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Republic of Kosovo



Zyra Kombëtare e Auditimit  
Nacionalna Kancelarija Revizije  
National Audit Office

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**AUDIT REPORT**  
**ON THE MUNICIPALITY OF RAHOVEC FOR**  
**THE YEAR ENDED 31 DECEMBER 2018**

**Pristina, May 2019**

The National Audit Office of the Republic of Kosovo is the highest institution of financial control, which for its work is accountable to the Assembly of Kosovo.

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

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.

This audit is carried out in line with internationally recognized public sector auditing standards and good European practices.

The Auditor General has decided on the audit opinion on the Annual Financial Statements of the Municipality of Rahovec in consultation with the Assistant Auditor General, Naser Arllati, who supervised the audit.

The report issued is a result of the audit carried out by Kapllan Muhaxheri (Team Leader) and Fetah Osmani, Fanol Hodolli and Arian Zenelaj (team members), under the management of the Head of Audit Department Luljeta Morina.

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## Executive Summary

This report summarises the key issues arising from our audit of the Municipality of Rahovec for 2018, which includes the Opinion of the Auditor General on Annual Financial Statements. Examination of 2018 financial statements was undertaken in accordance with the International Standards of Supreme Audit Institutions (ISSAIs). Our approach included tests and procedures that were necessary to arrive at an opinion on the financial statements. The applied audit approach is set out in the External Audit Plan dated 21/12/2018.

Our audit focus has been on:



The level of work undertaken to carry out the audit was determined depending on the quality of internal controls implemented by the Management of the Municipality.

### Opinion of the Auditor General

#### Unmodified Opinion with Emphasis of Matter

The Annual Financial Statements for 2018 *present a true and fair view* in all material aspects.

#### **Emphasis of Matter**

We draw your attention to the fact that the receivables for property tax in the amount of €53,515 and outstanding liabilities in the amount of €133,918 were not disclosed correctly in the annual financial statements. In addition, expenditures in the amount of €137,982 were misclassified, out of which €97,684 were budgeted and approved by the law on budget.

For more details, refer to Section 2.1 of this report.

Annex I explains different types of Opinions in line with ISSAIs.

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## Key Conclusions and Recommendations

Financial Statements - Emphasis of Matter reflect weaknesses in controls to confirm proper classification of expenditure and full disclosure of receivables and liabilities.



The Mayor should analyse reasons for Emphasis of Matter in 2018 and identify actions required for fair and true presentation of expenditure classification, receivables and liabilities for 2018 (see issue C1).

The AFS production contains a number of financial errors, lack of disclosures and uncertainties identified during the audit.



The Mayor should ensure that the 2019 AFS production process incorporates a formal and effective management review and the AFS declaration is not signed unless all necessary checks have been applied (see issue C1).

Budget planning and execution, procurement, non-procurement expenditures, management of receivables, payables, revenues, and management of personnel files are the areas that require further improvement.



The Mayor should apply a detailed assessment of procurement and other areas of concern highlighted in this report to identify reasons for weaknesses and action needed to address these (A1,A2,B1,A3,C2,C4,A12,A13 and A14).

Although internal controls operated effectively in some areas - evident weaknesses were noticed in a number of important financial systems including procurement.



The Mayor should carry out a detailed assessment of procurement and strengthen controls where failure in the process have been identified (See issues A4,A5,A6,A7,A8,C3,A9,A10 dhe A11).

The self-assessment process and response to prior year audit recommendations are not being addressed as required to ensure organisational development and improvement.



The Mayor should apply a rigorous process to ensure the self-assessment process and prior audit year recommendations are proactively addressed with key issues/progress reported to senior management on a monthly basis. (see issue B2).

Governance arrangements related to accountability, risk management and management reporting are poor. Internal Audit Activity does not support developments in these areas.



The Mayor should ensure that Governance arrangements are critically reviewed to ensure appropriate changes are made to improve accountability arrangements and management reporting to increase operational effectiveness supported by a more effective IAU (see issue C5).

## Management response to audit 2018

The Mayor agreed with the findings and conclusions of the audit, and has committed to address all the given recommendations. The National Audit Office evaluates the cooperation of the management and the staff of the Municipality during the audit process.

# 1 Audit Scope and Methodology

The Audit involves examination and evaluation of Financial Statements and other financial records, as follows:

- 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;
- Whether the internal controls and internal audit functions are appropriate and efficient; and
- Whether have been taken appropriate actions for implementation of audit recommendations.

Audit work undertaken is based on risk assessment. We have analysed the Municipality of Rahovec business, the level of reliance on management controls, in order to determine the level of detailed testing required to provide the necessary evidence and that support the opinion of the AG.

Our procedures have included a review of internal controls, accounting systems and related substantive tests, as well as 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 that may exist, or of all improvements that could be made to the systems and procedures operated.

The following sections provide a detailed summary of our audit findings and recommendations in each area of review. Management's responses to our findings can be found in Annex II.

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## 2 Annual Financial Statements and other External Reporting Obligations

Our audit of the Annual Financial Statements (AFS) considers both compliance with the reporting framework and the quality and accuracy of information presented in the AFS, including the declaration made by the Chief Administrative Officer and Chief Financial Officer.

The declaration on presentation of AFS includes a number of assertions relating to the compliance with the reporting framework and the quality of information within the AFS. These assertions intend to provide assurance to the Government 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 Rahovec for the year ended on 31<sup>st</sup> of December 2018, 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 31<sup>st</sup> of December 2018 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 by 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 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:

- The Municipality has not reconciled the final balance of the card of accounts receivable on property tax with the initial balances, therefore this account was underestimated by €53,515<sup>1</sup>

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<sup>1</sup>The initial balance of receivables was; €1,267,000, the Municipality billed €446,949 during the year and received incomes in the amount of €419,434, and the final balance should be €1,294,515. While the Municipality has disclosed the value of €1,241,000, underestimating receivables by €53,515.

