipality and provides sufficient assurance over the effectiveness of internal control. The impact of IA output should be judged by the importance that management places on addressing recommendations and the support and challenge provided by an effective Audit Committee. The IAU had planned to carry out 10 audits according to the annual plan (four with high risk, five with medium risk and one with low risk), and managed to finish nine of them. These audits related to the activities of 2015 and 2016. IAU had done a good job by auditing high-risk areas such as Revenues, Capital Investments, Goods and Services, Assets Management. We appreciate the work done by this Unit and can conclude that reports were of good quality and adequately proven, and had covered activities that are in the process thereby identifying some of the shortcomings in the municipal internal control systems.

Issue 5 - Poor addressing of IAU recommendations - High Priority

Finding We have assessed how the management of the Municipality is implementing IAU recommendations and concluded that they have been implemented only partially. This is also confirmed by the Annual Report of this Unit that was submitted to the Central Harmonisation Unit within the Ministry of Finance.

The Committee needs to conduct more intensive and better quality of work to incite implementation of internal and external audit recommendations.

Risk Poor addressing of IAU recommendations by the management poses a risk, as internal controls may not function at the right level. Lack of engagement by the Audit Committee to incite addressing of IAU recommendations poses a risk as shortcomings may be repeated.

Recommendation 6 The Mayor should take all actions against administrative units to which recommendations are addressed so that they demonstrate maximum commitment in taking corrective measures in areas where weaknesses have been identified.

3 Financial Management and Control

Introduction

Our work on Financial Management and Control outside of the areas of Governance referred to in Chapter 2, reflects the detailed work undertaken on Revenue and Expenditure Systems. As part of this, we consider Budget management, Procurement and Human Resources issues, and Assets and Liabilities.

Financial Management and Control Conclusion

The Municipality has established an internal control system which generally operates well, but the effectiveness of controls needs to improve in certain areas where shortcomings have been identified. Areas where more improvements are needed are procurement, revenues from renting of municipal property, property tax, budget planning and execution, assets management, reporting of outstanding liabilities.

3.1 Budget Planning and Execution

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

Table 1. Own Source Revenues

Description	Initial Budget	Final Budget	2016 Receipts	2015 Receipts	2014 Receipts
Own Source Revenues	9,480,000	9,480,000	6,292,849	5,276,000	5,353,482

Out of planned own source revenues the Municipality had managed to collect only 66%. Part of the total of own source revenues are also revenues from traffic fines (€312,603) court fines (€179,485), from forests (€16,043). The reason why the collection was low is that planning of revenues was poor and was not done on a real and sustainable basis.

Table 2. Sources of budgetary Funds (in €)

Description	Initial Budget	Final Budget ²	2016 Outturn	2015 Outturn	2014 Outturn
Sources of Funds	40,616,924	42,248,085	36,983,514	36,316,641	33,265,428
Government Grant -Budget	31,136,924	31,037,090	30,767,839	30,671,904	28,783,661
Carried forward from previous year ³ -	0	1,370,905	1,345,624	1,537,404	753,697
Own Source Revenues ⁴	9,480,000	9,480,000	4,679,230	4,062,518	3,634,429
Domestic Donations	0	210,421	84,038	28,956	37,796
External Donations	0	149,669	106,783	15,859	55,845

The final budget is higher than the initial budget by €1,631,161. This increase relates to Revenues carried forward from the previous year (€1,370,905), Domestic and External Donations (€360,090) and decrease of the Government Grant (€99,834) in the final budget.

Municipality used 88% of the final budget. A similar spending degree was also last year. However, the budget execution remains at an unsatisfactory level, and below are given explanations on current position.

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

Description	Initial Budget	Final Budget	2016 Outturn	2015 Outturn	2014 Outturn
Spending of funds by economic categories	40,616,924	42,248,085	36,983,514	36,316,641	33,265,428
Wages and Salaries	18,423,522	19,030,280	18,919,546	18,258,306	17,766,430
Goods and Services	3,125,019	3,083,195	2,807,989	2,448,555	2,477,087
Utilities	1,081,200	1,065,171	762,688	751,705	864,971
Subsidies and Transfers	477,615	512,179	325,767	334,608	521,614
Capital Investments	17,509,568	18,557,260	14,167,524	14,523,467	11,635,326

Explanations for changes in budget categories are given below:

- From the table we see that we have low spending across categories compared to the budget. For Goods and Services and Utilities was 86%, Subsidies and Transfers 64%, and Capital Investments 76%. The reason why spending is low across categories is due to poor planning and collection of own source revenues. Over three million euros of own source revenues planned to be collected could not be spent due to the failure to collect them.

