



REPUBLIKA E KOSOVËS / REPUBLIKA KOSOVA / REPUBLIC OF KOSOVA

**ZYRA KOMBËTARE E AUDITIMIT
NACIONALNA KANCELARIJA REVIZIJE**

NATIONAL AUDIT OFFICE

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AUDIT REPORT
ON THE ANNUAL FINANCIAL REPORT OF MUNICIPALITY OF
RAHOVEC 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 Rahovec Municipality in consultation with the Assistant Auditor General, Qerkin Morina, who supervised the audit.

The opinion and report issued are a result of the audit carried out by Team Leader, Mehmet Muçaj, Fikret Ibrahimiri- member and Muharrem Qyqalla-member under the management of the Head of Audit Department, 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 01.12.2016.

Our audit focus 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 an Emphasis of Matter, we would like to draw your attention to the fact that assets register is not complete as lands in the amount of €541,787 and six payments in the amount of €120,036, that were executed in 2016 for capital investments were not recorded in the assets accounting register. In addition, the Municipality had misclassified expenditures, and out of the category of Capital Investments had paid the amount of €74,299 for goods and services.

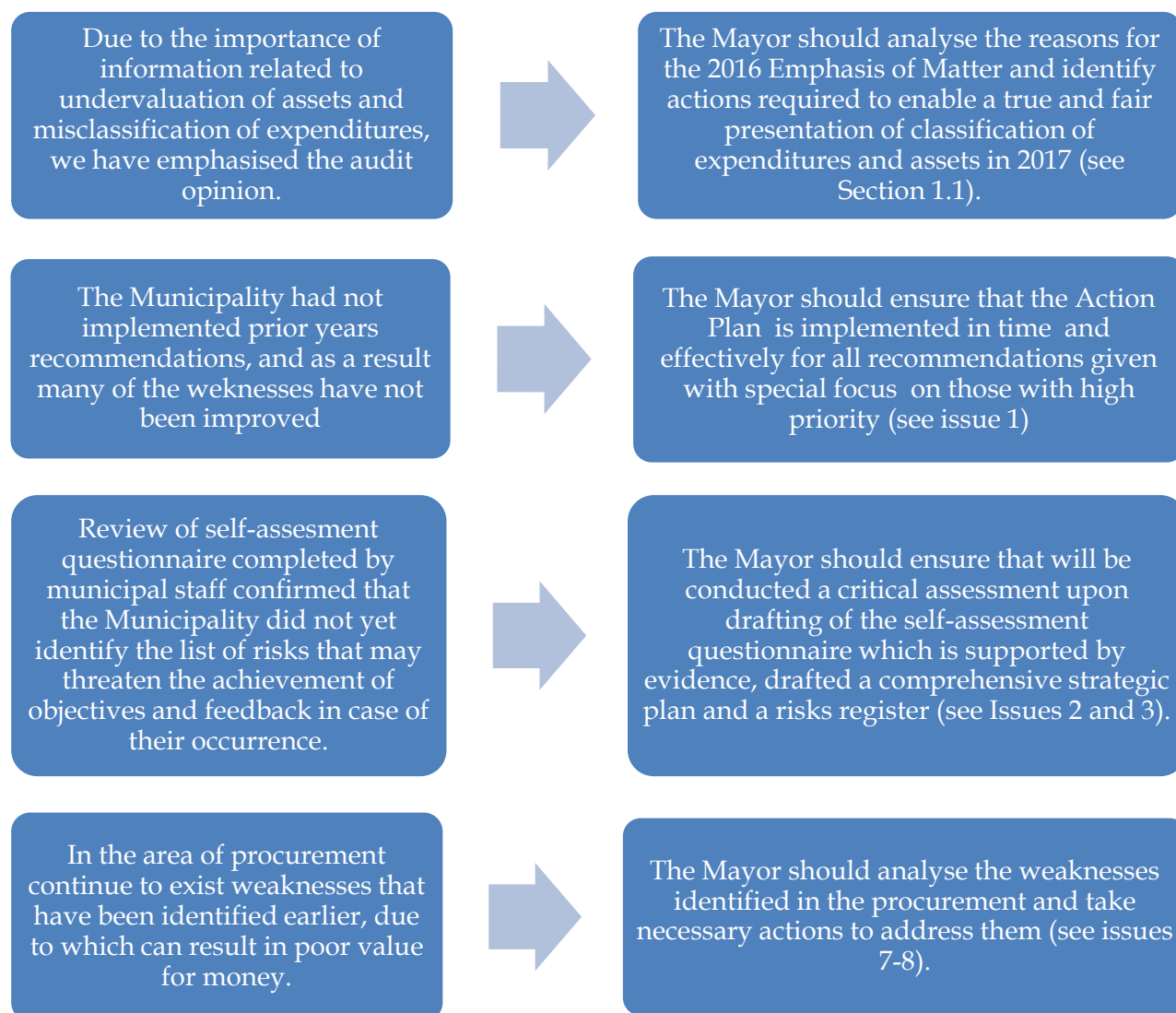
For more, please refer to Section 1.1 of this report.

