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NACIONALNA KANCELARIJA REVIZIJE**

NATIONAL AUDIT OFFICE

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AUDIT REPORT
ON THE ANNUAL FINANCIAL REPORT
OF THE MINISTRY OF ENVIRONMENT SPATIAL PLANNING
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 Ministry of Environment Spatial Planning in consultation with the Assistant Auditor General, Valbon Bytyqi who supervised the audit.

The opinion and report issued are a result of the audit carried out by Valbona Tolaj (Team Leader), Hysen Boqolli and Abdurrahmon Berbatovci (team members) under the management of the Audit Director (Bujar Sejdiu).

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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 Ministry of Environment Spatial Planning, 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 13/12/2016.

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



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 Ministry of Environment Spatial Planning.

Opinion of the Auditor General

Unmodified Opinion with Emphasis of Matter

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

We would like to draw your attention to the fact that disclosures of non-financial assets and outstanding liabilities are not fully reliable and accurate. Our opinion is not modified for this issue.

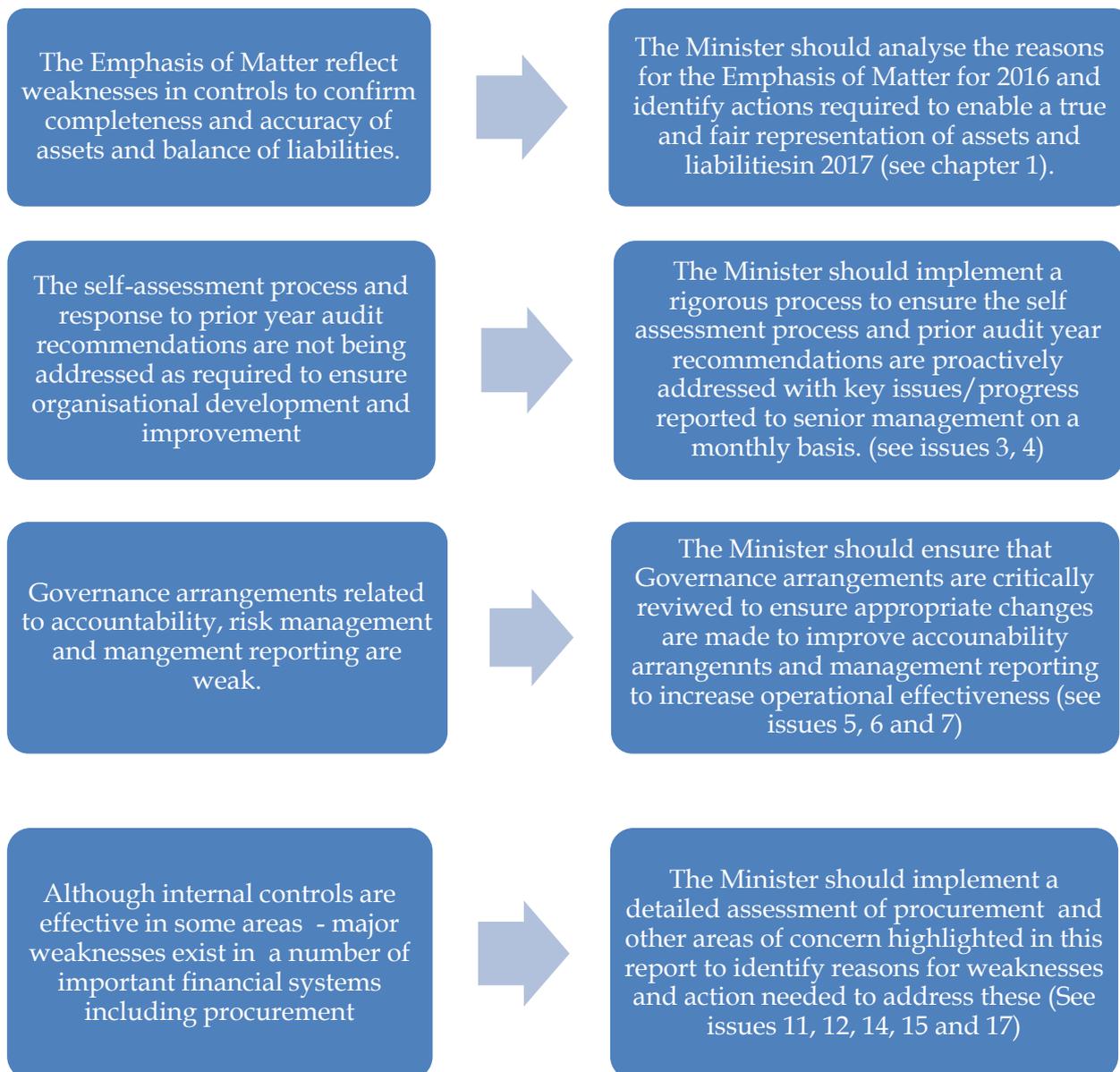
For more, please refer to Section 1.2 of this report.

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.

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

Key Conclusions and Recommendations



Minister's response

The Minister has considered and agreed on detailed audit findings and conclusions and agreed to address all recommendations given.