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 Receipts used by the entity for financing its own budget.

Issue 6 – Budget Execution – High Priority

- Finding** Budget execution was not at the expected level at the won source revenues and expenses. Needs to be mentioned that budget execution by 88% was affected also by the execution of payments by the Treasury (€657,356) under Article 39.2 of LPFMA.
- Risk** Inadequate budget planning and a low budget execution level will result in a failure to meet organisational objectives and result in current year obligations being funded from future year budgets.
- Recommendation 7** The Mayor should ensure that budget performance is systematically monitored on a monthly basis and that this review identifies and addresses barriers to planned levels of budget execution. Where initial budget assumptions are found to be incorrect this should be fully reflected in the final budget position.

3.1.1 Revenues

Revenues generated by Municipality in 2016 totalled €6,292,849, which are mainly from property tax, use of municipal property, vehicle registration tax, construction permits, administrative tax revenues, etc.

Issue 7 - Property Tax - High Priority

- Finding** The Municipality had not managed to verify 1/3 of immovable property as required under the Law No.03/L-204 on Taxes on Immovable Property and the applicable Administrative Instruction. Out of 48,645 properties, the municipality during 2016 has managed to verify only 1477. This was due to lack of field surveying officials to verify properties.
- According to Article 9 of the Law on Taxes on Immovable Property, “Every natural person who, on or before 1 March of a tax period, establishes that the property or residential unit serves as his or her principal residence shall be allowed a deduction of ten thousand (10,000) Euro from the taxable value of the property. We have identified seven cases where the Municipality had not acted in accordance with the Law as there were taxpayers who owned two or more properties registered as main residence and for each property was applied a deduction of €10,000 from the taxable value of the property.

Risk Failure to verify 1/3 of the properties can result in incomplete information on the current taxable property, with a potential impact that estimated property tax revenues will decrease.

Failure to apply charges in accordance with legal requirements on property tax poses a risk of revenues being lower in this category.

Recommendation 8 The Mayor should ensure that verification of municipal property should be done as foreseen under the Law, so that the database integrates all potential changes to the property that are valid for the taxable base. In addition, more actions should be taken to ensure that deductions by €10,000 are applied in accordance with Article 9 of the Law on Taxes on Immovable Property.

Issue 8 - Revenues from renting municipal property - High priority

Finding The Municipality for 2016 had planned to collect from rent €1,350,000, while it managed to collect €501,328 or 37%.

In 2016 was entered into contracts for use of municipal property with a price of €1 per month for eight business locations to some of the political parties, while no auctions have been organised as required under the on Allocation for use and Exchange of Immovable Property of the Municipality. These business locations were given based on the municipal assembly decision that was issued in 2005.

In addition, for eight other business locations and one building owned by the Municipality were not organised public auctions, while some Non-Governmental Organisations and political parties are using them without any contracts.

In two cases renters use the municipal property for markets without a valid contract, as their contracts had expired in 2013, while they continue to be charged with rent only based on a document from the Public Services Directorate dated 10.11.2014. These renters owe the Municipality €285,834.

The Municipality in one case has a contract with an Economic Operator as of 2009, for the use of green market space with a monthly rent of €180. We noticed that the EO did not meet obligations under the contract and had never paid the obligation to the Municipality, which amounted to €14,580. Furthermore, the Municipality had not organised public auctions for the mentioned cases even though the Law on Allocation for use and Exchange of Immovable Property of the Municipality had entered into force in 2012.

In addition, in two cases, the Municipality had signed contracts to rent business locations, but renters had not meet obligations under the contract and their debt amounts to €3,534.

Risk

Renting municipal property without organising public auctions poses a risk of making the wrong choice, by limiting the market offer, and undermining the principle of free competition and equal treatment of all parties interested. In addition, use of public spaces without valid contracts between the Municipality and users of municipal property risks the actual collection of liabilities, as a result of which the Municipality can suffer considerable financial losses.