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

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

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

Key Conclusions and Recommendations



Management response – audit 2016

The Mayor has taken into consideration and agreed on the audit findings and conclusions and committed to address the recommendations given.

We take it for granted that the Mayor:

- Will discuss the audit report in the Municipal Assembly; and
- By the end of January 2018, will also discuss the progress made on the implementation of the Action Plan on audit recommendations in the Municipal Assembly, before the AFS 2017 are submitted to the 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 Rahovec 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 to 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 would like to draw your attention to the fact that assets register is not complete as lands in the amount of €541,787 and six payments in the amount of €120,036, that were executed in 2016 for capital investments were not recorded in the assets accounting register.

In addition, the Municipality had paid €74,299 out of the category of Capital Investments, which by nature are goods and services. The most important of them are: demolition of illegal buildings

(€10,000), removal and cleaning of solid waste (€10,000 disinfection, disinsection and deratisation of public spaces (€17,475). This amount was approved with budget tables of 2016 budget as capital investments, but the projects presented in tables do not meet the conditions to be treated as capital projects. Errors are in initial planning by the Municipality and in inadequate approvals by the MoF.

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 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

The 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 in time;
- Procurement Plan for 2016; and
- Whether AFS are prepared and signed on time.

In the context of reporting requirements, we have not identified any irregularities.

A number of financial adjustments were required to the draft AFS and we have also made other suggestions to improve their quality as follows:

- Article 14 - inflow of cash - the Municipality had incorrectly presented the amount of €247,000 which were carried forward from 2015;
- Article 14 - inflow of cash, the revenues from donations were overvalued by €4,630;
- Article 18 - Contingent liabilities were disclosed in total, but not in detail as required under the AFS format; and
- Article 24 - Report on unspent donor funds - was incorrectly filled out as the Municipality in this Article had presented the situation of own source revenues and not the situation of donor funds.

Our suggestions have been taken into account by the Municipality and the abovementioned errors have been corrected, with the exception of assets issues and misclassifications based on which we have emphasised the opinion. See subchapter 1.1 Audit Opinion.

DECLARATION BY THE MANAGEMENT OF MUNICIPALITY

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 no material errors were identified, with the exception of issues mentioned in the audit opinion which we have considered to be immaterial.

1.3 Recommendations for the first part of the report

Recommendation 1 The Mayor should ensure that effective processes are in place to confirm that the 2017 AFS production plan addresses all issues raised in the report. This also includes Management review of the draft AFS with specific focus on areas where errors have been identified.

2 Governance

Introduction

Effective governance arrangements are fundamental to the 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 the Municipality particularly related to control environment and risk management. The self-assessment checklist completed by the Municipality only partially recognises this situation with some positive comments about existing arrangements not evidence based.

A key tool in support of effective governance is the implementation of audit recommendations. The Municipality implemented a small number of prior year recommendations (only 5 out of 15 recommendations have been fully implemented).

The Municipality did not draft a strategic plan and did not compile a list of risks with which the Municipality may face.

