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Zyra Kombëtare e Auditimit
Nacionalna Kancelarija Revizije
National Audit Office

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AUDIT REPORT
ON THE ANNUAL FINANCIAL STATEMENTS OF THE
MUNICIPALITY OF HANI I ELEZIT
FOR THE YEAR ENDED 31 DECEMBER 2017

Prishtina, June 2018

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 through quality audits strengthen accountability in public administration for an effective, efficient and economic use of national resources.

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 organizations 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 Hani i Elezit, in consultation with the Assistant Auditor General, Valbon Bytyqi, who supervised the audit.

The report issued is a result of the audit carried out by Enver Ramadani Audit Team Leader and Fetah Osmani and Hysen Restelica – Members, under the management of the Head of Audit Department Mujë Gashi.

TABLE OF CONTENTS

Executive Summary	4
1 Audit Scope and Methodology	6
2 Annual Financial Statements and other External Reporting Obligations	7
3 Financial Management and Control	11
4 Progress in implementing recommendations.....	18
5 Good Governance	19
Annex I: Explanation of the different types of opinion applied by NAO	22
Annex II: Progress in implementing recommendations of previous two years.....	25
Annex III: Letter of confirmation.....	30

Executive Summary

Introduction

This report summarizes the key issues arising from our audit of the 2017 Annual Financial Statements of the Municipality of Hani i Elezit, which determines the Opinion given by the Auditor General. The examination of the 2017 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 Plan dated 27/11/2017.

Our audit focus has been on:



The level of work undertaken by the National Audit Office to complete the 2017 audit is determined depending of the quality of internal controls implemented by the Management of the Municipality.

The National Audit Office acknowledges the Senior Management and Staff of Municipality, for cooperation during the audit process.

Opinion of the Auditor General

Unmodified Opinion with Emphasis of Matter

The Annual Financial Statements for 2017 *present a true and fair view* in all material aspects.

Emphasis of Matter

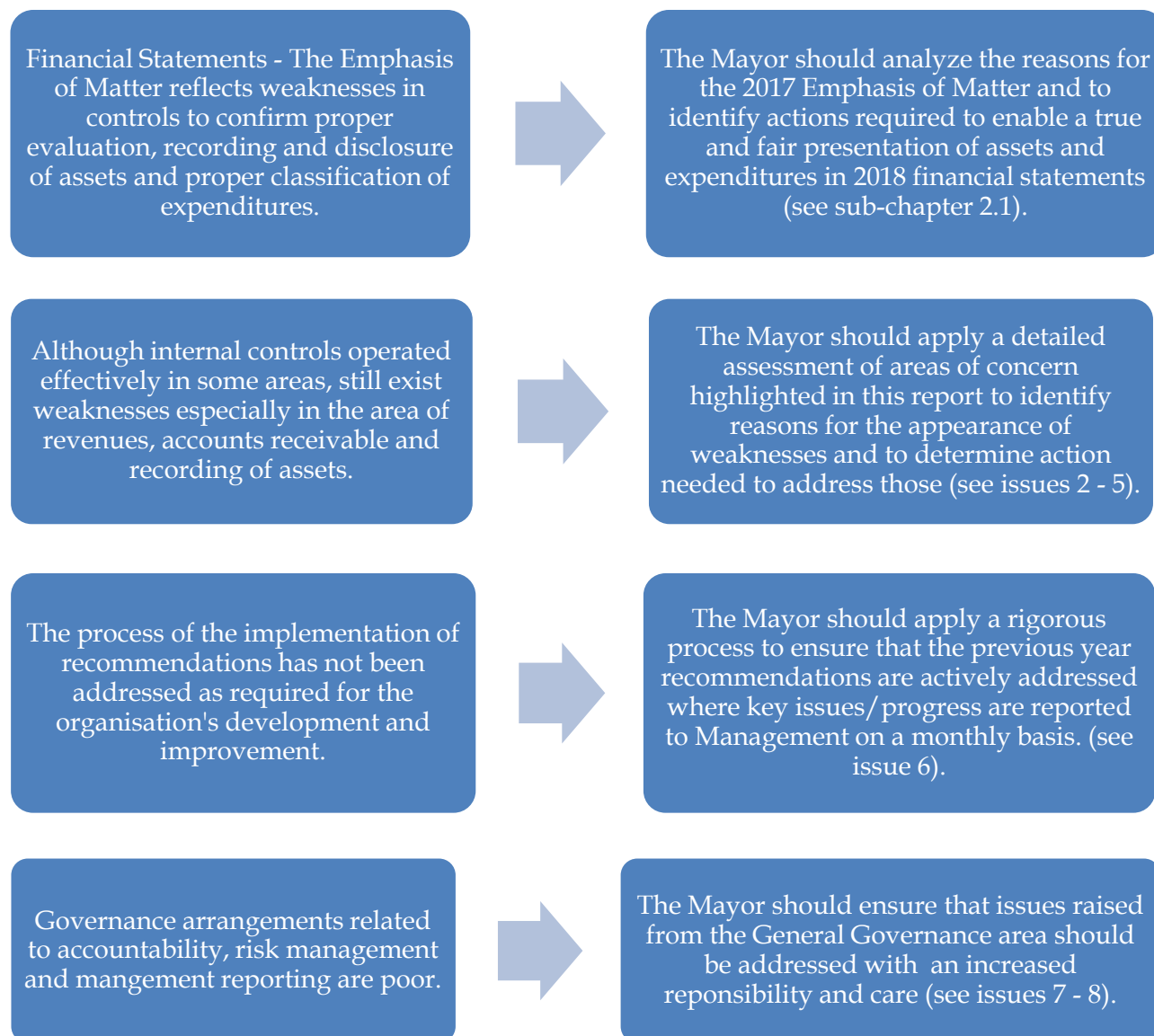
As Emphasis of Matter, we want to mention the fact that:

- Expenditures for goods and services in the amount of €24,821, were wrongly executed and reported from the capital investments category; and
- Disclosed information in the Annual Financial Statements in relation to assets is not correct.

For more, see Section 2.1 of this Report.

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

Key Conclusions and Recommendations



Management response to audit 2017

The Mayor has considered and agreed on the audit findings and conclusions and has committed to address all given recommendations.

1 Audit Scope and Methodology

Introduction

The National Audit (NAO) is responsible for carrying out a Regularity Audit which involves the examination and evaluation of Financial Statements and other financial records and expression of opinions on:

- Whether the financial statements give a true and fair view of the accounts and financial affairs for the audit period;
- Whether the financial records, systems and transactions comply with applicable laws and regulations;
- The appropriateness of internal controls and internal audit functions; and
- All matters arising from or relating to the audit.

Audit work undertaken reflected our audit risk assessment for the Municipality. We have analyzed the Municipality's business to the extent to which management controls can be relied upon when determining the overall testing required to provide the necessary level of evidence to support the Auditor General's (AG) opinion.

The following sections provide a more detailed summary of our audit finding with emphasis on observations and recommendations in each area of review. Management's responses to our findings can be found in Annex III.

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

2 Annual Financial Statements and other External Reporting Obligations

Introduction

Our audit 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 (MoF).

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 assertions are intended to provide the Government with the assurance that all relevant information has been provided to ensure that an audit process can be undertaken.

2.1 Audit Opinion

Unmodified Opinion with Emphasis of Matter

We have audited the AFS of the Municipality of the Hani i Elezit for the year ended on 31st of December 2017, which comprise of the Statement of Cash Receipts and Payments, Budget Execution Statement, Disclosures and other accompanying reports.

In our opinion, the Annual Financial Statements for the year ended on 31st of December 2017 present a true and fair view in all material aspects 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 MoF Regulation no. 01/2017 on Annual Financial Reporting of Budget Organisations.

Basis for the opinion

Our audit was conducted 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 Financial Statements” 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 for goods and services in the amount of €24,821, in the name of the project¹ for the execution of health services, were wrongly executed and reported from the capital investments category; and
- Three completed projects² in the total amount €322,000 were wrongly recorded as the following investments. As a result the depreciation in the amount of €10,175 has not been calculated, by overstating the Municipality's net assets. Further on, five facilities³, and two payments for capital investments, for "Construction of the Rezhanca creek bed" in the amount of €8,712 and payment "Supply with equipment" in the amount of €11,052, were not recorded in the assets account register.

Our opinion is not modified for these matters.

Responsibility of Management and Persons Charged with Governance for AFS

The Mayor of the Municipality of Hani i Elezit 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 no. 03/L-048 on Public Finance Management and Accountability (as amended and supplemented).

The Mayor of the Municipality is responsible to ensure the oversight 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.

¹ The health care project with Caritas Kosova.

² "Construction of the annex of the primary school Ilaz Thaçi" in the amount €237,000, "Paving of streets with concrete cubes" in the amount €25,000, and "Construction of the Rezhanca Creek" in the amount €60,000.

³ The facility of the high school "Dardania" financed by MEST, the facility of the primary school "Castle of Knowledge" in the village Paldenica, and the facility of the primary school "Veli Ballazhi" in village Goranca, the facility of the physical education hall financed by EU, as well as the Center for social work co-financed with the Ministry of Labor and Social Welfare.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will detect any material misstatement that might exist. 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.