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 Government.

The declaration regarding presentation of the AFS incorporates a number of assertions relating to compliance with the reporting framework and the quality of information within the 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 Ministry of Environment Spatial Planning for the year ended on 31st of December 2016 which comprise of the Statement of Cash Receipts and Payments, Budget Execution Statement and the Explanatory Notes of the Financial Statements.

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

Basis for the opinion

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

Emphasis of Matter

We draw your attention to the fact that disclosures of non-financial assets and outstanding liabilities are not fully reliable and accurate, such as:

- Assets in the amount of €1,758,177 related to the project for houses of repatriated persons have not been removed from the assets register, even after the houses have been handed over to beneficiaries. This was because of the MESP uncertainty on how to handle/account for such cases in line with the Regulation on assets management;
- The Ministry does not yet have a complete register of all its water properties (as defined under the Law on Waters of Kosovo No. 04/L-147); and
- The Liabilities of the Ministry were undervalued by €5,755,440, as was not disclosed the liability on expropriation based on Government's Decision no. 06/104. However, this was reported in regular reports on liabilities for 2017.

This reflects lack of an effective system of controls on assets management and handling of liabilities (payables). Our opinion has not been modified (or qualified) on these issues.

Responsibility of Management and Those Charged with Governance and AFS

The Secretary General of the Ministry of Environment Spatial Planning 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 Minister is responsible to ensure oversight of Ministry'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

Ministry 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;
- Progress reports on capital projects with value of €10,000; and
- Draft and final procurement plan in time.

The issues raised in the Audit Memorandum dated 13/12/2016 regarding the reporting framework have been partially addressed by the Management.

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

- In the Budget Execution Report, entry of cash flow to the Treasury account, the final budget for designated donor grants (Note 12) was undervalued by €1,733,557. On the other hand, the borrowed amount of €782,000 (Note 13) was reported in the initial and final budget and in the execution, thereby overvaluing for the entire amount. Receipts/returns of borrowings are managed and recorded by the Ministry of Finance;
- Values recorded in the KFMIS for trust deposits are not reconciled with the value of funds in the bank account; and
- Annexes on stocks and assets under €1,000 were not attached to the AFS.

The findings above show that preparation of draft AFS was poorly managed. In the final AFS, the Ministry has adjusted the errors presented in the first bullet point.

Given the above, the Declaration made by the Chief Administrative Officer and Chief Financial Officer upon submitting drafts to the Ministry of Finance can be considered correct, although some errors have been identified which have been disclosed in the audit opinion under subchapter 1.2.

In the context of other external reporting requirements, we have identified the following incompliances:

- Quarterly reports on capital projects were not submitted within the timeframe to the Ministry of Finance. In addition, the quality of reports was not at the required level; and
- MESP in the final procurement plan had included contracts that were signed before 2016. This was due to the aim to report on the values of contracts to be executed in the current year. Furthermore, the prior notification for contracts was done with a delay on 30/06/2016.

1.3 Recommendations for the first part of the report

For two abovementioned issues we give the following recommendations:

Recommendation 1 The Minister should ensure that an analysis is undertaken to determine the causes of emphasis of matter. Actions should be taken to address the underlying causes in a systematic and pragmatic manner to remove errors in the reporting of liabilities and to ensure correct valuation of capital assets.

Recommendation 2 The Minister should ensure that effective processes are in place to confirm that the 2016 AFS production plan addresses all compliance issues, timeframe and the quality. This also should include Management review of the draft AFS, with specific focus on high risk areas and/or areas where errors have been identified in previous years. The Declaration made by the Chief Administrative Officer and Chief Financial Officer should be submitted only after a detailed review of AFS by the management.

2 Governance

Introduction

Effective governance arrangements are fundamental to MESP 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. We have therefore applied a consistent approach across all audits to determine the quality of the completed self-assessment checklists and to assess the accuracy of the picture being presented on Governance in Kosovo.

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 MESP particularly related to accountability, risk management and the quality of management reporting. The self-assessment checklist completed by MESP only partially recognises this situation with some positive comments about existing arrangements not evidence based. Other arrangements which would support the development of governance such as an effective response to audit recommendations of the Auditor General (AG), establishment of objectives and risk management are not fully in place.

2.1 Progress in the Implementation of Prior Year Recommendations

Our Audit Report on the 2014 AFS of MESP resulted in 21 key recommendations. The Ministry had prepared an Action Plan stating how all recommendations will be addressed.

At the end of our 2016 audit, six recommendations have been implemented, eight (8) are in the process of implementation; and seven (7) have not been implemented yet. For a more thorough description of the recommendations and how they are addressed, see Annex III.

Issue 3 - Addressing Prior Year Audit Recommendations - High Priority

Finding Only a proportion of prior year recommendations have been implemented because MESP has not implemented any formal process to manage and monitor the way that the AG's recommendations are implemented.

Risk The continued weakness of management and other controls in key financial systems have resulted in weaknesses upon execution of payments, and low efficiency upon implementation of capital projects and operational activities.