Recommendation 9 The Mayor should ensure that are organised public auctions when renting municipal property in order to have an open and transparent process, and to exercise continuous monitoring over the use of public spaces so that municipal properties are not being used without meeting in advance the obligations stipulated under entered into contracts. In addition, should be established mechanisms so that properties are not being used without a valid contract signed with the Municipality.

3.1.2 Wages and Salaries

The planned budget for the category of Wages and Salaries was €19,030,280, while were spent €18,919,546 or 99%.

We have tested the compliance of payroll lists, recruitments, dismissals, maternity leaves, pensions and payments to municipal members. We also reviewed whether the employees have been paid under contracts. From our tested samples we have not noticed any issues that need reporting.

Recommendations

We have no recommendations in this area or.

3.1.3 Goods and Services and Utilities

The final budget for Goods and Services and Utilities was €4,148,366, while were spent €3,570,677. These expenses relate to fuel, office and medical supplies, contracted costs, maintenance of schools and buildings, and vehicle repairs.

Issue 9 – Contract signed without procurement procedures - High priority

Finding The Municipality had signed a contract for broadcasting municipal assembly sessions at €150 per session, without adhering to procurement procedures. The signing of the contract was done directly with the EO without conducting any procurement procedures. After our counselling in interim stage, the Municipality had immediately terminated the contract.

We noticed that in 22 cases the Education Directorate had not protocolled received receipts as required under the Article 24 of Financial Rule 01/2013 on Public Funds Expenditure.

In three cases, the Municipality had entered into obligations without committing all necessary funds. The value of these signed contracts was €89,029, while the commitment was done only for €11,000.

Risk Entering into obligations without securing sufficient funds can cause financial and budgetary problems for the Municipality. In addition, failure to record invoices poses a risk as it indicates that internal controls may not be functioning properly and invoices will not be paid on time.

Recommendation 10 The Mayor should consider the reasons why procurement requirements were not consistently applied in the abovementioned cases and to exercise more controls to ensure that such situations will not be repeated and that all invoices the moment they are received are firstly recorded then processed further for payment.

3.1.4 Subsidies and Transfers

The final budget of Subsidies and Transfers was €512,179, out of which €325,767 were spent in 2016. Those relate to subsidies to public entities; sports clubs, different NGOs cultural-artistic associations.

Recommendations

We have no recommendations in this area

3.1.5 Capital Investments

The final budget of Capital Investments was €18,557,260, out of which €14,167,524 was spent in 2016. Those relate to construction of roads, sewers, school buildings, city library etc.

Issue 10 – Contract with price per unit and lack of executive projects – High Priority

Finding

The Municipality had entered into three public framework contracts with price per unit for maintenance work for a duration of 36 months (Installation of public lighting, maintenance of local roads with cobblestone cubes, intervention in infrastructure in case of natural disasters) in disagreement with the Law on Public Procurement (LPP) without specifying in the Tender Dossier the quantity or the estimated value of the contract. Pursuant to Article 38 of the LPP, “The Contracting Authority specifies the indicative quantity, the Contracting Authority shall specify in the tender dossier the value or quantity of the contract as a threshold or a ceiling and allow derivation therefrom, stating also the percentage of permitted discrepancy. The permitted discrepancy cannot be higher than plus/minus thirty per cent (30%)”. Failure to determine the amount or the estimated value in the contract will make it impossible to determine the deviation threshold permitted under the law.

We have noticed that in the contract “Roof Renovation in the MFMC” in the amount of €42,220 the Municipality had not drafted the executive project. Article 28.10 of the LPP on technical specifications for works contracts among others states that “No contracting authority is permitted to issue tender documents without attaching a detailed project description.”

Risk

Failure to include approximate indicative amounts in the tender dossier or the estimated contract value, poses a potential risk of manipulation with necessary quantities and deliver works with favourable positions for the Economic Operator (with more expensive prices) and the failure to execute positions with cheaper prices. This can cause considerable losses to the municipal budget. In addition, due to development of procurement procedures without a beforehand drafted project, works carried out in these projects can deviate from the required construction standard and not achieve the right quality.

Recommendation 11 The Mayor should ensure that the Procurement Office prepares the tender dossiers in line with the LPP requirements and specify clearly approximate indicative quantities of works or the estimated contract value. In addition, not to initiate procurement activities without initially drafting the executive projects.