There were poor monitoring of Accounts Receivables and outstanding liabilities as they grow from year to year.

When it comes to compliance with legislation, as a result of non-implementation of relevant Regulations, our audit has disclosed weaknesses, including mainly procurement, revenues, assets, and Accounts Receivable.

2.1 Progress in implementation of Prior Year Recommendations

Our Audit Report on the 2015 AFS resulted in 14 recommendations. The Municipality implemented the requirement to prepare an action plan within 30 days after receiving the NAO audit report on AFS for 2015, stating how the recommendations will be implemented. The Audit Report on the AFS 2015 was also discussed at the Municipal Assembly on 27.09.2016.

At the end of our 2016 audit, 5 (five) recommendations have been implemented; 3 (three) were in process of implementation and 6 (six) were not implemented yet. For a more thorough description of the recommendations and how they are addressed, see Annex III.

Issue 1 - Implementation of Prior Year Recommendations - High Priority

Finding We have noticed that even though the Municipality had assigned a group to monitor implementation of recommendations given by the National Audit Office, there are still setbacks in their implementation. The monitoring group of implementation of recommendations had held several meetings in which was discussed the possibility of implementation of recommendations. However, it is needed a process that confirms the degree of implementation of recommendations and identification of obstacles in order to take actions for their full addressing. Such an approach is required to manage on-going improvements in the Municipality.

Risk	<p>Some recommendations are repeated from last year indicating continued weaknesses of internal controls in key financial systems which relate to:</p> <ul style="list-style-type: none">• Incomplete register of municipal assets;• Failure to draft risk register and lack of a comprehensive strategic plan;• Lack of management reporting;• Failure to collect revenues in line with the contract, and deficiencies in the monitoring process of buildings rented out; and• Addressing of challenges that relate to collection of Accounts Receivable.
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Recommendation 2 The Mayor should ensure that the monitoring group undertakes specific actions towards drafting a clear action plan on implementation of recommendations. This plan should be monitored at least quarterly, and is applied a rigorous accountability process in case this plan is not implemented.

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. During the audit we have tested the quality of FMC self-assessment submitted to the MoF, by assessing one key question in each component of the checklist. Our conclusions are 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	<p>As part of our audit we have considered key questions related to the five components of the self-assessment checklist. The Municipality had completed the self-assessment questionnaire based on the municipal development plan. For the questions considered we found that the following issues were not fully addressed:</p> <ol style="list-style-type: none">1. The Self-Assessment questionnaire completed by municipal staff confirmed that the Municipality has not yet identified the risk register that may threaten the achievement of objectives and feedback in case of their occurrence;2. The Municipality did not develop a comprehensive strategic plan;3. The Municipality did not monitor the progress on meeting the objectives.
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Internal audit did not carry through an independent assessment of management's assertions found within the completed checklists and did not report for accuracy and appropriateness to CAO as required by the FMC procedures.

Risk Failure to draft of a comprehensive strategic plan and risks register diminishes the quality of services provided to citizens, as Municipality's objectives are not addressed in a timely and planned manner.

Recommendation 3 The Mayor should ensure that a list of risks and strategic plan are drafted. The strategy should be monitored on constant basis to ensure that strategic objectives are being met. The Internal Audit Unit should conduct the final review in order to confirm the accuracy of the checklist, prior being submitted to the MoF.

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 the 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. The Municipality drafted a range of strategic documents such as: Urban plan which was updated in the spatial planning part in 2013, strategy of regional development 2010-2015, strategy of local development of 2009, local development plan of 2011, and the emergency plan for the Municipality of Rahovec.

Issue 3 - Strategic Documents - High Priority

Finding We have identified that Rahovec Municipality had not drafted documents such as: Anti-Corruption Plan, comprehensive strategic plan.

Risk Due to lack of strategic documents is hindered the establishment of long-term development objectives and measurement of progress made in achievement of Municipality's objectives, as one of essential conditions of good governance.

Recommendation 4 The Mayor should draft strategic plans and set clear objectives in all sectors of the Municipality, and the same are systematically monitored in order to evaluate the initial planning and progress in achieving objectives in certain periods.