Recommendation 3 The Minister should ensure that a revised action plan is implemented which clearly sets out a timetable for addressing the recommendations made by the AG with accountable staff members identified and with initial focus on those of greatest significance. A systematic monitoring is required by the management to ensure effective implementation of recommendations and within the timeframe specified.

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. For all audits, we undertook we have tested the quality of FMC self-assessment submissions made to the Ministry by assessing one key question in each component of the checklist. We have summarised our findings for MESP below and the summary of our work across all audits will be consolidated in our Annual Audit Report. This is not intended to give a commentary on the quality of the whole self-assessment questionnaire submission but will provide a 'snapshot' across a number of key questions to support the Ministry of Finance in its attempts to increase the effectiveness of the process and develop the FMC system as a whole.

Issue 4 – Self Assessment Checklist – High Priority

Finding As part of our audit we have considered only key questions related to the five (5) components of the self-assessment checklist. The checklist was completed and reflects the overall situation in the Ministry. While the Ministry has made progress in the self-assessment arrangements, for the questions considered we found that:

1. The Self-Assessment questionnaire completed by MESP acknowledged that required risk management systems were not yet in place. Despite the prior year recommendations, the risks register has not been drafted. This reflects lack of allocation of responsibility on risk management.
2. Effective monitoring processes and Comprehensive strategy development are considered partially in place by MESP but the evidence supporting these conclusions is poor. Monitoring issues are also considered further in section 2.3.1; and
3. Links between the procurement plan and budget and the production of adequate reports on a timely basis are not considered in place by MESP.

This situation has occurred because of a lack of clarity within MESP regarding both the importance of this checklist and who is the responsible officer for using it to support operational improvements.

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

Recommendation 4 The Minister should ensure that a review of the processes for completing the self-assessment checklist and proactively addressing areas of weaknesses is implemented. A revised mechanism to confirm the accuracy of the return and to ensure supporting documentation supports the submission should be applied.

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 MESP operates and the challenges that it faces.

2.3.1 Management Reporting and Accountability

The Management has implemented a range of internal controls 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.

MESP has two subsidiary Agencies: The Kosovo Cadastral Agency and Kosovo Environmental Protection Agency (KEPA). To ensure an effective financial management and reporting is required a qualitative and timely consolidation process.

Issue 5 – Weaknesses in High Level Management Controls – High Priority

Finding	Our review of the management controls applied to MESP’s key financial system highlighted inadequate financial reporting of expenditure and revenue to senior management and an incomplete analysis of service delivery. This is because the format of management reports does not provide explanations for variances against budget execution and budget forecasts are not updated on a monthly basis. Similarly, operational targets are not systematically managed.
Risk	Poor quality of financial and activity reporting to senior management has reduced the management’s ability to proactively manage the operations of MESP and undermines effective budgetary control. This can result in unplanned over or under spending and delay necessary actions to address these. It may also result in revenues not collected as expected. Similarly, it may result in poor quality service delivery.
Recommendation 5	The Minister 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 1 October 2017.

Issue 6 - Accountability Processes - High Priority

- Finding** The MESP is responsible for a number of activities in key areas in protection of environment, water, regulation and development of spatial planning, cadastre and expropriation at the national level. The MESP addresses these activities through its two agencies. They have their own management structure, while KCA even produces its own AFS. Due to the fact that reporting responsibilities between the MESP and its Executive Agencies are not clearly defined and effectively applied, has resulted in poor accountability and consolidation of information and financial reports. As a result of these weaknesses in March 2016, the Chief Executive Officer of KEPA without a formal decision of the Minister had decentralised procurement and certification of payments, despite the fact that this decentralisation was not foreseen under the organisational structure of the Ministry.
- Risk** Weak accountability requirements and poor quality financial reporting have reduced the effectiveness of financial management within MESP. This results in weaknesses in the budget process and reduces the ability of management to react to financial challenges on a timely basis. There is also an increased risk of irregular expenditure.
- Recommendation 6** The Minister should ensure that a review of existing accountability arrangements and reporting requirements placed on Executive Agencies is implemented with enhanced arrangements to achieve the set specified objectives by 1 October 2017. All changes to the Organisational Structure should be done under formal processes and approvals requested.

2.4 Internal Audit System

The Internal Audit Unit (IAU) operates with three members of staff - the Head of IAU and two auditors. An effective audit requires a comprehensive work programme that reflects financial and other risks to MESP and provides sufficient assurance over the effectiveness of internal control. The impact of IA output should be judged by the importance that management places on addressing recommendations and the support and challenge provided by an effective Audit Committee.

During 2016, the IAU managed to complete five out of six audits planned. Two additional audits were carried out at the request of the management. Two audits covered the period 2015, two others the period 2015/2016 and three (3) year 2016.

Issue 7 - Weaknesses in the IAU system - High Priority

Finding

A number of weaknesses exist related to current IAU operations:

- For one (1) internal audit report, the action plan on implementation of recommendations was not prepared;
- Only 43 out of 62 recommendations given by the IAU were fully implemented by the management; and
- There is a significant difference between the salaries of internal auditors. One auditor is paid with a multiplier 16 and the other with multiplier 7.