3.2 Assets

3.2.1 Capital and Non Capital Assets

The Municipality had presented in the AFS assets over €1,000 in the amount of €474,589,000 and under €1,000 in the amount of €921,000. Our audit has identified the following issues:

Issue 11 - Assets inventory and assessment of assets in disagreement with the Regulation - High priority

Finding The Assets Inventory Committee had not include in its report all non-financial assets of the Municipality, as foreseen under the Regulation 02/2013 on Management of Financial Assets. In this report was not included the inventory of schools assets, of family medicine centres, and social work centres.

Despite the fact that the inventory committee had identified damaged and old assets, we have noticed that the assets inventory committee had not assessed these assets and had not prepared the assessment report by date of our audit completion 17.03.2017. Article 24.1 of Regulation 02/2013 on Management Financial Assets states "After reconciliation of condition with inventory and assessment with the condition of non-financial assets registers, the condition of non- financial assets should be part of annual financial statements in accordance with the Financial Regulation on Annual Financial Statements".

Risk Failure to inventory all municipal assets poses a risk of them being lost, alienated, or misappropriated. In addition, failure to produce the assessment report on time according to the requirements of the Regulation can result in inaccurate presentation of Municipality's assets in the AFS.

Recommendation 12 The Mayor should ensure that the committee for inventory and assessment of non-financial assets shall carry out the work in accordance with the Regulation, by including and assessing Municipality's entire assets.

Issue 12 - Inoperable e-assets System - High Priority

Finding The e-assets system is not fully operational yet. In the e-assets is recorded only expendable material of Municipality's administration by the Warehouse Officer in the absence of the Receiving/Logistics Officer, which the Municipality had not yet recruited, although it was a recommendation in the previous year's report.

Risk Failure to recruit the Receiving/Logistics Officer for recording of assets leads to incomplete functioning of the e-assets system and the possibility of loss or appropriation of unrecorded assets.

Recommendation 13 The Mayor should recruit the Receiving/Logistics Officer at the shortest possible time so that the e-assets system is fully functional and assets records are updated.

Issue 13 - Lack of internal procedures on assets management - Medium Priority

Finding Article 4.1 of Regulation 02/2013 on Financial Property Management states that "The Chief Administrative Officer is responsible for adoption of internal rules and procedures on recording, preservation and alienation of non-financial assets." The Municipality does not have internal procedures on assets management.

Risk Due to lack of internal procedures on preservation and alienation of Municipality's, assets may not be managed and presented appropriately.

Recommendation 14 The Mayor should draft internal rules and procedures on recording, preservation and alienation of non-financial assets as required under the Regulation 02/2013.

3.2.2 Receivables

The Municipality has not managed to collect all debts for which services were provided. The structure of Accounts Receivable consists mainly of property tax, market revenues, renting of business locations, business fees, and waste collection services. Due to lack of adequate policies and specific measures for collection of revenues has resulted high level of Accounts Receivable.

Issue 14 - Continuous increase of Accounts Receivable and lack of measures to collect them - High Priority

Finding Total of Municipality's uncollected debts for 2016 were €15,567,347. The main debt remains from the property tax in the amount of €6,808,003, business fees €5,753,532, waste collection and management €1,859,235, renting of market spaces €455,577, and other fees €691,000. Compared to the previous year (€14,013,000), Accounts Receivable had increased by €1,554,347, due to lack of proper collection mechanisms by the Municipality.

Risk Due to lack of concrete measures to collect Account Receivable they have increased from year to year, and the Municipality suffered financial losses. In addition, this reduces Municipality's flexibility towards planned expenses that were planned to be financed from own source revenues.

Recommendation 15 The Mayor should consider establishing a special work group that reviews debt collection. To conduct an analysis so that are determined the causes behind the failure to collect debts, and to use all means available, without excluding administrative measures and legal actions.

3.3 Outstanding Liabilities

The statement of liabilities not paid to suppliers at the end of 2016 was €1,383,866. These liabilities are carried forward to be paid in 2017. This amount of liabilities is as a result of insufficient internal controls and entering into liabilities without sufficient funds.

Issue 15 – Failure to report liabilities in accordance with legal requirements - Medium Priority

Finding We have identified four invoices of 2016 (one invoice of month of May, two invoices of November and one invoice of December) with a total value of €51,594 that were not presented in the report of outstanding liabilities and in the AFS of 2016.