2.3.2 Management Reporting and Accountability

A range of internal controls is 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 - Lack of monthly reporting - High Priority

Finding The Municipality has in writing only the minutes of meeting from the Board of Directors, and there are no written monthly reports prepared by the Directors of the Departments for the Mayor, wherein should be described operational and financial activities.

According to the Budget Law for 2016, The Chief Financial Officer of every municipality shall submit to the Mayor within three (3) weeks of the close of each quarter a report detailing the progress on implementation of all capital projects with a value greater than ten thousand (€10,000). A copy of such report shall be delivered to the Minister of Finance, but these reports were not prepared and submitted according to legal requirements.

Risk Lack of monthly reports from the directors to the Mayor, reduces the ability of management to manage effectively the activities of the Municipality, to respond to financial challenges in a timely manner and implement effective budget control.

Recommendation 5 The Mayor should ensure that a review is carried out to determine the form of financial and operational reporting and monthly written reporting is made by the Directors to the Management. In addition, to take measures to ensure that reporting by the CFO are done in line with legal requirements on the physical progress of capital investments.

2.4 Internal Audit System

The Internal Audit Unit (IAU) operates with one auditor who at the same time is a Director of the Unit. IAU prepared an internal audit strategic and annual plan which was approved by the Management. IAU had planned seven audit reports, which have been finalised. Audits carried out relate to: (1) Revenues and Expenditures in the Directorate of Cadastre and Geodesy (audit of activities of 2015 and the first quarter of 2016), (2) Revenues and Expenditures in the Directorate of Urban and Spatial Planning (audit of activities of 2015 and the first quarter of 2016), (3) Revenues and Expenditures in the Main Family Medicine Centre (audit of activities of 2015 and 2016), (4) Revenues and Expenditures in the Public Services Directorate (audit of 2015 and 2016), (5) Revenues and Expenditures in the Administration Directorate (audit of activities of 2016), (6) Revenues and Expenditures in the Budget and Finance Directorate, and (7) Audit of the Procurement Office, namely initiation of procurement procedures for 2016.

Issue 5 - Internal Audit Unit - High Priority

Finding

We have not relied on the work of the IAU due to the fact that some reports had focused on activities of 2015, and our objectives differed from those of the IAU. Furthermore, reports of IAU were not clear and properly documented and as a result, the manner in which issues were handled in the reports does not provide sufficient assurance to management.

The Audit Committee was not operational during 2016, although it was established in 2014.

Risk

Internal audit did not provide adequate assurance on the effectiveness of internal controls. Due to lack of expected contribution by the IAU increases the risk, as the internal control system may not improve. While, inoperable Internal Audit Committee affects assessment, quality and strengthening of the internal audit unit.

Recommendation 6

The Mayor should ensure that the internal audit will focus on the activities in the current year and its contribution to be more productive through qualitative reports. In addition, to ensure that the Audit Committee is functionalised within a reasonable period.

3 Financial Management and Control

Introduction

Our work on Financial Management and Control (FMC) outside of the areas of Governance referred to Section II reflects the detailed work undertaken on Revenue and Expenditure Systems within the Municipality. 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 built-in an internal control system which operates in general, but effectiveness of control needs to be improved in certain areas where shortcomings have been identified. The main areas where improvements are needed are: monitoring over rented buildings, procurement, assets management, management of accounts receivable, and increase 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 (in €)

Description	Initial Budget	Final Budget	2016 Receipts	2015 Receipts	2014 Receipts
Own Source Revenues	1,158,014	1,158,014	1,009,926	969,696	1,017,555

Out of the total planned Own Source Revenues (€1,158,014), the Municipality managed to collect only 87% (€1,009,926). Total collected revenues include revenues from court fines (€72,420) and traffic fines (€59,764).