Risk

Weaknesses identified in the internal audit system result in weaknesses in controls not being identified and addressed thus resulting in operational inefficiency and financial loss to MESP. Failure to address recommendations will exacerbate this situation.

Recommendation 7

The Minister should ensure effective communication with the Audit Committee to gain maximum benefit from Internal Audit activity. The Audit Committee should critically review internal audit plans (to confirm that they are risk based and provide the required assurance to management), internal audit outputs and the reason behind such difference between internal auditors salaries. It should also review actions taken by management on audit recommendations.

3 Financial Management and Control

Introduction

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

Financial Management and Control Conclusion

The major concern of MESP remains Procurement as this is directly linked to the old projects that have been going on for a long time and are not completed yet. In the context of financial systems, controls over revenues are generally operational, including the fact that the department of waters is having challenges in collecting revenues despite the new secondary legislation. Controls over a range of expenditure areas require further enhancement to prevent MESP from suffering financial losses or poor value for money. The main areas where most improvements are required are the procurement process and expropriations.

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	0	0	609,575	686,399	616,742
Total	0	0	609,575	686,399	616,742

Own source revenues of €609,575 were transferred to the Kosovo Budget (KB). The total of revenues collected is smaller by 13% (€76,823) compared to those of prior year. This decrease is as a result of fluctuations of requests for permits or environmental consents by businesses and individuals.

Table 2. Sources of budgetary Funds (in €)

Description	Initial Budget	Final Budget ²	2016 Outturn	2015 Outturn	2014 Outturn
Sources of Funds	39,173,728	39,392,076	38,172,422	38,126,445	44,967,147
Government Grant -Budget	38,454,728	36,318,333	36,157,798	35,781,311	42,501,820
Borrowings	719,000	782,000	720,076	1,756,619	1,945,368
External Donations		2,291,743	1,294,548	588,515	519,960

The final budget is higher than the initial budget by €218,348. This increase is a result of budget movements due to External Donations, budget review and Government decisions.

MESP used 97% of the final budget in 2016 or €38,172,422, an improvement of 2% compared to 2015.

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	39,173,728	39,392,076	38,172,422	38,126,445	44,967,147
Wages and Salaries	2,138,187	2,077,548	1,984,177	1,817,788	1,613,389
Goods and Services	1,118,081	1,923,072	1,358,734	1,510,329	1,607,834
Utilities	83,220	55,504	40,974	41,702	48,063
Subsidies and Transfers	190,000	0	0	-	-
Capital Investments	35,644,240	35,335,952	34,788,537	34,756,626	41,697,861

Explanations for changes in budget categories are given below:

- The budget for Wages and Salaries had decreased by €69,639 as budget savings. This has occurred because the approved staff number was 335, while the staff number during the year was 317 (18 less);
- The budget for Goods and Services had increased by €804,991. Initially, it had increased as a result of donations by €990,484, and transfers and subsidies by €25,000. While on the other hand, under the budget review process it was reduced by €76,145 and under Government Decisions by €134,348;
- The budget for subsidies and transfers was initially reduced due to a transfer of €25,000 to the category of Goods and Services, and at the end, the entire remaining budget was reduced by a Government Decision; and

² Final budget - the budget approved by the assembly which was subsequently adjusted for by the Ministry of Finance.

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- The budget for capital investments was reduced by €308,288. Initially, it was increased by €2,341,364 (as a result of donations €1,352,115, and with the budget review €259,444, and with Government Decisions €729,805), but at the end of the year it had suffered budget cuts with Government Decision by €2,586,652 which were transferred to another category of expenditures €63,000.

Funds received by donors in the amount of €2,291,743 were allocated to different categories of expenses.

Issue 8 – Budget Execution – Medium Priority

Finding Even though budget execution had reached 97%, the process of budget management during the year was not administered effectively, particularly considering the liabilities reported at the end of the year. A very low budget execution was presented at the budget from donations where only 56% of the funds were spent. This was because one donation was received on 15/12/2016.

Risk Inadequate budget planning and a low budget execution level will result in a failure to meet organisational objectives. The low level of spending of funds from donors can result in reduction of donations in the future.

Recommendation 8 The Minister should ensure that budget performance is systematically monitored on a monthly basis and that this review identifies and addresses barriers to planned levels of budget execution. Where initial budget assumptions are found to be incorrect this should be fully reflected in the final budget position and in planning of future years.

3.1.1 Revenues

Revenues generated by MESP in 2016 totalled €609,575. These relate to licenses and different services provided by this Ministry mainly through the Department of Waters (DW), Department for Environment Protection (DEP), Department of Housing (DSPCH) and KCA.

Issue 9 – Weaknesses upon management of revenues – Medium Priority

Finding Our audit of revenues management system identified that revenues from sales and sanitisation of public forests as well as licenses for environmental consents and water permits are all recorded in a single economic code (50201 - Licenses for individual and free activities). This has occurred due to lack of codes in the KFMIS.

Risk Recording of different revenues in a single economic code shows inaccurate presentation of revenues and makes management's monitoring and decision-making difficult.