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in the AFS. The Municipality failed to provide us with evidence to justify the presented difference; and

- The liabilities of 2017 in the amount of €122,516 from the category of capital investments and €11,402 from the category of goods and services paid in 2018 were not disclosed as outstanding liabilities under Article 17<sup>2</sup> of the AFS 2017. This account was understated by €133,918, so the initial balance of accounts payable for 2018 is incorrect.
- Expenditures for goods and services and salaries and wages in the amount of €113,456 were incorrectly executed and reported out of the capital investment category, out of this value the amount of €97,684 was budgeted and approved by the law on budget. These funds were mainly spent on contracts: seasonal maintenance of roads, demolition of illegal buildings, co-financing agreement. Further on, wages and salaries and subsidy expenditures were paid from the category of goods and services in the amount of €24,526<sup>3</sup>. According to the Municipality the reason for such misclassification was the lack of budget in the relevant categories, although for the majority of expenditures the budget was approved by the treasury but the project codes were misclassified. Additional causes were payments for court decisions and treasury, payments were made using free funds regardless of the nature and the correct classification of expenditure. Despite the presented justifications, according to public sector accounting standards these expenditures do not meet the criteria to be regarded as capital.

## Key Audit Matters

As key audit matters we mention the fact that:

- The Municipality of Rahovec has presented the status of accounts receivable in the amount of €2,115,000. This amount includes old receivables from many years from the tax on business activity in the amount of €827,000, where the possibility of their collection is minimal. Also, 59% of this account is made of receivables from property tax;
- During 2018, the Municipality has been indicted for significant amounts of liabilities, where the amount of €105,933 was paid directly from the treasury and through court decisions; and
- The Municipality has a continuous increase of contingent liabilities where their value has reached the value of over €32 million, with an increase of €690,000 compared to the previous year. If litigation is decided in favour of the operators, the organization is expected to have serious financial loss.

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<sup>2</sup> "Statement of Liabilities, unpaid (invoices) " / AFS-2017.

<sup>3</sup> 7 cases resulted in poor classification of expenditures. Out of these, four payments were presented as goods and services while they were wages in the amount of €15,526.24; one payment of €14,581.20 presented as a capital investment belonged to wages; and in two cases payments of €1,190.21 presented as capital investment belonged to goods and services. In 10 other cases payments of €97,683.93 presented as investments belong to goods and services. Also in one case, the payment of €9,000 presented as goods and service belonged to subsidies.

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## **Responsibility of Management for AFS**

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

The Mayor 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.

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**

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

- Compliance with MoF Regulation no.01/2017 on the Annual Financial Reporting of Budget Organisations;

- Requirements of LPFMA no. 03/ L-048, (as amended and supplemented);
- Law on Local Government Finance No. 05/L -108 as amended and supplemented by No. 03/L-049;
- Compliance with Financial Rule no.01/2013 on Expenditure of Public Money and No. 02/2013 on Management of Non-financial Assets by BOs;
- Action Plan on implementation of recommendations;
- Procurement Plan and Report on Signed Public Contracts;
- Requirements of Financial Management and Control (FMC) procedures.
- Regular Quarterly Reports for the Municipal Assembly and discussion of IA and NAO Reports by MA;

The AFSs submitted in January 2019, were presented with some errors, which were adjusted and corrected by the management on 22/02/2019. Even though improvements were made to the AFSs, there were still some errors, mainly misstatements, disclosure of assets, receivables and liabilities, which we have presented in the emphasis of matter in audit opinion.

Given the above - the Declaration made by the CEO and CFO when the draft AFS are submitted to the Ministry of Finance cannot be considered fully correct.

In the context of other external reporting requirements, we have no issues to raise.

## 2.3 Recommendations related to Annual Financial Statements

**Recommendation C1** The Mayor should ensure that an analysis is undertaken to determine the causes for Emphasis of Matter. Actions should be taken to address key weaknesses in correct classification of expenditure, and to eliminate weaknesses for fair presentation of receivables and liabilities, disclosed in the Emphasis of Matter in Audit Opinion.

Further on, the Mayor should ensure that effective processes are in place to confirm that the 2019 AFS production plan formally addresses all compliance issues related to the AFS. This should also 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 Financial Officer should not be signed unless all necessary checks have been applied to the draft AFS.

### 3 Financial Management and Control

Our work related to Financial Management and Control (FMC) reflects the detailed audit activities undertaken on Revenue and Expenditure Systems within Budget Organisations. Specifically, we have handled budget management, procurement, human resources as well as assets and liabilities.

#### Financial Management and Control Conclusion

Although the Municipality has established a system of controls over expenditures and revenues, our audit has highlighted the presence of some weaknesses in terms of compliance as a result of non-implementation of regulations and guidelines related to revenues and expenditures. This reflects a lack of proper oversight by the Municipality in the mentioned areas. Other areas where more improvements are needed are the process of management and reporting of accounts receivable, liabilities and in classification of expenditures.

#### 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 <sup>4</sup>	2018 Outturn	2017 Outturn	2016 Outturn
<b>Sources of Funds</b>	<b>13,698,232</b>	<b>14,284,134</b>	<b>13,064,949</b>	<b>11,661,181</b>	<b>11,567,016</b>
Government Grant -Budget	11,862,731	12,125,110	11,995,391	10,591,533	10,420,032
Carried forward from previous year <sup>5</sup> -	0	174,221	153,712	205,751	245,380
Own Source Revenues <sup>6</sup>	1,650,027	1,650,027	778,167	769,469	801,797
Domestic Donations	0	6,112	4,853	0	5,400
External Donations	0	95,588	95,493	89,100	94,407
Borrowings <sup>7</sup>	185,474	233,076	37,333	5,328	0

The final budget is higher than the initial budget by €585,902. This increase is a result of Government Grant in the amount of €262,379, revenues carried forward from previous year in the amount of €174,221, increase of borrowings funds in the amount of €47,602, internal donations in the amount

<sup>4</sup> Final budget - the budget approved by the assembly which was subsequently adjusted for by the Ministry of Finance.

<sup>5</sup> Own Source Revenues unspent in previous year carried forward into the current year.

<sup>6</sup> Receipts used by the entity for financing its own budget.

<sup>7</sup> Borrowings from World Bank (for Health and Education Directorate).

of €6,112 and external donations in the amount of €95,588.

In 2018 the Municipality has spent 91.5% of the final budget or €13,064,949, with a decrease of performance compared to 2017 (96%). However, the budget implementation remains at an unsatisfactory level and explanations for the current position are detailed below.