2.2 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 Organizations;
- Requirements of LPFMA no. 03/L-048, (as amended and supplemented);
- Compliance with Financial Rule no. 01/2013 and 02/2013;
- Action Plan on addressing of recommendations;
- Requirements of Financial Management and Control procedures;
- If the draft plan and the final procurement plan has been submitted in time;
- Quarterly reconciliations of expenditures and revenues with the Treasury;
- Report of the procurement signed contracts; and
- If the Municipality had prepared and submitted regular quarterly reports to the Municipal Assembly and one copy to the MoF.

The Municipality of Hani i Elezit had prepared and submitted AFS within the legal deadline in the MoF. As a result of some identified errors, the Municipality had corrected the AFS by improving their reporting, however even after the correction, we have identifies some errors which have been disclosed to the Emphasis of Matter to the Audit Opinion.

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 correct in all material aspects.

2.3 Recommendations related to Annual Financial Statements

Recommendation 1 The Mayor should ensure that an analysis is undertaken to determine the causes of the Emphasis of Matter, and proper actions to be taken to address the causes systematically and to confirm the full recording of assets and to eliminate errors in the classification of expenditures.

Further on, it should ensure that effective processes are in place to confirm that the 2018 AFS production plan addresses all issues raised in the report and the Declarations made by the Chief Administrative Officer and Chief Financial Officer, should not be signed unless all necessary checks have been applied to the draft AFS.

3 Financial Management and Control

Introduction

Our work related to Financial Management and Control (FMC) reflects the detailed audit activities undertaken on Revenue and Expenditure Systems within Budget Organisations. Specifically, the focus of the audit was Budget management, Procurement issues, Human Resources as well as Assets and Liabilities.

Financial Management and Control Conclusion

The Municipality had spent 90% of the final budget for 2017 that means a good execution in the general level, however, the level of expenditures to the capital investments was low.

In the context of financial systems, controls over revenues are generally appropriate and are being implemented effectively, however, additional mechanisms are needed to react in their collection and collection of receivables in a greater extent. Improvements are required even to the assets management and reporting. Meanwhile, controls over expenditures were improved significantly in 2017.

3.1 Budget Planning and Execution

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

Table 1. Sources of budgetary Funds (in €)

Description	Initial Budget	Final Budget ⁴	2017 Outturn	2016 Outturn	2015 Outturn
Sources of Funds	2,406,534	2,694,976	2,422,548	2,189,897	2,094,367
Government Grant -Budget	2,166,680	2,332,005	2,240,415	1,851,081	1,901,743
Carried forward from previous year ⁵ -	-	86,192	31,440	106,108	44,134
Own Source Revenues ⁶	239,854	239,854	113,852	188,624	94,536
Internal Donations	-	-	-	-	-
External Donations	-	36,925	36,841	44,084	53,954

⁴ Final budget - the budget approved by the Assembly subsequently adjusted by the Ministry of Finance.

⁵ Own Source Revenues of Municipalities unspent in previous year carried forward into the current year.

⁶ Receipts used by the entity for financing its own activities.

The final budget in relation to the initial budget was increased for €288,442. This increase is a result of external donations of €36,924, revenues carried forward from the previous year in the amount of €83,192 and the budget increase of €165,325 based on the Government of Kosovo of date 15/12/2017.

The Municipality has spent 90% of the final budget in 2017 or €2,422,548, with an under spending of 5% compared to 2016 (95%). If we see the budget execution by economic categories, the execution was in a better level in all categories, with exception of the capital investments which was in a lower level (in 77% level).

Table 2. Spending of funds by economic categories - (in €)

Description	Initial Budget	Final Budget	2017 Outturn	2016 Outturn	2015 Outturn
Spending of funds by economic categories	2,406,534	2,694,976	2,422,548	2,189,897	2,094,367
Wages and Salaries	1,393,609	1,393,609	1,367,010	1,391,497	1,366,432
Goods and Services	180,551	206,591	188,215	211,387	264,565
Utilities	44,533	49,989	49,932	48,264	48,061
Subsidies and Transfers	51,104	51,492	49,801	53,159	47,640
Capital Investments	736,737	993,295	767,590	485,590	367,669

Explanations for changes in budget categories are given below:

- Despite the increase of the budget for capital expenditures during the year in the amount of €256,558, only 77% of the budget was spent. The low level of the execution in this category was because of the delayed approval of the additional budget for €134,831, with the Government decision of date 15/12/2017;
- The increase of the budget for Goods and Services was from the revenues carried forward in the amount of €545 and from the Government of Kosovo in the amount of €25,494;
- The increase of the budget for Utilities was from the revenues carried forward from previous year in the amount of €456 and from the Government of Kosovo in the amount of €5,000; and
- The increase of the budget for Subsidies and Transfers was from the revenues carried forward from previous year in the amount of €388.