Recommendation 9 The Minister should strengthen controls over revenues management in order to ensure that all revenue are recorded in adequate codes of KFMIS and fully in compliance with the Chart of Accounts and Financial Rule no.03/2010 on Revenues.

3.1.2 Wages and Salaries

Wages and Salaries are paid through a centralised system. The key controls that operate at the Ministry's level are: authorisation of the payroll, changes to the payroll list, and reflection of changes occurred.

Unimplemented recommendations from the previous year are detailed in Annex III of this report.

Recommendations

We have no recommendations in this area.

3.1.3 Goods and Services and Utilities

The final budget of Goods and Services in 2016 was €1,923,072, out of which €1,984,177 were spent. Those relate mainly to operational expenses such as travelling, rent, goods and services, and utilities.

Issue 10 - Disagreement with the tax law - Medium Priority

Finding The law stipulates that the employer, in this case the MESP, should withhold source tax on personal income for professional payments and services. Our testing has identified that the MESP had not withheld the source tax and the pension contribution for professional services, although the value of payments for these services during 2016 was €33,159. This was due to delayed receipt of the notice to change legislative requirements.

Risk Failure to withhold tax and pension contributions leads to disagreements with the law and financial losses for the Kosovo Budget.

Recommendation 10 The Minister should ensure that all legal requirements for personal income tax are implemented in full compliance with the Law, so that MESP obligations as an employer are fulfilled.

Issue 11 - Weaknesses in Procurement for Goods and Services - Medium Priority

Finding Our audit has identified that controls over procurement for goods and services in some cases have not been effective, due to which have resulted the following discrepancies:

- In the procurement process "Supply with toners" in the amount of €44,953, there was no decision on appointment of the Contract Manager whilst the decision on the Goods Receiving Commission was made in delay. Moreover, the received goods were not in line with the specification as they were not original but "compatible" which was excluded under the Tender Dossier; and
- In the contract "Written and simultaneous translation services" in the amount of €8,641 was required that the evidence on professional and technical abilities (diploma and court ruling as an interpreter) be original or notarised. We found that the Tender Dossier lacked these documents because, according to officials, the EO had withdrawn them for other reasons.

These findings emphasise the lack of a critical review of the tendering process results that would enable identification and adequate implementation of the procurement law.

Risk Weaknesses identified in the procurement process lead to disagreement with legal requirements and poor value for money spent, and can result in potentially improper spending.

Recommendation 11 The Minister should consider why the procurement requirements for goods and services have not been implemented, and to strengthen procurement controls to ensure full compliance with legal requirements and value for money spent.

3.1.4 Capital Investments

The final budget for capital investments was €35,335,952. Out of them in 2016 were spent €34,788,537 (98%). They mainly relate to capital expenditures for arrangement and maintenance of the environment as well as expropriation expenditures.

The management has established a control system for capital investments including the process of procurement and payments. Our tests have identified that these controls were not effective throughout the period. The identified weaknesses are presented below.

Issue 12 - Weaknesses in Procurement for Capital Investments - High Priority

Finding Our audit has identified weaknesses in procurement procedures such as:

- In the Tender Dossier “Stage III - Regulation of Drenica River and Verbovc-Drenas” in the amount of €689,926, the winning EO had not fully meet the criteria on technical and professional capacities regarding the submission of the list of employees (minimum 20) and copies of contracts to be identical to the original;
- In regard to the progress payment of €108,353 for the Project “Water supply of nine villages of Kačanik” funds of €10,835 (10% of the value of the progress payment) were not withheld as foreseen under the special terms of the contract; and
- Designing of the main concept paper for regulation of Drenica riverbed in Drenas - Second stage was accepted by the Project Coordinator, and not by a professional committee appointed by the Secretary General. Moreover, the master plan was drafted in delay.

Risk Awarding the contract to an Economic Operator that does not meet all the criteria results in disagreement with the law, unequal treatment of bidders, and in uncompleted contracted works. Failure to hold funds and projects accepted by a single official besides being in disagreement with law can result in poor quality of works and potential financial losses for the Ministry.

Recommendation 12 The Minister should review the design of controls over capital investments, and strengthen them to ensure full compliance with the legal requirements of procurement and payments. All projects should be accepted by professional committees and should be practised holding of funds in order to prevent low quality of works and potential financial losses.

Issue 13 - Planning and management of projects - Medium Priority

Finding Our audit has identified several weaknesses in planning and management of projects for 2016. Weaknesses identified were:

- For the project “Construction of the accumulating lake in Ibër River” in Mitrovica, the MESP had a contract in the amount of €2,848,212. Due to inadequate projections and unclear technical specifications, two annex contracts of €77,645 and €198,373 respectively were signed. For additional works in the same project, the MESP had signed another contract with another Operator in the amount of €948,639, and one annex contract in the total of €275,837. The signed annex contracts did not specify the value of the base contract. This was because of the specifics of the area where the project is planned on;
- For the project “The First Base of Illegality of KLA in Lladovc”, the Ministry had one contract for €999,621 and one annex contract in the amount of €94,359. For the same project were signed two additional works contracts in the amount of €19,840; and
- For the memorial complex “Battle of Koshare”, the Ministry had a contract in the amount of €411,867. For the same project an additional contract was signed for continuation of works in the amount of €177,304;

Risk Due to ineffective implementation of capital projects can result in failure to meet Ministry's annual and strategic objectives and makes it impossible to cover liabilities with current funds. Furthermore, these weaknesses can result in potentially improper payments and low value for money.