Table 2. Sources of budgetary Funds (in €)

Description	Initial Budget	Final Budget ²	2016 Outturn	2015 Outturn	2014 Outturn
Sources of Funds	11,384,998	11,970,412	11,567,016	11,473,317	10,463,701
Government Grant -Budget	10,226,984	10,458,940	10,420,032	10,403,275	9,530,093
Carried forward from previous year ³ -	-	247,444	245,380	256,666	166,113
Own Source Revenues ⁴	1,158,014	1,158,014	801,797	746,922	737,857
Domestic Donations	-	11,512	5,400	0	0
External Donations	-	94,502	94,407	66,454	29,638

The final budget compared with the initial budget was increased by €585,414. This increase is a result of revenues carried forward from the previous year (€247,444), and increase of government grant (€231,956) following the budget review.

In 2016, the Municipality spent 97% of the budget, which is quite significant execution level, with a slight increase of 2% compared to the previous year.

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	11,384,998	11,970,412	11,567,016	11,473,317	10,463,701
Wages and Salaries	6,895,620	7,002,751	6,966,078	6,818,898	6,228,063
Goods and Services	686,913	659,262	657,625	771,189	634,577
Utilities	270,500	250,500	250,497	280,665	226,174
Subsidies and Transfers	123,312	174,340	173,992	142,160	105,951
Capital Investments	3,408,653	3,883,559	3,518,824	3,460,405	3,268,936

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.

3.1.1 Revenues

Own Source Revenues collected by the Municipality in 2016 of €260,404, were increased by around 12% compared with previous year. They relate to revenues from property tax, construction license, and other administrative fees.

The following shortcomings were identified during the audit of the Own Source Revenues:

Issue 6 – Revenues from property tax and rent – Medium Priority

When planning revenue from property tax, the Municipality does not carry out a proper evaluation of the collection capacities based on collection trends from previous years. In 2016 it planned to collect €332,000 from property tax whereas were collected €370,509. In addition, we have identified that Municipality had not managed to verify 1/3 of registered properties for property tax. According to the property tax register, the Municipality has 14,894 municipal registered properties, while during 2016 had made only 198 verifications (this is based on the register provided).

We have noticed lack of activities by the Municipality on collection of revenues from renting municipal buildings. In five cases we have reviewed contracts on use of municipal buildings and noticed that liabilities owed to the Municipality are €43,459.

Risk

Planning without being supported in collecting trend analysis presents a basis for poor planning. Failure to verify 1/3 of properties may result in lack of complete information in terms of current taxable property with the potential impact that the estimated revenues for property tax are not collected.

Due to uncollected revenues from rent, capital projects planned to be financed from own source revenues will not be implemented.

Recommendation 7 The Mayor should ensure when planning the revenues from property tax, the trend of collection as in prior periods is taken into account and ensure that the verification of municipal property is done on a regular annual basis, as required by law. In addition, should carefully administer all municipal properties and cease the use of public properties when users fail to meet financial obligations.

3.1.2 Wages and Salaries

The planned budget for Wages and Salaries was €7,002,751, and the same were spent almost at maximum level €6,966,078€ or 99%.

Wages and Salaries are paid through a centralised system. We have tested the compliance of payroll lists with the payroll system (current employees, recruitment, dismissals, maternity leaves, pensions, and payments to municipal advisors). We have also reviewed whether employees are paid in line with the contract. Our samples have not resulted with any issues that need reporting.

Recommendations

We have no recommendations in this area.

3.1.3 Goods and Services and Utilities

The final budget for Goods and Services and Utilities in 2016 was €909,762, while were spent €908,122. Our samples have not resulted with any issues that need reporting.

Recommendations

We have no recommendations in this area.

3.1.4 Subsidies and Transfers

The final budget for Subsidies and Transfers was €174,340, while were spent €173,992. The Municipality has an internal regulation based on which subsidies are awarded. From our review, we have not noticed any issues that need reporting.

Recommendations

We have no recommendations in this area.

3.1.5 Capital Investments

The final budget for capital investments was €3,883,559, while were spent €3,518,824.