Recommendations

We have no recommendations in this area.

3.2 Revenues

Revenues generated by the Municipality of the Hani i Elezit in 2017 were in the amount of €225,193. . These relate to revenues from property tax in the amount of €79,588 or 35% from the total revenues, revenues from business activities, revenues from construction permits, revenues from rent, administrative fees, etc.

Table 3. Own Source Revenues (in €)

Description	Initial Budget	Final Budget	2017 Receipts	2016 Receipts	2015 Receipts
Own source revenues	239,854	239,854	225,193	244,030	223,521
Total	239,854	239,854	225,193	244,030	223,521

Regarding the own source revenues, it can be seen that the execution percentage was 92% until 31 December 2017, that results with a decrease of 8% compared to 2016 (€244,030). The own source revenues have been used for Capital Expenditures 79%, Goods and Services 7% and Subsidies and Transfers 14%. While the amount of €181,518 was carried forward in 2018. The identified weaknesses have been presented in the following:

Issue 2 – Failure to verify the recorded properties

Finding The Municipality had not managed to perform the re-survey for the verification of 1/3 recorded properties, as required with the law for the immovable property tax, no. 03/L-204 and the applicable administrative instruction⁷. The Municipality had 864 recorded properties, but none of them was re-surveyed during the 2017. The lack of re-survey was as a result of the lack of surveying officials in field for the verification of properties and collection of information.

Risk Failure to verify the properties can result with deficiencies that the current information about the property tax database to be incorrect. This would negatively impact in the evaluation and billing of the property tax, and as a result, the understate of revenues from this category

Recommendation 2 The Mayor should improve the process of properties verification and to ensure that the verification of their 1/3 is being made on a regular annual basis, in order that notes about the property tax to be complete, to reflect the real situation of taxed properties. The increase of the property recording will result with more municipal revenues and better budget performance.

⁷ With AI no. 03/2011 on Collection and Recording of information about the property and the taxpayer, is required that within the year to be verified the 1/3 of the recorded properties.

Issue 3 – Failure to collect the business fees

Finding From the testing of seven samples in business, we have identified that the taxpayers liabilities to the Municipality were in the amount of €37,361. The Municipality only against one business had raised a procedure in courts, while against others had done only remarks, although with issued decisions by its side, was foreseen to stop their business activity.

Risk The identified weaknesses can result with fewer revenues from this category and unequal treatment of businesses. Failure to take punishment measures for all businesses that have not paid the liabilities, as business fees, increases the risk of non-collection of fees.

Recommendation 3 The Mayor should ensure that proper measures are set in order that all its receivables are collected within a reasonable time period. Further on, he should actively review all possible options, including legal remedies to ensure that the revenues have been executed.

3.3 Wages and Salaries

Wages and Salaries are paid through a centralized payment system managed by MoF. Controls that operate in the local level by the Municipality relate to: payments control, by signing the payroll lists, verification of possible changes that could be presented through forms; the budget review for this category and reconciliation with the Treasury. According the KFMIS data, the budget for the Wages and Salaries category was €1,393,609, while expenditures were €1,367,010, or expressed in percentage about 98% of the final budget of this economic category. The participate of the Wages and Salaries expenditures in the Municipality's total expenditures is 56%

Recommendations

We have no recommendations in this area.

3.4 Goods and Services and Utilities

The final budget for Goods and Services in 2017 was €256,579. Out of them €238,147 or 93% of the final budget were spent. Those relate to utilities €49,932 or 21% from the total expenditures, supplies for office €17,326 (7%), vehicle maintenance and repairing €14,062 (6%), supply with wood €18,562 (8%), and fuel for vehicle's €18,211 (8%).

Controls in this are generally have operated good, where from the tests carried out have not resulted with findings.

Recommendations

We have no recommendations in this area.

3.5 Subsidies and Transfers

The final budget for Subsidies and Transfers was €51,492. Out of them €49,801 or 97% of the final budget were spent in 2017. Awarded subsidies relate to financial support by the Municipality for different area and activities, as for sports clubs, cultural-artistic society, scholarships, the agricultural sector, etc. In this category, we have not encountered in problems that would result with findings.

Recommendations

We have no recommendations in this area.