Recommendation 13 The Minister should ensure that planning of projects is subject to a real analysis of capacities of organisation for project management, in line with initial plans and legal requirements. Controls over planning and management of projects should be strengthened in order to overcome challenges identified so that Ministry's objectives are achieved within the timeframes and within budgets planned. A reconciliation of cash flow with planning of projects is necessary to address an adequate management of financial and physical progress of capital projects.

3.1.5 Payments for expropriation

The MESP is responsible for the process of property expropriation. Expropriation expenses are incurred from the budget of capital investments. The procedures for recording of expropriated properties are regulated by the Law No. 03/L-139 on Expropriation of Immovable Property (amended/supplemented by the Law No. 03/L-2015). All expropriation data such as assessment, compensation and recording of immovable property should be recorded in the Electronic System of Expropriation (ESE).

Our tests have identified that the expropriation process has been followed by various challenges due to ineffective controls over the cases presented in the following.

Issue 14 - Management of expropriation process - High Priority

Finding Weaknesses in the management of expropriation process are disclosed in the following:

- Even though the Secretary General had established a work group for drafting of an operational guideline for ESE, this guideline has not been finalised yet. Consequently, the expropriation process is still done manually (Excel). In addition, the Ministry does not have a formal procedure that regulates the internal functioning of the process and that ensures segregation of duties and responsibilities to officials;
 - In 11 out of 13 samples tested, we have found that expropriated parcels were not recorded in the Kosovo Cadastre Land Information System (KCLIS). In addition, a considerable number of cases that needed to be recorded were rejected by the Municipal Cadastral Offices because elaborations of expropriations were not completed in line with AI 18/2015; and
-

- Within the KCA was developed the project of Reconstruction of Cadastral Information in 20 cadastral zones. In four of these zones had started the expropriation process. Out of 1,724 expropriation cases that were processed by this project, for 1,224 (71%) were not met technical and legal requirements for recording due to errors in expropriation elaborates.

Risk Recording expropriation data in Excel forms and lack of procedure for this process poses a risk of errors and reduces the quality of data needed for recording and for Management. Moreover, the possibility of making changes without a trace (in Excel) and lack of recording can be subject to irresponsible changes and double compensations.

Recommendation 14 The Minister should consider the reasons why the Operational Guideline on use of ESE and on errors in expropriation elaborates so that are identified actions needed to address them. The Operational Guideline and procedures for the expropriation process should be finalised and implemented by October 1, 2017. At the same time, an action plan should be drafted to ensure that all errors in the expropriation process are eliminated and the same will be recorded in the System in order to prevent double compensations and Ministry's potential financial losses.

Issue 15 - Execution of expropriation payments - High Priority

Finding The Ministry had not managed to ensure controls over the management of payments' process. Weaknesses in their management have been disclosed in the following:

- The Ministry had executed a payment for the expropriation of a non-state property in the amount of €265,720 into a private account. This had occurred after the request and authorisation of the head of the institution that the payment be executed in the private account of one of the cashiers of this institution; and
- Due to delays by the Ministry in executing expropriation payments, the Treasury had executed payments based on court decisions and bailiffs in the amount of €1,793,057. Our tests have identified two cases where due to delays the Ministry had paid additional costs of €100,773 (for enforcement procedures €18,739, interest €79,668, and other administrative expenses €2,366).

Risk Paying funds into private accounts is in disagreement with financial rules and can result in improper expenses. Due to execution of payments by the Treasury and additional payments can result in reduction of funds for annual operations and in failure to achieve Ministry's objectives.

Recommendation 15 The Minister should strengthen controls related to execution of payments to ensure that all payments are executed in full compliance with applicable financial rules. Reasons for delays should be identified and addressed in order to prevent execution of payments from judicial/enforcement procedures that can result in additional costs for the Ministry.

3.1.6 Common Issues on Goods and Services and Capital Investments

In the following have been presented common issues that relate to Goods and Services and Capital Investments:

Issue 16 - Non-enforcement of penalties - Medium Priority

Finding Our tests have identified several cases when the Ministry had not implemented penalties towards Economic Operators who were late in completing works. Cases identified were:

- In the contract, "Construction of the Accumulating Lake on the Ibër" in the amount of €2,848,212, up to the stage XVII there was a delay of 654 work days. The amount of penalties not imposed (5/1000 days and maximum 10% of the contract value) in this case it reached €284,821; and
- In the contract, "Drafting of Annex to Elaborate on Expropriation of Properties for Construction Needs of the Memorial 'Base I'" in the amount of €4,453 had a delay of 130 days. The amount of penalties not imposed reached €445.

Risk Failure to apply penalties over delays in execution of works results in continuous delays in achievement of Ministry's established plans. Moreover, in addition to being disagreement with the law, these cases motivate Operators for other delays and cause financial losses to the Kosovo Budget.