Risk Failure to present outstanding liabilities in accordance with legal requirements poses a risk of inaccurate and unfair presentation of liabilities in the AFS. This also affects management’s decision-making to plan and budget liabilities that were carried forward.

Recommendation 16 The Mayor should ensure that all invoices are fairly reported to the Ministry of Finance in accordance with the Financial Rule 04/2011- on Reporting Outstanding Liabilities, so that this reflects fair presentation of liabilities in the AFS.

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

ANNEX I: Audit Approach and Methodology

The responsibilities placed on the Auditor and Those Charged with Governance are detailed in the Opinion set out in Section 1.1 of this report.

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

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

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

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

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

Findings considered low priority were reported separately to finance staff.

Our procedures included a review of the internal controls and accounting systems and associated substantive testing and associated governance arrangements only to the extent considered necessary for the effective performance of the audit. Audit findings should not be regarded as representing a comprehensive statement of all the weaknesses which exist, or all improvements which could be made to the systems and procedures operated.

Annex II: Explanation of the different types of opinion applied by NAO

(extract from ISSAI 200)

Form of opinion

147. The auditor should express **an unmodified opinion** if it is concluded that the financial statements are prepared, in all material respects, in accordance with the applicable financial framework.

If the auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement, or is unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement, the auditor should modify the opinion in the auditor's report in accordance with the section on "Determining the type of modification to the auditor's opinion".

148. If financial statements prepared in accordance with the requirements of a fair presentation framework do not achieve fair presentation, the auditor should discuss the matter with the management and, depending on the requirements of the applicable financial reporting framework and how the matter is resolved, determine whether it is necessary to modify the audit opinion.

Modifications to the opinion in the auditor's report

151. The auditor should modify the opinion in the auditor's report if it is concluded that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement, or if the auditor was unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement. Auditors may issue three types of modified opinions: a qualified opinion, an adverse opinion and a disclaimer of opinion.

Determining the type of modification to the auditor's opinion

152. The decision regarding which type of modified opinion is appropriate depends upon:

- The nature of the matter giving rise to the modification – that is, whether the financial statements are materially misstated or, in the event that it was impossible to obtain sufficient appropriate audit evidence, may be materially misstated; and
- The auditor's judgment about the pervasiveness of the effects or possible effects of the matter on the financial statements.

153. The auditor should express a **qualified opinion if**: (1) having obtained sufficient appropriate audit evidence, the auditor concludes that misstatements, individually or in the aggregate, are material, but not pervasive, to the financial statements; or (2) the auditor was unable to obtain sufficient appropriate audit evidence on which to base an opinion, but concludes that the effects on the financial statements of any undetected misstatements could be material but not pervasive.

154. The auditor should express an **adverse opinion if**, having obtained sufficient appropriate audit evidence, the auditor concludes that misstatements, individually or in the aggregate, are both material and pervasive to the financial statements.

155. The auditor should **disclaim an opinion if**, having been unable to obtain sufficient appropriate audit evidence on which to base the opinion, the auditor concludes that the effects on the financial statements of any undetected misstatements could be both material and pervasive. If, after accepting the engagement, the auditor becomes aware that management has imposed a limitation on the audit scope that the auditor considers likely to result in the need to express a qualified opinion or to disclaim an opinion on the financial statements, the auditor should request that management remove the limitation.

156. If expressing a modified audit opinion, the auditor should also modify the heading to correspond with the type of opinion expressed. ISSAI 1705¹⁹ provides additional guidance on the specific language to use when expressing a modified opinion and describing the auditor's responsibility. It also includes illustrative examples of reports.

Emphasis of Matter paragraphs and Other Matters paragraphs in the auditor's report

157. If the auditor considers it necessary to draw users' attention to a matter presented or disclosed in the financial statements that is of such importance that it is fundamental to their understanding of the financial statements, but there is sufficient appropriate evidence that the matter is not materially misstated in the financial statements, the auditor should include an Emphasis of Matter paragraph in the auditor's report. Emphasis of Matter paragraphs should only refer to information presented or disclosed in the financial statements.