Issue 7 - Weaknesses in procurement procedures - High Priority

Finding In the project "Purchase of Geodetic Instrument", the Municipality had entered into a contract with the Economic Operator (EO) that had the highest price, even though according to the bid evaluation committee, the EO with the lowest price had met the criteria and was responsive. The contract was entered concluded for €11,978 while the price of the competing EO was €9,250. Furthermore, the procurement office had not notified the eliminated EO in writing on the reasons behind elimination from the tender.

In three cases, the procurement office had not notified EOs in writing on the reasons of their elimination from the tender.

Risk Awarding the contract to the EO with the highest price damages the municipal budget. Failure to notify the EO in writing on tender elimination makes it impossible for the eliminated EO to file a complaint to competent institutions.

Recommendation 8 The Mayor should analyse the reasons why in the abovementioned cases procurement requirements were not implemented consistently, and to ensure that in the future contracts are awarded to the EOs that have the most favourable prices, and that EOs eliminated from tender are notified in writing.

Issue 8 - Contract contracts more than budget appropriations - Medium Priority

Finding In the project "Construction and asphaltting of the road Rahovec - Pataqan i poshtëm" The Municipality on 16.09.2016 had entered into a contract with a price higher than budget appropriations foreseen in table 4.2 for capital projects. The contract was signed in the amount of €845,981 while budget appropriations were €75,000 (2016), and the estimates for the two following years were €130,000 (2017), and €100,000 (2018).

Similarly, in the project "Construction and asphaltting of the road Drenoc - Zatriq", the contract was signed in the amount of €348,947 while budget appropriations for 2016 were €55,000 and estimates for the two following years were €100,000 (2017), and €80,000 (2018).

Risk It is not clear how these projects will be completed, as the financial structure of these projects is not clear. Entry of Municipality into contracts that exceed budget appropriations foreseen under the budget law poses a risk of such projects being delayed, damaged before being completed, or not get completed at all.

Recommendation 9 The Mayor should implement requirements of the law and financial regulations and not to enter into contracts with EOs before allocating appropriate funds, and to ensure that will not be entered into contractual obligations beyond budget appropriations foreseen under the law on the annual budget.

Issue Issue 9 - Weakness in the development of procurement procedures - Medium Priority

Finding In the project “Construction and asphaltting of the road Retijë - Mamushë”, the Municipality on 23.06.2016 had concluded a contract in the amount of €99,355. We have noticed that publication for contract award was done on 31.05.2016 without presenting the required document under the Tender Dossier (Certification by the Basic Court) which was submitted on 09.06.2016, namely nine days after the publication.

Risk Failure by EOs that participate in a tender to provide evidence on time, besides being in disagreement with the requirements of the Tender Dossier, poses a risk of that EO not to be the most adequate EO, and is a discrimination towards other EOs.

Recommendation 10 The Mayor should ensure that the Procurement Office fully adheres to the requirements of the Tender Dossier, so that the contracts are concluded with responsive EOs, and procedures are fully transparent.

3.2 Assets

3.2.1 Capital and Non Capital Assets

The Municipality during 2016 continued to register municipal assets in the accounting records. The value of assets recorded in the AFS 2016 was €60,556,000 and in 2015 was €52,206,000. Therefore, we have a positive trend when it comes to recording municipal property. However, the Municipality has not yet managed to complete the comprehensive register of municipal assets.

Issue 10 - Management of assets through e-assets system - High Priority

Finding The e-assets system is not fully operational. In the e-assets are recorded assets under €1,000 of the municipal administration and education directorate, while are not recorded assets of the health directorate.

Risk Incomplete functioning of e-assets system makes it impossible to manage and have control over assets and stocks available, and this poses a risk of loss and misuse of assets.

Recommendation 11 The Mayor should ensure functionality of the e-assets system and strengthening of requirements so that all assets and stocks under €1,000 are recorded in this system.

3.2.2 Receivables

Receivables at the end of 2016 were €2,074,000 and compared with the previous year (€1,940,000) they have increased by €134,000.

Issue 11 - Poor policy on collection of Accounts Receivable - Medium Priority

Finding Municipality's Accounts Receivable have increased every year, as the management has not taken any specific actions to collect them. The value of AR consist of property tax (€1,195,000), business fees (€818,000), rent from business locations and public spaces (€61,000).