Recommendation 16 The Minister should strengthen financial and procurement controls over contracts, namely to adhere to deadlines. In case of delays, all penalties should be applied in full compliance with the conditions of the contract.

Issue 17 - Receiving of supplies - High Priority

Finding In two cases we have identified that there were no adequate controls over the supplies received. These are disclosed as follows:

- The supplying of computer equipment supplies in the amount of €472,255 out of the World Bank Grant was done only by the Receiving Officer and not by the Receiving Committee appointed by the Chief Executive Officer of KCA; and

- In the supply with toners in the amount of €1,220 was missing the committee as foreseen under the Financial Regulation 01/2013/MoF – on Spending of Public Funds.

Risk Supplies being receiving by only one person and lack of an acceptance report are in disagreement with financial rules and can result in inadequate quality/quantity and in low value for money. Payments under these circumstances can result in improper expenses.

Recommendation 17 The Minister should ensure that all goods and services are received by committees appointed by the management, in order to confirm the appropriate amount and the quality against the value for money, and to ensure full compliance with requirements of financial rules.

3.2 Assets

3.2.1 Capital and Non Capital Assets

Capital assets represent assets over €1,000 while non-capital are assets under €1,000. The net assets value in the AFS for 2016 is €192,069,275. A proper assets management system requires a clear definition of duties on their recording, comparing, reporting and disclosure in the financial statements.

While issues related to the reported value of assets have been handled in sub-Chapter 1.2 of this report, other issues have been presented below.

Issue 18 - Asset Use - Medium Priority

Finding Our audit has identified some incompatibilities related to the use of assets of the Ministry, which are presented below:

- Some of the officials whose mandate has expired had not returned the property of the Ministry with which they were charged (laptops and digital cameras); and
- Officials of the Ministry used 11 official vehicles after the official working hours in disagreement with Minister's decision 12/2015 on Use of Vehicles outside working hours.

Risk Failure to return and/or use assets of the Ministry without relevant authorisations constitutes a violation of legal procedures and results in misuse, damage or loss of public assets.

Recommendation 18 The Minister should analyse the reasons why assets were not returned or used without appropriate authorisations. Controls should be strengthened to ensure full implementation of legal acts on use of assets. The Minister should initiate administrative and judicial procedures for unreturned assets and ensure that they are returned by October 1, 2017.

3.2.2 Receivables

The value of Accounts Receivable in the AFS of 2016 was €986,055, which indicates an increase of these Accounts by €28,217 compared to the previous period. These accounts derive from taxes that Economic Operators pay which are mainly water users. The Ministry has taken administrative and judicial actions to collect these accounts, but their collection remains a constant challenge.

Recommendations

We have no recommendations in this area.

3.3 Outstanding Liabilities

According to the AFS of 2016, the Ministry's liabilities at the end of the year were €150,038,276 or €4,038,276 more than in the previous period. The structure of liabilities comprises of: final expropriation decisions in the amount of €149,676,926, capital investments in the amount of €228,372, goods and services in the amount of €129,161, and utilities in the amount of €3,817.

The continuous increase of the value of liabilities presents a serious operational and budgetary challenge for the future periods of the Ministry. Undervaluing these liabilities in the AFS for 2016 has been addressed in audit opinion with emphasis of matter.

Recommendations

We have no recommendations in this area.

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 1.2 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 actions that the Minister should ensure are taken to address identified management/control weaknesses.

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

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

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

Findings considered low priority were reported separately to finance staff.

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
2. Financial Statements	The Minister should ensure that effective processes are in place to confirm that the 2016 AFS production plan formally addresses all compliance related issues			No measures taken
2.3 Prior Year Recommendations	The Minister should ensure that a revised action plan is implemented which clearly sets out a timetable for addressing the recommendations made by the AG with accountable staff members identified and with initial focus on those of greatest significance.		The MESP has shown dedication on implementation of recommendations. However their complete implementation remains a challenge.	
2.4 Self-Assessment Checklist	The Minister should ensure that a review of the processes for completing the self-assessment checklist and proactively addressing areas of weaknesses is implemented. A revised mechanism to confirm the accuracy of the return and to ensure supporting documentation supports the submission should be applied.		There is progress in the completion of the checklist but improvement is needed in some components.	No measures taken
2.5.1 Risk Assessment	The Minister should ensure that immediate responsibility for risk management is delegated to named officials and ensure monthly reporting on the implementation of requirements in this area and the risks that are being managed.			No measures taken
3.3 Budget Planning and Execution	The Minister should ensure that incurred expenditures are register in adequate categories in order to present fair occurred expenditures. Furthermore, during the budget planning to consider the budget requirements in the category of subsidies, in order to identify the exact expenditures.	Yes		