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

Description	Initial Budget	Final Budget	2018 Outturn	2017 Outturn	2016 Outturn
<b>Spending of funds by economic categories</b>	<b>13,698,232</b>	<b>14,284,134</b>	<b>13,064,949</b>	<b>11,661,181</b>	<b>11,567,016</b>
Wages and Salaries	7,296,623	7,259,001	7,219,001	6,991,962	6,966,078
Goods and Services	1,563,385	1,585,148	975,106	694,080	657,625
Utilities	250,500	250,500	248,823	249,753	250,497
Subsidies and Transfers	191,322	193,514	179,062	188,900	173,992
Capital Investments	4,392,402	4,995,970	4,442,957	3,536,486	3,518,824

Explanations for changes in budget categories are given below:

- Despite the increase in final budget for capital investments by €603,568 compared with the initial budget, during the year only 89% of the budget was spent. Execution of the capital investment budget presented at €4,442,957 includes payments in the amount of €1,681,513 for accumulated debts from previous years. So real spending under the capital investment program is only €2,761,444 or just 55% of the current budget. Out of 86 signed contracts during 2018 in the amount of €7,102,009, 42 of them in the amount of €4,157,938 or 48% were signed at the end of the year, this is another reason for not executing the budget, which is a challenge that should be addressed by the management.
- In the category of salaries and wages, the final budget was increased by €585,902 compared to the initial budget, and 99% of the final budget was spent;
- The final budget for goods and services compared to the initial budget was increased by €21,763. Despite this, the level of execution was only at 62%. Ambitious planning in the category of revenues from waste collection has led to limited execution of expenditures for goods and services. Also, the dynamics of execution is not in line with the planning, because 42% of the expenditures from this category were executed in the last quarter of the year, due to the municipality's inability to plan and manage the available budget well;
- The final budget for utilities has not changed compared to the initial budget and the Municipality has managed to spend 99% of the budget for this category. It is also worth noting that the liabilities in this category have been reduced by €5,650 (from €18,448 in 2017 to €12,799 at the end of 2018);

- The Municipality has also received grants from domestic and external donors in the amount of €101,700, which during this year were implemented at level of 99%. Also the value of €37,333 was spent on borrowings in the category of goods €26,081 and €11,252 in the category of investments for the Directorate of Education and Health<sup>8</sup>.

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## Issue A 91 - Weaknesses in budget execution

**Finding** Execution of the budget for goods and services, which was only 62% and capital investments are the main challenges faced by the municipality, since the amount of €1,681,513 was used to pay the debts accumulated from previous years, and the estimated budget execution for capital investments is 55%<sup>10</sup>. The level of execution compared to the aimed objectives was not achieved since the management had not made a realistic revenue planning and a significant number of contracts were concluded at the end of the year. Further on, the lack of a regular analysis of budget performance has led to the transfer of revenues in the amount of €402,538 in the following year as unspent funds.

**Risk** Ineffective use of available funds will result in failure to achieve the organization's objectives, less projects for citizens, and in funding current year liabilities with next year's budget.

**Recommendation A1** The Mayor should ensure that budget performance is monitored systematically on a monthly basis, and that this review identifies and addresses obstacles for budget execution at a planned level. Budget planning should refer to real possibilities to secure funds from revenues, and to prioritize budget execution in settlement of outstanding liabilities.

### 3.1.1 Revenues

Revenues generated by the Municipality for 2018 were €994,864, or compared to the last year the Municipality has higher collection of own source revenues by €173,725 or expressed in percentage 21% more. As the dominant category in the structure of own source revenues is the collection of property tax revenues, about 42%. The Municipality has collected property tax in the amount of €419,434 with an increase of 37% compared to the same period of the previous year. However, the Municipality does not yet have effective internal controls related to collection and reporting of revenues, including their aggregation in the AFS.

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<sup>8</sup> 18,884.40(Education) and 8,485(Health).

<sup>9</sup> Issue A and Recommendation A – implies new issues and recommendations.

Issue B and Recommendation B – implies repeating issues and recommendations.

Issue C and Recommendation C – implies issues and recommendations that are partially repeated.

<sup>10</sup> Execution of the budget not including the payment of debts from previous years

Table 3. Own Source Revenues (in €)

Description	Initial Budget	Final Budget	2018 Receipts	2017 Receipts	2016 Receipts
Own source revenues	1,650,027	1,650,027 <sup>11</sup>	994,864	820,959	1,009,926

In addition to the revenues presented in the table, the Municipality has also received revenues from police fines, court fines, and forestry agency and in the amount of €165,359.

Revenue collection was at 70%, which is a low performance compared to an ambitious planning. This is because the revenue planning according to economic code "50201" (License for Free Individuals Activities) was €400,000 while the collection for this category was only €842. According to municipal officials these are planned revenues for waste management and collection that will be applied for the first time this year, which were also coded incorrectly. In addition to the economic code "50026" (tax on legalization of buildings), the Municipality has planned to collect revenues in the amount of €45,000 while there was zero collection. Such planning has resulted in poor performance in collecting these revenues, although at the level of total collection of revenues the Municipality has shown progress compared to the previous year. Own source revenues in the amount of €931,879 was spent mainly for capital projects, even at a rate of 90% or €838,449.

## Issue A 2 - Weaknesses in Management of Property Tax Revenues

### Finding

Article 16 of the Administrative Instruction 03 / 2011- "On Property Registration", stipulates that "All of the unfinished buildings should be taxed at 40% of the market value of residential buildings and in calculating the tax deduction will not be included €10,000, the depreciation rate and quality of construction ". Out of the 15 audited cases, in three cases, the Municipality had incorrectly calculated the tax by calculating the construction quality rate by 1.1 (excellent) for unfinished building, by overestimating about €45 billed tax charge for these taxpayers. While in two other cases the value per m<sup>2</sup> was not calculated in accordance with the property tax regulation overestimating the taxpayer's tax obligation by €47. This happened due to incorrect appraisal of properties by field surveyors; and

According to the Administrative Instruction 03/2011 and the Municipality Regulation on Setting of Property Tax for 2018 in Article 2, point 2.3, is cited the quality of construction material for the construction of the building were are defined 5 categories. In two cases, property tax (for industrial business "basement on and below the ground") is calculated and billed with the wrong coefficient by calculating the value of the tax with coefficients 0.79 in the first case and 0.82 in the second case, which coefficients are not foreseen in the

<sup>11</sup> Includes revenue planning from traffic fines (€ 100,000), court fines (€ 120,000) and forestry agencies €1,000

regulation. Revenues from property tax for this case are underestimated by about €1,057. According to responsible officials, this is a technical error, which was not detected or corrected by the municipality.