3.6 Capital Investments

The final budget for Capital Investments was €993,295. Out of them €767,590 or 77% of the budget were spent in 2017. Those relate to construction of education facilities in the amount of €67,887 (9%), construction of local roads in the amount of €144,091 (19%), sewages in the amount of €179,367 (23%), other equipment's in the amount of €76,199 (10%), adjustment of rivers in the amount of €91,226 (12%), etc.

The identified weaknesses in this area have been handled to the Emphasis of Matter, to the Audit Opinion.

Recommendations

We have no recommendations in this area.

3.7 Capital and Non-Capital Assets

During the 2017, the Municipality has done a progress in the aspect of assets recording compared to previous year. However, despite the progress, still has not been achieved that the assets account register to be correct. The non-recording of capital assets by respective categories has been handled to the part of Emphasis of Matter, to the Audit Opinion, while in the following will be presented some other issues, which the Municipality should have taken into consideration in 2017.

Issue 4 – Poor management of non-financial assets

Finding The Municipality's non-capital asset under €1,000 disclosed in AFS was €77,937. According to the rule no. 02/2013 on Management of Assets, article 19, requires to be done the inventory of non-financial assets, and the article 22 requires to be done their depreciation. We have identified the following deficiencies:

- The Municipality has not depreciated non-capital asset with value under €1,000, therefore their value in AFS was overstated. According to the municipal officials the e-Asset system is not sufficiently functional because it does not enables the depreciation calculation that has resulted with incorrect disclosure of assets in AFS. Further on, in this system were not recorded 19 non-capital assets purchased during 2017 in the total amount €12,994; and
- Chief Administrative Officer had formed a committee for inventory of assets for 2017, but it had performed only the inventory of assets under €1,000 in the Municipality's facility and in the culture house, while in other locations was not performed the inventory. While the inventory of capital assets over €1,000 was not done at all. Further on, the committee for annual inventory of non-capital assets had not done the reconciliation of inventory registers with account registers kept from the assets officials.

Risk Failure to fully inventory of assets, causes deficiency in correct management and reporting of assets, at the same time risking misuse or loss of assets, while the non-recording of assets and lack of depreciation impacts in the overstate of municipal assets value.

Recommendation 4 The Mayor should ensure that in cooperation with the Ministry of Public Administration, the deficiencies in the e-Asset system are eliminated, including the assets depreciation and recording of remaining assets. Further on, the inventory process should be timely carried out, before the AFS have been prepared, and the inventory report should include a comparison of physical situation with that in the registers situation. If the difference is confirmed, those should be presented in the assets register and in the accounting register.

3.8 Receivables

The Municipality's accounts receivable shows amounts of funds that citizens and organizations are obliged to the Municipality for services, works, goods or properties they have benefited from the Municipality. According to the presented data in AFS, the total amount of these accounts at the end of 2017 was €511,754.

Issue 5 - Handling of receivables

Finding The Municipality had not taken active measures for the collection of receivables. The total debts to the Municipality, at the end of 2017 were €511,754 that results with increase for 13% in relation to 2016 (€451,291). Receivables consist of fees of property tax in the amount of €240,577, fees from business activities in the amount of €250,680, and from municipal property rents of €20,497. This is a result of non-placement of proper mechanisms by the Municipality for the increase of their collection.

Risk The lack of specific measures to collect the receivables has resulted in their increase, and consequently even with financial loss for the Municipality. Further on, this reduces even the Municipality's flexibility to the planned expenditures that are financed from own source revenues.

Recommendation 5 The Mayor should ensure the strengthening of mechanisms for the collection of receivables, using all available measures, initially using all necessary actions within the Municipality, then after to use even other legal measures.

3.9 Outstanding Liabilities

The statement of liabilities not paid to suppliers at the end of 2017 was €12,312, while in 2016 were €10,238. These liabilities are carried forward to be paid in 2018. Further on, at the end of the year have been contingent liabilities as court disputes in the amount of €69,189, while in the previous year were €70,600.

The Municipality in general applied a process relatively regular of the liabilities reporting. The Municipal Officials are aware for the requirements of the regulation for reporting of unpaid invoices and the responsible officer timely reports to the Treasury/MoF in relation to this. However, the liabilities amount in relation to previous year was increased for €2,074 or approximately 17%.

Recommendations

We have no recommendations in this area.

4 Progress in implementing recommendations

Our Audit Report on the 2016 AFS of the Municipality of the Hani i Elezit has resulted in 15 recommendations. The Municipality had prepared an Action Plan stating how all given recommendations will be implemented. Our reported was discussed even in the Municipal Assembly.