3.4 Procurement	The Minister should ensure that the rules on prior notification of contracts are applied with the purpose of advertising, transparency and fair competition in the process.		Prior notifications on planned procurement procedures were done, even though there were delays in these processes.	
3.4 Procurement	The Minister should ensure that the ministry received a construction permit prior of beginning any project, especially when it comes to the third category projects.			No measures taken
3.4 Procurement	The Minister should ensure a detailed review of why specific procurement requirements are not addressed for all procurement and identify appropriate measures to ensure that identified weaknesses are addressed effectively.	Yes		
3.4 Procurement	The Minister should ensure that approximate quantities are planned when signing contracts in which the price per unit is applicable. This would enable a comprehensive overview of expenditures associated with the contract.	Yes		
3.4 Procurement	The Minister should exercise additional controls to ensure that the procedures started on time and prior to beginning of each project to insure financial resources in accordance with the implementation of works dynamic plan.			No measures taken
3.4 Procurement	The Minister should ensure enhancement of financial controls over the registration of invoices into Balance to ensure the accurate data input in the system.	Yes		
3.5.2 Expropriation Payments	The Minister must ensure application of the current Expropriation Electronic System (EES) in a short period of time, in order to obtain higher security for the expropriation management process including expenditure realization for expropriation.		MESP has taken actions but EES is still not operational	

3.5.2 Expropriation Payments	The Minister should ensure that the compensation of expropriated properties is paid within deadlines in accordance with the law and relevant government decisions and their implementation is in chronological order based on party applications.		In some cases, the interest for delays in expropriation was applied. However, there are still challenges in this process	
3.5.3 Remunerations (Wages and Salaries)	The Minister should ensure implementation of the rules during the engagement process of employees for special services not to pass over six months and make efforts that for regular working positions the employees to be engaged through payroll. Should consider that for positions of engagement periods longer than three months and no legal obstacles to announce job vacancies by filling those positions with regular employees.			No measures taken
3.5.3 Remunerations (Wages and Salaries)	The Minister should ensure that an assessment of staffing needs across departments is provided and this is approved number by the regulations or budgetary requirements.		Under the regulation for internal organising of the MESP, the Office of Minister has nine staff members, while under the budget are specified 20.	
3.5.3 Remunerations (Wages and Salaries)	The Minister should ensure a more efficient management of future recruitment processes in order to address the delays in various stages of the process.	Yes		
3.6 Revenues (including own source revenues)	The Minister should consider the involvement of revenue planning by relevant units and ensure that budget revenue plans are based on previous achievements and experiences from past and seek effective accountability for their performance level		MESP has planned the revenues but there were weaknesses in the revenues management	

3.7.1 Capital and Non Capital Assets	Registering the renovations as organisation assets in facilities should only be made on the premises where the legal owner is the funding organization, otherwise the capitalization of these expenditures is impossible.			No measures taken
3.7.1 Capital and Non Capital Assets	The Minister should ensure that only assets documented as property owned by BO are registered by the assets official as assets of ministry, while the co-finances recorded as continues investment to be closed when the building is completed and delivered to beneficiaries for use.			No measures taken
3.7.3 Handling of Debts	The Minister should ensure that budget planning requirements are made in accordance with the requirements for expropriation and the compensation are made in chronological order, based on the application date and the corresponding deadlines. Also, we recommend the Ministry that together with the Ministry of Finance to consider possibility and potential of budget transfer for expropriation to the Ministry of Finance where budget limits are planned and the price is established for each individual expropriation. Conducting the budgeting planning, evaluation of properties and the payments processing from the same decision-making level could avoid existing obstacles in the process of expropriation. Among other things, it will enable more accurate planning of the budget toward real needs and would contribute on eventual handling of complaints regarding the evaluation of properties.		MESP has taken actions but the required outcome is still missing.	
3.7.3 Handling of Debts	The Minister should ensure that all controls on the data presented in AFS are functioning so that disclosed information are accurate and reliable.	Yes		

Annex IV: Letter of confirmation

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: 10.05.2017

Honoured,

We hereby confirm that:

- We have received the draft audit report of the National Audit Office on the 2016 Annual Financial Statements of Ministry of Environment and Spatial Planning, 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.

Secretary General:

Mr. Arben Citaku

Zyra e Sekretarit të Përgjithshëm/Kancelarija e Sekretarit të Përgjithshëm			
11.05.2017			
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Numri i regjistrimit Reg. No.	SP	Numri i Protokollit Prot. No.	2389/17
Numri i Dokumentit No. Dokumenti	01	Data e Miratimit Data	10.05.2017
Printime / g			

Republika e Kosovës
Republika Kosova - Republic of Kosovo
Qeveria - Vlada - Government

*Ministria e Mjedisit dhe Planifikimit Hapësinor
Ministarstvo Sredine i Prostornog Planiranja
Ministry of Environment and Spatial Planning*

Zyra e Sekretarit të Përgjithshëm/Kancelarija e Sekretarit të Përgjithshëm/Office of the Permanent Secretary

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

Të nderuar,

Përmes kësaj shkrese, konfirmoj se:

- kam pranuar draft raportin e Zyrës Kombëtare të Auditimit për auditimin e Pasqyrave Financiare të Ministrisë së Mjedisit dhe Planifikimit Hapësinor 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.

z. Arben Çitaku.....

Sekretar i Përgjithshëm

Data: 04/05/2017