**Risk**

Lack of effective controls on management of property tax revenues will continue to result in low collection rates, while in the case of overestimating the tax charge, the Municipality may lose trust for fair treatment of taxpayers and may become subject of lawsuit by taxpayers.

**Recommendation A2** The Mayor should establish sound controls that ensure effective collection of revenues by including and determining a fair assessment of the tax charge in accordance with the rules and real situation in the field by engaging competent surveyors.

**Issue B1 – Delays in collection of rent and exercise of business activity****Finding**

“The rent payment shall be carried out at the latest on the 5th of the following month by the renter, in contrary the contract will be terminated, followed by enforced collection of the unpaid debt” based on article 2 of the contract between the Municipality and users of the municipal property “. In 5 cases the users of municipal property did not make rent payments according to the conditions stipulated in the contract and the debts amounted to €48,283. The Municipality has warned these users but did not proceed with further procedures, to execute the collection of debts after 5/15 days through private enforcement agents or terminations of the contract; and

Article 28, point 2 of the “Regulation on Municipal taxes, fees, charges and fines” states: “ All business entities that don’t perform payment of tax, fees, charges and municipal fines foreseen by this Regulation shall be subject to enforced execution of payment through a competent court and private enforcement agents. Failure of businesses to pay the tax for exercising the activity in 10 cases has resulted in accumulation of debts in the amount of €35,812, without making any payments. The Municipality has applied warnings notifying businesses that they have to pay their debts within 15 days otherwise enforced execution of payment will be applied, including interest or closure of the premises. The Municipality did not refer any case to the court or to the private enforcement agencies, as a result of how they conduct their businesses activities.

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**Risk** Poor management of rented property contracts has resulted in increase of uncollectible accounts from business tax revenues. The unwillingness to take effective measures for collection of revenues, increase the risk of non-fulfilment of the revenue plan and results with less capital projects planned to be funded by these funds.

**Recommendation B1** The Mayor should review the reasons behind the existing situation and set appropriate measures so that the responsible departments within a reasonable timeframe will collect the arrears, or to stop them for using public properties or exercising their activities if they do not meet the obligations towards the municipality.

### 3.1.2 Wages and Salaries

Wages and Salaries are paid through a centralized payment system managed by MAP and MoF. The final budget for the category of wages and salaries was €7,259,001, while expenditures were €7,219,001 or 99%. Key controls should confirm the accuracy and completeness of payments such as approval and placement of employee wages, verification of the allowed number and other controls, and approval of the budget for salaries and wages by the Municipal Assembly. We also reviewed whether employees were paid according to the contract.

The number of approved staff was 1,160 employees, while the current number of employees was 1. We have audited recruitment procedures as well as personnel files to confirm their regularity.

#### Issue A 3 – Weaknesses in Management of Personnel

**Finding** The Municipality was not able to provide us with completed files and contracts for 19 officials who are engaged in the Emergency and Security Directorate, on the basis of which compensation payments are made. According to the Personnel Manager there is no relevant documentation for these officials and this occurrence has emerged as a result of a memorandum signed years ago, because the officials are part of the Ministry of Internal Affairs, while compensation of wages and other compensations are carried out by the Municipality. This shows that there is a lack of clear specifications for the Municipality's Human Resources.

Further on, the Government of Kosovo, based on the decision no. 11/26 dated 19/05/2010, all employees categorized as Civil Servants under the Law on Civil Service will receive payments on a monthly basis in the amount of €30 gross. According to the data required by the Ministry of Internal Affairs we have identified that these officials are not categorized as civil servants, while they are compensated with additional of €31.2 per month, and these employees were compensated in total amount of €7,488 during 2018. This situation has occurred because these officials are part of the staff of the Ministry of Internal Affairs, as a result of the memorandum.

**Risk** Payments of the officials in the absence of the relevant documentation results with inability to justify wages/salaries or to allow evaluation of the performance review, and allowances that are made not in compliance with the government decision, are irregular payments and result in budget loss.

**Recommendation A3** The Mayor should ensure the review the possibility for these officials to be transferred to the institutions where they work or to complete their files in the municipality, to establish legal basis for execution of their wages. Allowances are made only to officials foreseen by the Government's decision and the amounts obtained in violation of this decision are returned to the municipal budget.

## **Issue C2 - Personnel files not-updated**

**Finding** Government Decision no. 06/29 dated 15.05.2015, requires a certified decision by authorized personnel officers for proving the years of work experience. Also Law no. 04/L-032 on pre-university education, Article 20, paragraph 2.2 determines that the director of the educational institution has executive responsibilities in the overall management and administration of the institution, including the duty for evaluation, discipline and other matters pertaining to teachers; and other education employees. Out of the 21 audited samples, in nine cases in the education directorate and two cases in the health directorate, evidence of work experience years was not reflected in a decision certified by authorized personnel officers, as the basis for payment of work experience. Also the files in the directorate of education were missing Leave Requests and performance evaluations. This was due to the lack of coordination between schools and the directorate for education, and the negligence of the management and responsible staff.

**Risk** Payments made without supporting documentation increase the risk for incorrect payment of allowance for work experience. Further on, absence of staff performance evaluation does not provide a fair view of the performance achieved.

**Recommendation C2** The Mayor should ensure that the Directors of Educational/Health Institutions and the Personnel Manager must complete the documentation about work experience in order to establish a legal basis for execution of the allowance based on experience. Further on, school directors should monitor staff leave requests and performance evaluations and to update personnel files with new documents.

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### 3.1.3 Goods and Services and Utilities

The final budget for goods, services and utilities in 2018 was €835,648. Out of them €1,223,929 or 66% were spent.

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#### Issue A 4 – Non-compliance in recruitment of staff for special services

**Finding** Article 12, paragraph 4 of the Law on Civil Service, fixed term appointments for a period of less than six months shall be made on the basis of contracts called “Special Services Agreement” which are subject to the Law on Obligations, and for which a simplified recruitment procedure is applied.

In 2018, the Municipality had signed special services agreements with nine (9) employees, and from six (6) audited samples, it resulted that the Municipality has engaged and paid these employees for a term of more than six (6) months. The Municipality initially used the wrong legal basis by entering into contracts for specific duties and tasks with a duration of 120 days according to the Law on Labour for recruitment of the civil staff (as an interviewer, official etc.) and after conclusion of these contracts, it continued for another 6 months with special service agreements, based on the Law on Civil Service. According to the personal manager this happened due to misinterpretation of laws.