158. An Emphasis of Matter paragraph should:

- be included immediately after the opinion;
- use the Heading “Emphasis of Matter” or another appropriate heading;
- include a clear reference to the matter being emphasised and indicate where the relevant disclosures that fully describe the matter can be found in the financial statements; and
- indicate that the auditor’s opinion is not modified in respect of the matter emphasised.

159. If the auditor considers it necessary to communicate a matter, other than those that are presented or disclosed in the financial statements, which, in the auditor’s judgement, is relevant to users’ understanding of the audit, the auditor’s responsibilities or the auditor’s report, and provided this is not prohibited by law or regulation, this should be done in a paragraph with the heading “Other Matter,” or another appropriate heading. This paragraph should appear immediately after the opinion and any Emphasis of Matter paragraph.

Annex III: The progress in implementation of Prior Year Recommendations

Audit Component	Recommendation given	Implemented	Under implementation	Not implemented
1.5 Recommendations	The Mayor should ensure that an analysis is undertaken to determine the causes that led to emphasis of matter, to eliminate errors in the classification of expenditures and incomplete recording of assets. It is necessary to undertake actions required to address causes that may impact on audit opinion, namely to record correctly all capital assets.			No
Prior Year Recommendations	The Mayor should ensure that an action plan is produced and will be rigorously implemented with specific activities and persons accountable for implementation of recommendations, which clearly sets out a timetable for addressing the recommendations. Recommendations affecting the greatest areas of significance of financial management and controls should be treated with primary focus.			No
2.4 FMC Self-Assessment Checklist	The Mayor should ensure that a review of the processes for completing the self-assessment checklist and proactively addressing areas of weaknesses is implemented. A revised mechanism to confirm the accuracy of the checklist and to		Internal audit has revised the self-assessment checklist, but still this list does not contain all the requirements as required with FMC.	

	ensure supporting documentation should be applied.		Such as lack of risk management list, lack of strategic plan, etc.	
2.5.1 Risk Assessment	The Mayor should produce an overall risks management strategy as soon as possible, which would clearly set forth the management approach to respond to risks. Management should also produce, besides identification of risks at operational and strategic level, an action plan which would define action measures to prevent and manage potential risks.			No
2.5.2 Management Reporting	The Mayor should ensure that a review is implemented to determine the format of financial and operational reporting to senior management which is required to support effective business management and ensure that an appropriate solution is in place by the end of 2016.			No
2.5.3 Municipality strategic planning	The Mayor should adopt an overall strategic plan for Municipality, which would define long-term objectives and serve as an orientation platform for the production of annual plans, for the conduct of comparative analysis between years and measuring results against objectives.			No
2.6 Internal Audit System	To gain maximum benefit from Internal Audit activity, the Mayor should review reasons for limited actions taken by Management related to internal audit recommendations and		The IAU Recommendations have been implemented partially by the	

	should coordinate cooperation with Audit Committee for increasing and improving internal control quality.		management of the organization.	
3.2 Financial Management and Control Conclusion	The Mayor should ensure that budget performance is systematically monitored on a monthly basis and that this review identifies and addresses barriers to planned levels of budget execution. Where initial budget assumptions are found to be incorrect this should be fully reflected in the final budget position.			No
3.3 Procurement	The Mayor should initiate a detailed review of all cases mentioned above to conduct an analysis why legal requirements and procurement rules are not implemented and take adequate measures after reviewing the cases. It should also be assessed why certification controls have failed to prevent irregular payments; such is the case with fuel payments.		Partially implemented, there were no cases where the evaluation committee had eliminated cheaper bidders, but we have examined contracts that are signed with the absence of funds.	
3.4 Expenditure not related to Procurement	The Mayor should conduct a review of compensations/payments for commission and of the agreements with other institutions in order to confirm their reasonability and should be in accordance with applicable laws to avoid irrational payments.	Yes		
3.4 Expenditure	The Mayor should ensure a review of cases identified to find out causes of occurrence and should take necessary	Yes		