Risk Failure to collect of debts may have an impact on non-fulfilment of the spending plan. Inefficient policies of the Municipality in handling these accounts, resulted in their growth and it increases the risk for failure to execute municipal projects planned from own resources. In addition, if such accounts are not collected for a long time can turn into bad debt, thus not collectable.

Recommendation 12 The Mayor should ensure that a reassessment process is initiated, where all accounts receivable are analysed in terms of age and real possibilities for collection and propose concrete measures, not excluding administrative and other measures (if needed).

3.3 Outstanding Liabilities

The Statement of outstanding liabilities to suppliers at the end of 2016 was €920,458, which presents a significant increase compared with the previous year (€333,000). These liabilities were carried forward to be paid in 2017.

Issue 12 – Increase of outstanding liabilities - High Priority

Finding While auditing liabilities we have identified that liabilities had increased by €587,458 compared to the prior year. This is as a result of insufficient internal controls over the area of liabilities and entry into contracts without sufficient funds.

Risk Reported amounts of outstanding liabilities are significant for the municipal budget, and as such can cause large budget movements. Entry into contracts without sufficient funds results in increased liabilities and it affects budget and objectives of the following year, as the Treasury can execute payments, and court disputes may be faced due to complaints filed by Economic Operators.

Recommendation 13 The Mayor should carefully analyse the reasons why the Municipality is uncontrollably creating liabilities, financing of which is not safe at all. Thereafter, should strengthen controls over liabilities and ensure that it will not enter into contracts without having a secure source of funds.

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 Mayor 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: Prior Year Recommendations

Audit Component	Recommendation given	Implemented	Under implementation	Not implemented
1.5 Recommendations	The Mayor should ensure that effective processes are in place to confirm that the 2016 AFS production plan formally addresses all issues raised, including significant risks on misclassification of expenditures and disclosure of assets. This also should include the management review of the draft AFS with specific focus on high risk areas and areas where errors have been identified.		The municipality had recorded payments from third parties in KFMIS, while in 2016 had misclassification of expenditures and the register of assets is still incomplete.	
2.3 Implementation of the prior year Recommendations (issue 2)	The Mayor should strengthen control measures and accountability against those persons charged to address fully the recommendations that the actions defined in the Action Plan are implemented, particularly in high risk identified areas and within the timetable set.	X		
2.4 Self-Assessment Checklist (Issue 3)	The Mayor should ensure that completion of the self-assessment checklist is critical and ensure that areas of weaknesses are proactively addressed. The possibility of updating the municipal development strategy should be reviewed which would include clear objectives and achieve municipal objectives. Further on, a revised mechanism should be applied to provide evidence supporting self-assessment allegations.		The checklist was prepared by the Municipality, but Internal Audit did not make an independent assumptions of management that the controlling lists are completed and there was no risk management list.	

2.5.1 Risk Assessment (issue 4)	The Mayor should ensure that a list is prepared where risks are identified according to the level and the likelihood that they may occur, and whether response measures are foreseen if they occur. Further on, the responsibility for risk management should be delegated to a responsible person who will report to management and ensure the implementation of the requirements in this field.			X
2.5.2 Management Reporting (issue 5)	The Mayor should ensure that a review is implemented to determine the format of financial reporting to senior management which is required to support effective business management and ensure that an appropriate solution is in place.			X
2.6 Internal Audit System (issue 6)	The Mayor should draft an action plan, which should be implemented by confirming responsible officials including timeframe to undertake the actions. Internal audit should have a special focus on activities in the current year, having preventive effect in terms of the actions. In order to strengthen the role of Internal Audit, the Audit Committee should be operational.			X
3.3 Budget Planning and Execution (issue 7)	Approach to budget planning for capital projects needs substantial improvements. Before defining investment funds, the Municipality should carefully and objectively analyse which projects are of priority and which of them have a real chance to succeed. Timely procedures (project design, security performance, procurement, etc.) are some of the prerequisites for projects to be implemented according to plan.	X		