**Risk** Such recruitments result in legal non-compliances and lack of monitoring, increase the risk for the Municipality will not get in return the desired contribution / performance / service by the staff engaged in this form.

**Recommendation A4** The Mayor should ensure that the entry into the agreement for special services / contracts for specific duties is done in full compliance with the legal framework and the term of contract does not exceed the deadlines set by the laws. The Mayor must also ensure that such recruitments are made only in cases where there are specific needs.

#### Issue A 5 – Shortcomings in payment process, according to the co-financing agreement

**Finding** In April 2018, the Municipality entered into a co-financing agreement in the amount of €109,315 (the Municipality participated with the amount of €99,815, while Caritas Kosova with €9,500) with the possibility of renewing one year for the project “Social Health Care and Ambulatory Care in Rahovec Home Care 2018. Article 5, point 1.3 of this agreement stipulates that; the selection of new professional staff who will be involved in these activities will be done in cooperation between the parties and in compliance with the legal procedures. According to the agreement point 2.1 for the purpose of implementing the agreement, the Municipality takes the responsibility to monitor the implementation of the project (agreement) and point 2.3 to

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regularly monitor staff performance. In two (2) cases, the payment for contracting services in the amount of €20,000 was paid by the Municipality whereas we were not provided with evidence that the activities according to the agreement were coordinated starting from the selection of the staff to the detailed reporting of the activities, and achievement of the project goal. Failure to appoint an officer who will be responsible for implementation of the agreement and the negligence of the officials responsible for execution of payments supported by relevant documentation was the main cause of the lack of necessary evidence in the relevant cases.

**Risk** Failure to comply with the obligations based on the agreement results in poor controls and increases the risk for the Municipality to pay for services that have not been received, or provided to the citizens, or even achieved low value for money spent.

**Recommendation A5** The Mayor should ensure that measures are taken for supervision of the co-financing agreements including clear reporting requirements during the implementation and monitoring of the project, in accordance with the requirements of the agreements and the rules on expenditure of public money.

### 3.1.4 Subsidies and Transfers

The final budget for subsidies and transfers was €193,514. Out of them €179,062 was spent in 2018. They relate to subsidies to public entities: sports clubs, various NGOs, cultural arts associations, individual beneficiaries, etc.

#### **Recommendations**

We have no recommendations in this area.

### 3.1.5 Capital Investments

The current budget for the Capital Investment category is €4,995,970 while expenditures during 2018 are €4,442,957 or expressed in percentage 89% of the budget. They relate to the construction of roads, sewer systems, school buildings, social housing facilities, etc. Compared to the previous year, there is a better budget performance in this category by €906,471, or about 26%.

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**Issue A 6 – Regular weaknesses in management of payment for investments**

**Finding** Article 26, point 2 of the Financial Rule No.01 / 2013 on Expenditure of Public Money, specifies that, “ to process a payment the following documentation is required in advance: Request for purchase / commitment; Copy of contract signed by the responsible procurement officer as an authentic copy of the original, purchase order; report of acceptance, payment order and original invoice” .

In two (2) cases the Municipality executed payments in the absence of the report on the acceptance of works whose total value of payments was €15,206. The cause of this phenomenon was the negligence by the staff and the responsibility to implement the laws and rules in force, which resulted with failed internal controls.

**Risk** Processing of payments in absence of relevant documentation as required by applicable laws and regulations increases the risk that these payments will not be executed for the purpose intended, or bring over the risk that the Municipality has made payments for potentially unfinished works.

**Recommendation A6** The Mayor should ensure that the responsible persons perform checking of the necessary documentation prior to the execution of the payments, and strengthen control measures that the works or goods are received through relevant evidence or with reports on acceptance.

**Issue A 7 - Works carried out after the expiration of the contract and validity of the performance security**

**Finding** In the contract “Construction of a common building for housing of families in need in Rahovec, respectively point 10.2 of the special terms amongst others stipulates that this is a three year contract, the value of which is: €517,784 signed on 22/12/2014 , and should end in December 2017, however, we have noticed that based on the positions during 2018, €90,000 have been executed and paid after the expiration of the contract, as well as the validity of the performance security of the project required under the contract had expired. In this case, the Municipality did not undertake any necessary procedures to renew the contract and the already expired performance security. Insufficient planning of funds when the contract was concluded and the municipality's inability to provide funds for ongoing project implementation and negligence were caused by exceeding the contract's terms of validity. The contract manager through the Supervisory Body has ordered the Operator to carry out the works to fulfil the relevant contract.

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**Risk** Entry into contractual obligations without sufficient funds and poor contract management resulted with delays in project implementation and poor controls during execution of payments. Execution of payments without security of execution, in case of a dispute increases the risk for non-implementation of regular work, as set forth in the contract. As a result, the Municipality is also exposed to the constant risk for management of other projects.

**Recommendation A7** The Mayor should develop policies and procedures to ensure that the implementation of the projects is fulfilled within specified time frame in the respective contract, and the execution of all payments shall be made in accordance with the contract and guaranteed with performance security, eliminating the possibility of entering into contract without sufficient funds.

#### **Issue A 8 – Adjustment of positions for the contracted Estimated value**

**Finding** Construction of the Roadway in Brestoc - Hoqë e Madhe and Construction of the Roadways in Hoqë e Vogël, Brestoc, Krusha e Madhe and Fortesë. According to Article 25 point 1 states that “Estimated value and Bill of Quantities will be used to calculate the price of the contract. The contractor will be paid for the amount of work performed at the indicative rate and before calculation of each item, in two (2) cases the Municipality executed the payment for positions that were exceeded in comparison to the contracted bill. So the oversight body respectively the contract manager did not respect the estimated value and bill of quantities as annex to the initial contract. Inadequate planning of projects, respectively lack of drafting of executive projects before the initiation of procurement procedures has led to the adjustment of the positions within contracted estimated value.

**Risk** Exceeding of the positions stipulated in the contractual agreement constitutes a breach of the Contract and as such increases the risk that the operator will not perform the jobs according to the standards and quality defined under the initial contract. Incorrect estimated values bring over additional expenditures and delays in implementation.

**Recommendation A8** The Mayor should ensure that the requesting units evaluate requirements correctly, and ensure to prevent initiation of any procurement procedure in the absence of an executive project, and should pay higher attention in determining positions so that such errors are not repeated.