Until the end of out 2017 audit, four recommendations have been implemented, seven were in process and four have not been addressed yet. Further on, from the 2015, seven recommendations were carried forward, and within the 2017 four of them were implemented, two were in process and one was not addressed. For a more thorough description of the recommendations and how they are addressed, see Annex II.

Issue 6 – Low level of implementation of recommendations from the previous and earlier year

Finding Due to the poor management of the process and the lack of a formal monitoring of how AG’s recommendations have been implemented, only a part of previous year’s recommendations and those previously carried forward have been implemented. This indicates a lack of concentration of the responsible persons in application of specific measures regarding their implementation that come as a result of identified weaknesses. We have not noticed that the Municipality applies responsibility measures for non-implementation of the recommendations.

Risk Failure to fully implement the recommendations increases the risk of continuous presence of same deficiencies and can result in continuous inefficiency of controls, difficulty in management of challenges on fulfilling objectives or even in financial losses.

Recommendation 6 The Mayor should ensure that the implementation of the action plan is continuously monitored and reported on a monthly or quarterly basis in relation to the progress achieved in this direction. The recommendations which are not implemented according to the timeframes, to be reviewed in a short timeframe by the Mayor, and proactive actions to be taken against the presented barriers during the implementation.

5 Good Governance

Introduction

Good Governance implies basic principles of accountability, effectiveness of controls, risk management, independence of internal audit, coordination of NAO with internal audit and good governance with public assets.

A key indicator supporting effective governance is the implementation of audit recommendations as this demonstrates that Management are seeking to develop existing processes and controls. The level of compliance with FMC requirements by Budget Organizations is monitored by the completion of the self-assessment checklists completed by all BOs, which are submitted at the end of the year to the Ministry of Finance.

Specific areas of our governance-related reviews have been the accountability and risk management process, while the other components are handled within the chapters or subchapters above.

Overall Governance Conclusion

There are a number of governance weaknesses within the Municipality, particularly related to accountability, risk management and the quality of management reporting.

One of the key elements of an effective governance of the Municipality is also the implementations of given recommendations by the external audit. The effective response to the implementation of the recommendations is unsatisfactory. This part has been more detailed handled to the chapter "Progress in implementation of recommendations".

The self-assessment questionnaire, completed by the Municipality, presents this situation only partially, by responding to the most of questions with average grade of 2.69. According to the questionnaire, the Municipality had given a negative response in seven questions from 106 total questions. The questions that relate with the assets recording were evaluated with maximum grade, while during the audit we have noticed that the non-financial assets registers are incomplete. This means that the Management should take into account the issues which have not reached the expected level.

The Municipality has the 2010-2025 Municipal Development Plan, also during the 2017 has approved the 2018-2022 Social Economic Development Strategy.

5.1 Internal Audit System

According to the Administrative Instruction no. 23/2009 on Establishing and Functioning of the Internal Audit Units in the Public Sector, each public subject with budget of 1 up to 3 million should have an internal auditor.

Issue 7 – The lack of the IAU establishment

Finding The Municipality still had not secured the IAU establishment. According to the AI 23/2009 on Establishing and Operating of IAU in the Public Sector, article 3, point 2.1, it determines that the public sector with budget 1 up to 3 million should have an internal auditor. However, during 2017 they have secured an Internal Audit from the Ministry of Finance.

Risk The lack of an internal Audit can result with continuous repetition of weaknesses in key internal control systems. Furthermore, the management may not timely identify and respond to irregularities and control weaknesses.

Recommendation 7 The Mayor should ensure that the legal requirement is met, respectively to recruit one internal auditor. If this requirement cannot be executed, then the internal audit service should continue to be performed by the Ministry of Finance, or any other public entity. The audit service would support the Management in decision-making and elimination of weaknesses.

5.2 Management Reporting, Accountability and Risk Management

In order to have a proper planning, supervise the activities on a regular basis and allow effective decision-making, the Management needs to have regular reports. Accountability as a process is the acceptance of responsibilities, holding persons into account for their actions and disclosing results in a transparent way. Whereas, risk management is a process related to identification, analysis, evaluation and actions/measures taken by the Management to control and respond to risks threatening the Organization.

Although, a range of internal controls are applied by Management to ensure that systems and operate as intended, we have noticed that the measures applied are weak and ineffective and therefore do not provide an effective and timely response to the identified operational problems.

Issue 8 – Weaknesses in management controls and risk management

Finding As a result of poor management controls, and late approval of the budget review by the Government, a part of the capital investments budget has remained unspent. Despite this, the Municipality had no proper mechanisms for the management of receivables. As a result, those are increasing year after year.