3.4 Procurement (Issue 8)	The Mayor should conduct an internal review to determine why procurement requirements were not addressed in all procurement cases and exercise more controls to ensure that the systematic weaknesses identified are addressed. He should ensure that the Municipality will not enter into obligations more than the appropriations foreseen by law on budget appropriations.		Written notification to the operators eliminated from the bids has been made, the approximate quantities are specified in the tender dossier, procurement procedures that were not included in the procurement plan were minimized. There were cases also in the year 2016 of signing contracts in higher amount than the budget appropriations.	
3.4 Procurement (Issue 9)	The Mayor should examine the case why the Project Manager did not apply the terms of the contract and ensure that bill of quantity, calculations and other technical analyses for projects to be tendered are thoroughly carried out and deviations from the original contract are within allowed limits. After reviewing the case, the responsible persons should initiate appropriate accountability measures.	X		
3.5 Expenditure not related to Procurement (issue 10)	The Mayor should ensure that payments are not made before confirming that the works or services are rendered. Payments must be documented with reports confirming the receipt of the works/services. In terms of monitoring and reporting obligations arising from such agreements, it should be subject to regular reviews by the management of the Municipality. In order to eliminate the risk of failure for these agreements, we would suggest that such practices of payments are stopped.	X		

3.5.1 Expenditure not related to Procurement(Issue 11)	The Mayor should review contracts for special services and ensure that such contracts are used only for the real needs and not engage persons for common positions.		In 2016, the municipality had employed 28 workers with special services contracts and the term of the contracts was up to 6 months. Recruitment procedures took place in the municipality in several cases.	
3.5.2 Remunerations (Wages and Salaries) (Issue 12)	The Mayor should ensure that of night shifts at FMC are reviewed in order not to exceed the number of overtime and labour law is considered.	X		
3.6 Revenues(Issue 13)	The Mayor should ensure that contracts are terminated as foreseen by the decision of MA for lessees who do not fulfil their obligations to the Municipality. In the future, the Municipality's property should be verified as required by law.			X
3.7.1 Capital and Non Capital Assets(Issue 14)	The Mayor should immediately establish the competent committees for proper and complete evaluation of all non-financial assets and monitor the results of the evaluation. Recording results should be integrated into a single register for all sectors. The process of recording assets higher than €1,000 in KFMIS should be continued until the recording is finalised. Asset Management Officer and officials involved in receiving municipal assets should communicate effectively to avoid non-implementation of the Regulation and non-consolidation of assets" value.		The Municipality has established a property valuation commission that had evaluated some properties but in 2016 we have identified that there are properties which are not yet included in the assets register.	

3.7.2 Handling of Receivables (Issue 15)	The Mayor should systematically monitor the issue of revenue collection, to ensure that appropriate policies and measures are taken to maximize the collection of debts. It is necessary to carry out a detailed analysis setting out the reasons of delays in payments and propose concrete actions and resources needed to collect these debts.			X
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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 Rahovec, 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:



LETËR E KONFIRMIMIT

Për pajtueshmërinë me të gjeturat e Auditorit të Përgjithshëm për vitin 2016 dhe për implementimin e rekomandimeve.

Për: Zyrën Kombëtare të Auditimit

Vendi dhe data: Rahovec

Dt. 03.05.2017

I nderuar,

Përmes kësaj shkrese, konfirmoj se:

- kam pranuar draft raportin e Zyrës Kombëtare të Auditimit për Auditimin e Pasqyrave Financiare të Komunës së Rahovecit, për vitin 2016 (në tekstin e mëtejshëm "Raporti");
- pajtohem me të gjeturat dhe rekomandimet dhe nuk kam ndonjë koment për përmbajtjen e Raportit; si dhe
- brenda 30 ditëve nga pranimi i Raportit final, do t'ju dorëzoj një plan të veprimit për implementimin e rekomandimeve, i cili do të përfshijë afatet kohore dhe stafin përgjegjës për implementimin e tyre.

Kryetari:

Idriz Vehapi