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**Issue C3 – Signing of Contracts without sufficient funds available**

**Finding** According to the Financial Rule No.: 01/2013 on the Expenditure of Public Money “no public contract should be signed without commitment of funds” also “budget organization does not undertake any obligation during the current fiscal year in the amount exceeding the allocated funds”.

While testing of procurement procedures we have observed that in one case the contract was signed without sufficient funds committed. The total value of the signed contract was €16,480, while the commitment of funds was only €15,000. Also from testing the payments for compliance purposes, in 49 cases the Municipality had received the bill together with the supporting documentation before the date of the request for commitment of funds, the amount of these payments was €2,692,026. This phenomenon results from inadequate budget planning, initiation of procurement procedures, and signing of contracts without sufficient funds available and commitment of funds.

**Risk** Entering into obligations without commitment of funds, risks complete financing of projects, thus result in failure to implement them. There is also the risk of incurring additional expenditures from payment of interest, penalties, due to delays in execution of payments.

**Recommendation C3** The Mayor should ensure that the procurement office carries out additional controls so the signing of the contracts is made upon commitment of funds.

**Issue A 9 – Calculation errors in contracted estimated value**

**Finding** According to the Public Procurement Manual, respectively point 41.8, the Contracting Authority (CA) will correct completely calculation errors in the tender if such errors are found during the examination of tenders, however, this correction cannot be more than (2%) of the total bid value. If the corrected amount is less than +/- 2%, the CA will correct such mistakes and will inform in writing the operator using the Standard Form or the Standard Letter of Tender Clarification Letter. If the operator in question refuses to correct the error, the offer will be rejected. The Contracting Authority should also to all relevant tenderers (EO which have submitted tenders) a written notice of such changes.

In three (3) cases, the Municipality had signed employment contracts where the bidders had made calculation errors in the estimated value they had applied with. Such errors were below the norm allowed by the Public Procurement Law, but the same was not identified by the evaluation commission nor by procurement officers, to intervene with correction in the

contracted estimated value. Lack of competence by the members of the evaluation commission and procurement officers has resulted in such error.

**Risk** Failure to make necessary corrections based on legal requirements poses a risk where the same errors may accompany implementation of contracts until their completion, and as such to carry financial implications that are not identified by the Municipality in due time.

**Recommendation A9** The Mayor through the Procurement Manager should ensure that each procurement procedure is carefully analysed and evaluated by the evaluation committee in order to avoid potential errors during the procurement process, and to ensure compliance with established legal criteria.

#### **Issue A 10 - Lack of Execution Project**

**Finding** According to the Public Procurement Guide issued by the PPRC respectively point 20.13 specifies the following: The Executing Project is a graphic design of all administrative and engineering processes of the required works as described in the Technical Specifications and therefore, in special cases, it requires architectural and structural works to be executed. The Contracting Authority is responsible for drafting the Executing Project and which must be attached (also in electronic equipment) to the Technical Specifications, which are part of the tender dossier. No Contracting Authority is permitted to issue tender documentation without attached detailed description of the project. We have identified that;

In the contract "Repair of roads and sidewalks LOT II" in the amount of €87,765, the Municipality did not make proper drafting of the executive project as required. The reasons for not drafting the project were the dilemmas of the persons responsible for drafting or not the executive project for the framework contract.

**Risk** Development of procurement procedures without a previously drafted project may produce the effect that the works implemented in these projects deviate from the standard construction requirements and fail to achieve the right quality.

**Recommendation A10** The Mayor should ensure that drafting of executive projects is carried out in accordance with legal requirements and the Procurement Office is in possession of completed projects prior to initiating procurement procedures for execution of works.

### 3.1.6 Common Issues on Goods and Services and Capital Investments

Issues of concern are payments executed based on court decisions and provisions under Article 39.2 of the Law on Public Financial Management and Accountability (LPFMA):

#### Issue A 11 - Payments based on Court Decisions

**Finding** Out of the 13 audited cases we have found that based on court decisions and provisions of Article 39.2 of LPFMA the Treasury has executed payments in favour of operators and municipal officials in the amount of f €105,933, nine (9) of them resulted in additional expenses in the amount of €4,360 for enforcement procedure, interest etc. There were mainly delays in payment of obligations due improper time planning, especially for the payment of jubilee payments to the officials on the occasion of retirement.

**Risk** Entry into obligations without funds available, delays in implementation of the agreements, and the failure to plan and compensate jubilee payments results in continuity of the execution of payments by the Treasury through court decisions, where additional administrative costs may occur. This imbalances budget projections and risks achievement of objectives and execution of planned projects.

**Recommendation A11** The Mayor should strengthen controls to ensure they have available funds needed to meet their financial obligations on time. Further on, should ensure that the Municipality handles all legal obligations to legal claimants, and take necessary actions to address them in order to eliminate additional unnecessary expenditures.

## 3.2 Capital and non-capital assets

The value of capital assets presented in the 2018 AFSs in the amount of €81,807,000. The reason for the increase of the value of assets by €19,502,000 was mainly due to the valuation of assets by the valuation commission where the land value has been increased from €15,093,000 to €30,495,000, while the value of non-capital assets was €470,000. We have reviewed whether the record keeping process is in compliance with the requirements of the MoF Regulation-no.02/2013 on management of non-financial assets in budget organizations, the inventory process and the physical existence of assets. We have no recommendations in this area.

#### Issue C4 - Shortcomings in Asset Inventory

**Finding** The commission report on asset inventory was incomplete, it contains the assets of the municipality, but not the non-financial assets of petroleum stocks in MFMC, Article 19.4 of Regulation 02/2013 on Non-financial Assets Management states that the responsibilities of the commission for inventory

among other things are "Inventory of all non-financial assets owned and controlled by the budget organization". Based on information from the responsible officer and verification by the team we noticed that there is an amount of 3,000 litres. We have also noticed that the latest fuel supply was made on 25/12/201 in the amount of 10,000 litres. Such a failure occurred from not informing the commission of the existing fuel quantity in the tank.

**Risk**

Due to the failure to perform complete asset inventory as required by the regulation, Municipality may not identify the real and factual situation of assets, which may become subject to loss or alienation. This may result in lower value of financial assets than that which is presented in the AFS.