The Municipality also has no written policies and procedures for managing risks, in particular the risk of fraud and irregularities. They have started with the drafting of the risks register from some directorates, but have not been completed as a process. Further on, the Municipality has no risk management strategy.

Risk Poor accountability requirements and poor quality financial reporting reduces the effectiveness of financial management. This results in weaknesses in the budget process and reduces Management’s ability to respond to financial challenges in time. Further on, it also reduces the effect of budget controls and increases the risk of improper spending. Consequently, this may also result in providing poor quality services.

Recommendation 8 The Mayor should ensure that a review has been carried through to determine the form of financial and operational reporting to Senior Management. Budgetary performances, including revenues and expenditures, and procurement plan should be subject to regular reporting and review by the Management. Further on, in order to reduce the impact of risks to acceptable levels, the Organization should draft a risk register with all appropriate measures/actions to put the exposed threats under control.

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

Annex I: 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 emphasized 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 emphasized.

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 judgment, is relevant to users’ understanding of the audit, the auditor’s responsibilities or the auditor’s report, and provided this is not prohibited by law or regulation, this should be done in a paragraph with the heading “Other Matter,” or another appropriate heading. This paragraph should appear immediately after the opinion and any Emphasis of Matter paragraph.

Annex II: Progress in implementing recommendations of previous two years

Audit Component	Recommendations carried forward from 2015	Implemented during 2017	Under implementation during 2017	Not implemented
1.4 Compliance with AFS and other reporting requirements	The Mayor should ensure that an analysis is undertaken to determine the causes that led to Emphasis of Matter. It is necessary to undertake to be undertaken appropriate actions to address the causes behind non-recording of assets in the KFMIS and correct presentation of assets in the AFS.			No measures taken.
2.5.1 Risk assessment	The Mayor should ensure that, after having drafted the list of risks with respective levels, immediate responsibility for risk management is delegated to a named director who, in cooperation with the heads of units, will manage and regularly report on the progress of the process.		Some directorates have started with the preparation of risks registers, but still the Municipality does not have a complete risks register.	
2.6 Internal Audit System	The Mayor has to consider the possibility of obtaining internal audit services, in order to test appropriateness, effectiveness and functioning of organization's internal controls.	Yes.		
3.3 Budget Planning and Execution	The Mayor should ensure that budget performance is systematically monitored and that barriers to planned levels of budget execution are identified and addressed.		The level of budget expenditures was high in all categories, except the capital investments category.	

3.4 Procurement	The Mayor should initiate a thorough analysis in order to determine why weak procurement practices were applied in these cases and enhance controls, which ensure that: procurements reflect needs; tender specifications reflect current requests of departments. In general, the procurement controls need to be strengthened.	Yes.		
3.4.1 Remunerations (Wages and Salaries)	The Mayor has to review the internal regulation applied so far by the municipality, and correct the same in accordance with organic regulations and apply it adequately in order not to damage the municipal budget.	Yes.		
3.5.3 Handling of debts	The Mayor should ensure full reporting of liabilities and strengthen controls and discipline of officials responsible for forwarding of outstanding invoices to the finance department. For handling of contingent liabilities in coordination with the municipal legal representative should undertake a review of the condition of liabilities, in order to determine the priority of payments, by avoiding direct payments from the MoF.	Yes.		
Audit Component	Recommendations given in 2016	Implemented	In process of implementation	Not implemented
1.3 Annual Financial Statements	The Mayor should ensure that an analysis is undertaken to determine the causes of Opinion with Emphasis of Matter, and to take adequate actions to eliminate errors in misclassification of expenditures and incorrect recording of assets. In addition, to ensure establishment of effective processes in order to confirm that the plan for drafting AFS for 2017 addresses all issues raised in the report, and the Declaration made by the Chief Administrative and Financial Officer should not be submitted unless all necessary checks have been applied to the draft AFS.			No measures taken.