not related to Procurement	measures for their elimination in the future. The Mayor should consider the possibility to contract one single package of mobile telephony services. This would ensure more convenient prices and would decrease the cost of telephony services.			
3.4.1 Remunerations (Wages and Salaries)	The Mayor should ensure that contracts are signed based on clear criteria in order that the process is transparent and competitive and employment contracts are preliminary secured. Contracts should specify the monthly amount and payment of salaries should be in compliance with contracts. Personnel officers should complete evidence on work experience to create the legal grounds for additional execution based on experience. Remuneration for holding informal classes should be done in accordance with regulation.	Yes		
3.4.2 Subsidies and Transfers	The Mayor should review cases identified to ensure that controls in this area are applied according to requests, to ensure that funds are used for the purpose planned and in accordance with regulations.	Yes		
3.5 Revenues (including own source revenues)	The Mayor should ensure a process of monthly regular harmonisations between municipal departments and finance administration and should put in place sustainable controls which ensure a sound planning and effective	Yes		

	collection of Municipality own source revenues.			
3.5 Revenues (including own source revenues)	The Mayor should ensure that sound analysis of the failure to collect revenues from waste management is carried out in order to achieve Municipality's objectives in the creation of sustainable financial system. Reconciliation with EO should be considered preliminary and payments should not be done to those owing to the Municipality.		The collection of invoices from the waste collection services have had signs of progress, but still the companies dealing with waste management have liabilities to the Municipality.	
3.5 Revenues (including own source revenues)	The Mayor should review reasons of the existing situation and establish measures required to collect all outstanding obligations within the reasonable period, or otherwise, should stop the use of public properties to owners, not paying their obligations to Municipality.			No
3.5 Revenues (including own source revenues)	The Mayor should ensure that when announcing public auctions, participants are preliminary conditioned with sanctions if they withdraw after the opening of public auction and should respect regulation for the allocation on the use of public areas through public auction.	Yes		
3.6.1 Capital and Non Capital Assets	The Mayor should review why assets identified are not recorded in the E-asset system, and address weaknesses related to constant update of the assets register. Requirements related to recording and maintenance should			No

	be fully applied.			
3.6.2 Handling of Receivables	The Mayor should consider establishing a special working group to review the execution of collection of debts, in particular, the enormous increase within a year of the accounts receivable from the waste collection services. The Mayor should also conduct an analysis in order to identify causes of failure of businesses in the payment of debts, and all means available should be used, including legal remedies.			No
3.6.3 Handling of Debts	The Mayor should conduct a critical review of the situation of arrears , to define necessary measures for addressing the issues identified, while payments should be made within the time limits set out in financial regulation. To handle these contingent liabilities, in coordination with the legal Municipality representative, a review of the status of liabilities should be undertaken, to determine the priority of payments, to eliminate the circumstances which may cause their direct payment from MoF or according to court decisions.		The municipality has addressed partially this recommendation and there were no cases where invoices to be presented in AFS to be presented as unpaid liabilities, but still haven't managed liabilities at a satisfactory level due to the reason that the amount of liabilities was very high.	

Annex IV: Letter of confirmation

[Put the Municipality's logo]

LETTER OF CONFIRMATION

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

To: National Audit Office

Venue and date:

Honoured,

We hereby confirm that:

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

Mayor:



Republika e Kosovës
Republika Kosova
Kosova Cumhuriyeti



Komuna e Prizrenit
Opština Prizren
Prizren Belediyesi

DATË:	02.05.2017
REFERENCE:	Zyrtarisht
PËR:	Lavdim Maxhuni Udhëheqës Ekipi nga Zyra Kombëtare e Auditimit
CC:	Florim Beqiri Drejtor i Departamentit në Zyrën Kombëtare të Auditimit
PERMES:	Prof. Dr. Ramadan Mulla Kryetar i Komunës së Prizrenit
NGA:	Ertan Simitci, Drejtor i Drejtorisë për Ekonomi e Financa
LËNDA/TEMA	LETËR E KONFIRMIMIT - Për pajtueshmërinë me të gjeturat e Auditorit të Përgjithshëm për vitin 2016 dhe për implementimin e rekomandimeve

Të nderuar,

Përmes kësaj shkrese, konfirmoj se:

- Kam pranuar draft raportin e Zyrës Kombëtare të Auditimit për auditimin e Pasqyrave Financiare të Komunës së Prizrenit, për vitin 2016 (në tekstin e mëtejme "Raporti");
- Pajtohem me të gjeturat dhe rekomandimet, si dhe
- brenda 30 ditëve nga pranimi i Raportit final, do t'ju dorëzoj një plan të veprimit për implementim të rekomandimeve, i cili do të përfshijë afatet kohore dhe stafin përgjegjës për implementimin e tyre.

Me respekt!