**Recommendation C4** The Mayor should ensure that the commission of inventory and valuation of non-financial assets makes the registration and evaluation of all assets in the possession of the Municipality and after the completion of the process prepares a final report on the condition of assets, which should be reconciled with the accounting registers of the municipality. Displayed differences should be clarified and registries should be updated according to the latest recorded data.

**Issue A 12 - Inadequate management of parking lot****Finding**

According to the requirements of the AI No.3-2008 - for management of official vehicles, the forms that are used for use of official vehicles have been defined. In three cases when using the vehicles in the Directorate of Administration, Education and MFMC, we found that the forms for using the vehicles were not completed, as required by the AI. Also the form, order for the use of vehicles was not signed by the competent officer, the Vehicle Authoriser. This situation resulted by the negligence of the competent municipal officials, failure to segregate duties and lack of sufficient controls over the management of the vehicle fleet.

**Risk**

Lack of control in management of official vehicles increases the risk for occurrence of unjustified expenditures and unauthorized use of municipal vehicles.

**Recommendation A12** The Mayor should ensure drafting of an internal policy that clearly defines the requirements and responsibilities for use of vehicles. The persons responsible for oversight of the parking lot should ensure that trip tickets for use of official vehicles are updated and that vehicles are used only upon approval of the authorised persons.

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### 3.3 Receivables

The list of debtors to the municipality, according to the data presented AFS is €2,115,000. Most of them relate to property tax, in the amount of €1,241,000, business tax at €827,000, for property rent €38,000, etc.

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#### Issue A 13 - High amount of receivables

**Finding** Although the Municipality faces high amount of uncollected receivables, no adequate policy on collecting receivables from previous years has been developed or applied, in particular for property tax, business taxes and rent payments. Failure to set adequate mechanisms by the Municipality to collect these revenues has led to this situation. Despite of warnings used as a measure by the municipality, there were no continuous actions such as the initiation of procedures for imposed collection of debts through other competent bodies.

**Risk** Lack of mechanisms has resulted in high amount of receivables that increase the risk for these accounts may become uncollectible due to its statutory limitation, and may result in non-implementation of the expenditures plan.

**Recommendation A13** The Mayor should ensure that all possible options are actively reviewed by setting policies, regulations and other mechanisms in order to increase the efficiency in collecting receivables. Further on, all measures in accordance with the law should be considered, against operators who do not meet their contractual obligations.

### 3.4 Outstanding liabilities

The statement of liabilities not paid to suppliers at the end of 2017 in the amount of €2,243,767 have shown a decrease in value by €1,435,458. These liabilities are carried forward to be paid in 2019. This amount of outstanding liabilities is the result of insufficient internal controls and entry into the liabilities without sufficient funds available. The Municipality has also contingent liabilities and the amount presented in the AFSs is €32,695,000.

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#### Issue A 14-High amount of Liabilities

**Finding** According to the Financial Rule 01-2013 MoF - Expenditure of Public Money the BO must pay every valid invoice for payment of goods and services received within 30 calendar days from the date of receipt of invoice. Furthermore, we have identified 57 cases in the amount of €1,716,604 that have exceeded the legal deadline. Reason behind this occurrence was the

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entry into obligations without sufficient funds available, and ineffectiveness of internal controls.

**Risk**

As a result of payment delays and lack of complete information, the ability of the Municipality to plan in advance and manage liquidity needs may be diminished. Also, the Municipality may face additional expenditures by interest on penalties for delays in payment.

**Recommendation A14** The Mayor should strengthen controls in the payment management process to ensure that the Municipality does not enter into obligations without sufficient funds available, so that all invoices are paid within the legal deadline. Further on, should ensure that the reporting of the obligations is done on a monthly basis, in accordance with the legal requirements which should include their exact status.

## 4 Good Governance

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

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. The level of compliance with FMC requirements by Budget Organizations is monitored by 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

We have evaluated several activities that can contribute to good governance, as well as existing opportunities for further improvement as follows:

The full and quality addressing of our recommendations as well as raised compliance issues remain a challenge for the Municipality of Rahovec. Progress in the management of the organization, mainly in revenue collection, settlement of debts, as well as considerable actions have been undertaken in the construction of contractual relations with various donors. For most municipal activities there is good communication and reporting between heads of the units and the Mayor, but there are no minutes of meetings and strategic monitoring, and there is no formal and systematic reporting (monitoring) that links the municipal objectives to the results.

There are a number of weaknesses in the municipal governance system, particularly with regard to accountability, risk management and quality of managerial reporting. The self-assessment questionnaire completed by the municipality reflects this situation only partially, with some positive comments on presence of existing arrangements not based on evidence.

A key tool to support effective governance is the implementation of recommendations given by external auditors. The effective response to the implementation of the recommendations is not satisfactory. This section is dealt with in more detail in the chapter "Progress in implementing recommendations".

The municipality is in possession of the integrated plan (2016-2018), urban modality plan (2016-2020), waste management plan (2017-2021), municipal development plan (2011-2020) and general urban plan. However, other strategic plans such as spatial plans, strategic anti-corruption plan, regional development strategy etc., were still missing.

The internal audit had not provided a clear view on the level of security of internal controls, while the audit committee during this year was more efficient in its activities.

### 4.1 Internal Audit System

To carry out an effective audit requires a comprehensive work program that reflects the financial and other risks of the audited entity, and provides sufficient assurance on the effectiveness of internal control. The impact of Internal Audit reports should be judged by the importance given to management by addressing the recommendations as well as by the support provided by an effective Audit Committee. The Internal Audit Unit (IAU) operates with two staff members - the Director of IAU and one auditor. IAU had completed 10 planned audits, as well as conducted an additional audit at the management's request.

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**Issue C5 - Inefficient functioning of IAU**

**Finding** IAU had given recommendations on how management should improve the functioning of internal control. According to the Action Plan prepared by this unit out of 53 recommendations, 21 were in the process of implementation, while other 32 were implemented. The checklist of addressing the recommendations for 2018 based on carried out audits by this unit, the facts (evidences and supporting documents) that indicate that there are specific actions taken for implementation of the recommendations by the audit findings are not established. During this year, the Audit Committee held three meetings with the IAU, but the committee's influence did not improve management's activities in addressing the recommendations.

**Risk** Failure to document the facts that there are specific actions that the recommendation has been implemented by the audited directorates with the necessary evidence and supporting documents, may undermine the effectiveness of the IAU's work and reduce the possibility for the NAO to obtain assurance from IAU's work, despite the volume and quality of the work undertaken. Further on, failure to address internal audit recommendations can result in continued weaknesses, inefficiency in the internal control system, financial loss for the municipality, and poor value for money.