2.1 Implementation of Prior Year Recommendations	The Mayor should ensure application of a strengthened accountability process by the responsible staff on implementation of recommendations in line with timeframes and priorities set out under the action plan. Monitoring of implementation progress should be done in a systematic manner, in order to eliminate barriers during the process.		The Municipality has prepared an action plan for the implementation of recommendations, but the level of implementing the recommendations was high.	
2.2 Self- Assessment Checklist	The Mayor should ensure drafting of a comprehensive development strategy by including stakeholders and calculating costs for its implementation, and the list of risks is completed with measures that need to be taken in order to minimize the damage in case of risk occurrence.		Some directorates have started with the preparation of risks registers, but still the Municipality does not have a complete risks register.	
2.3.1 Strategic Plans	The Mayor should approve an overall strategic plan for the Municipality that would establish long-term objectives and serve as an orientation platform to draft annual plans, conduct comparative analysis between years and measure results against objectives.	Yes.		
2.3.2 Management Reporting and Accountability	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 by the end of 2017.		Although reports about management controls were not missing, reports of the physical and operational progress should be further improved.	
2.4 Internal Audit System	The Mayor should review budget possibilities to establish the IAU, which would contribute more to the assessment, and improvement of internal controls, alternatively, to continue obtaining annual services by the MF or another municipality that is nearby.			No measures taken.

3.1 Budget Planning and Execution	The Mayor should ensure and establish clear objectives for improvement of planning and budget execution in future periods, and establish a systematic monitoring over the planned budget execution, particularly for capital projects.		The level of budget expenditures was high in all categories, except the capital investments category.	
3.1.1 Revenues	The Mayor should uncover the reasons why purchased software has remained passive for many years, and ensure that it will be operational so that the database provides sufficient information on each business or seek an improvement to the existing format of record-keeping in Excel. In addition, should demand concrete actions from competent bodies to stop those businesses that have not met liabilities towards the Municipality.		The Municipality has improved the receivables reporting, but has not created proper mechanisms for their collection.	
	The Mayor should review abovementioned cases of debt forgiveness and ensure that debts are forgiven only for the categories permitted under applicable laws and regulations. Prior to making decisions, cases should be reviewed in advance and ensure that decisions taken are in full compliance with relevant laws or regulations.	Yes.		
3.1.2 Wages and Salaries	The Mayor should strengthen controls over the processing of personnel data in the payroll system, and ensure that are taken necessary actions for correct categorization of employees in line with adequate classification of salary grades.	Yes.		
3.1.5 Capital Investments	The Mayor should ensure that procurement office gathers all requests for the same purchase in order to enable development of open procurement procedures. This would enable greater competition and more favorable prices for the municipal budget.	Yes.		

3.2.1 Capital and Non Capital Assets	The Mayor should ensure that the respective inventory committee accelerates and complete the work started before and will submit the final report of the recording results. Otherwise, to establish a new committee.		During 2017 was done the inventory only for the Municipality facility inventory and the culture house and partially the MFMC, and not in the education facilities.	
3.2.2 Handling of Cash and Cash Equivalentents	The Mayor should ensure that this practice is stopped and implemented requirement of financial regulations, so that all cash collected, is deposited into the bank within legal deadlines.			No measures taken.
3.2.3 Receivables	The Mayor should ensure a comprehensive approach in treating receivables. The management should initiate a reassessment process where all accounts will be analyzed in terms of age, significant amounts, and real opportunities for collection, and exercise administrative measures for their collection.			No measures taken.
3.3 Outstanding Liabilities	The Mayor should ensure that there is a fair and timely reporting of all outstanding invoices from all departments, and to ensure that budget planning is based on a clear cash flow plan, so that budget appropriations are not exceeded by any means.		There is a good liabilities reporting, however those have been increased in relation to previous year.	

Annex III: Letter of confirmation



Republika e Kosovës
Republic of Kosovo



Komuna Hani i Elezit
Municipality of Hani i Elezit

DALËSE - IZLAZNA - OUTGOING
REPUBLIKA E KOSOVËS - REPUBLIKA KOSOVA, REPUBLIC OF KOSOVA
QEVERIA - VLADA - GOVERNMENT
KOMUNA HANI I ELEZIT, OPSTINA HANI I ELEZIT, MUNICIPALITY HANI I ELEZIT
Nr.1 Fide: 12333 Data: 19.06.2018
HANI I ELEZIT

LETËR E KONFIRMIMIT

Për pajtueshmërinë me të gjeturat e Auditorit të Përgjithshëm në Raportin e auditimit për vitin 2017 dhe për zbatimin e rekomandimeve

Për: Zyrën Kombëtare të Auditimit

Të nderuar,

Përmes kësaj shkrese, konfirmoj se:

- kam pranuar draft raportin e Zyrës Kombëtare të Auditimit për auditimin e Raportit/Pasqyrave Financiare të Komunës së Hanit të Elezit, për vitin e përfunduar më 31 dhjetor 2017 (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 zbatimin e rekomandimeve, i cili do të përfshijë afatet kohore dhe stafin përgjegjës për implementimin e tyre.

 z. Rufki Suma

Kryetar i Komunës,

Data: 19 Qershor.2018, Hani i Elezit,