**Recommendation C5** To achieve maximum benefit from internal audit services, the Mayor should review the reasons for the limited actions undertaken by management in relation to internal audit recommendations, and to cooperate with the Audit Committee for establishment and improvement of the quality of internal control. Further on, to ensure that a quality control review will be applied to each audit file by the IAU Director.

## 4.2 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.

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## Issue B2- Weaknesses in Management Control and Risk Management

**Finding** Our review of managerial controls implemented in the municipality's main financial system has highlighted ineffective financial reporting on expenditures and revenues to senior management as well as incomplete analyses. This has happened because the format of managerial reports does not provide explanations on adjustments in the budget and that budget projections have not been updated on a monthly basis. As such general government arrangements require improvement. We have identified that revenue controls are still not very effective, and there are deficiencies in controls in some areas of expenditure, in particular the low level of budget execution from the category of investments, goods and services. Also during 2018, the Municipality has no written policies and procedures for risk management, in particular the risk of fraud and irregularities.

**Risk** Failure to update financial reporting and activities of the senior management reduces management's ability to manage municipal activities in proactive manner and diminishes the effect of budget controls. This may also result in low collection of revenues. Further on, it may result in poor service provision.

**Recommendation B2** The Mayor should ensure that a review has been carried out to determine the form of financial and operational reporting to senior management from which all relevant information that influences the quality and timely decision-making by the management. Budget performance, including revenues and expenditures, and implementation of the procurement plan should be subject to regular reporting and review by the management.

## 5 Progress in implementing recommendations

Our Audit Report on the 2017 AFS of the Municipality of Rahovec resulted in 13 key recommendations. The Municipality prepared an Action Plan stating how all recommendations will be implemented. Further on, the Municipality had not followed any formal process to monitor the implementation of the recommendations and take the necessary actions for their implementation. This has affected only a part of the recommendations being implemented and the same shortcomings in some areas are repeated. The Municipal Assembly of Rahovec on 26<sup>th</sup> July 2018 has reviewed and discussed the audit report of the NAO for 2017. Despite the above mentioned commitments, the majority of the recommendations have remained in the process of implementation or not implemented.

By the end of our 2018 audit, four (4) recommendations have been implemented, two (2) have been closed; five (5) were in process and two (2) were not yet implemented. For a more detailed description of the recommendations and how they are addressed, see Table 4 (or Table of Recommendations).

**Table 4 Summary of prior year recommendations and of 2018**

No	Audit area	Recommendations of 2017	Actions taken	Status
1	AFS	The Mayor should ensure that an analysis is undertaken to determine the causes of the Qualification and Emphasis of Matter. Actions should be taken to address the underlying causes in a systematic and pragmatic manner to remove errors in the classification of capital expenditure, registration of capital and non-capital assets, contingent liabilities, and to ensure that the Municipality has filled in the position of the Chief Financial Officer by an employee of Civilian Servant Status. Further on, the Mayor should ensure that effective processes are in place to confirm that the 2018 AFS production plan formally addresses all compliance issues related to the AFS and includes 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 Executive Officer and Financial Officer should not be signed unless all necessary checks have been applied to the draft AFS.	Specific actions have been taken, the Municipality has fulfilled the position of CFO, has managed to register capital assets but not stocks, a there is still misclassification of expenditures.	Partially implemented.
2	Revenues	The Mayor should take all necessary actions to ensure that a 1/3 property verification is carried out, so that property tax records are complete and to get the optimum benefits of this property. Additional actions should be undertaken to ensure that the deduction of €10,000 is applied only to the principal residences.	During the testing and analysis of the database, as well as the change of the law on property tax, the necessary actions have been taken.	Implemented.
3	Delays in collection of rent	The Mayor should ensure effective management of leasing contracts and establish effective mechanisms for collection of revenues in accordance with the contracted terms, respectively to follow deadlines for collection of leased assets.	In addition to the warnings, the Municipality does not apply other legal measures, but this year has been reformulated.	Not implemented.
4	Inadequate management of Personnel Files/ Records	The Mayor should ensure that specific steps have been undertaken to improve controls on personnel files so that all records are complete with the necessary documentation for management of staff, and assessment of their performance (annual performance evaluation). The Municipality should issue an internal act (policy) on performance evaluation.	During the audit we found that the personnel files are still incomplete.	Partially implemented.

5	Signing of contract without procurement procedures	The Mayor should ensure that the Law on Public Procurement is applied, in order for every service to be contracted based on competition.	During the audit, we found that the Municipality applies agreements for services without procurement procedures.	Implemented.
6	Shortcomings in award of subsidies	The Mayor should ensure that payments are made to the official account of the subsidy beneficiary, and adequate measures are taken to ensure that the civil registry is updated on a regular basis.	This year, the Municipality has taken measures to make payments on the official account of the beneficiary.	Implemented.
7	Entering into contractual liabilities, without funds	The Mayor should provide additional checks on signed contracts, so that budget funds are committed prior to entering into contractual obligations. Long-term commitments should be harmonized with the dynamics of projects and planned with the Municipal Mid- Term Budget Framework.	The Municipality continues to have same situation this year. This is related to recommendation C3.	Recommendation Closed.
8	Delays in execution of payments	The Mayor should ensure that the appropriate financial discipline is established to ensure that received invoices are paid within the legal time limit for the purpose of managing and controlling contractual obligations.	No measures have been taken during this year for invoices to be paid within the legal deadline.	Partially implemented.
9	Poor Asset Management	The Mayor should ensure that the management of non-financial assets is made in full compliance with Regulation 02/2013 on management of nonfinancial assets. In this regard, should provide controls on registration of noncapital assets, and ensure the full operation of the e-Asset system for registration of assets under €1,000, and stocks.	The Municipality has undertaken several activities for asset management based on Regulation, but there is still no evidence / stock registration.	Partially implemented.
10	Shortcomings in managing and reporting of liabilities	The Mayor should strengthen controls over the management and reporting of Outstanding Liabilities. Further on, should ensure that all received invoices are recorded and signed in the protocol book. Further on, should establish an effective control system by which all unpaid invoices are accurately and thoroughly reported on a monthly basis to the MoF, and correctly disclosed in the AFSs, at the end of each year.	Specific actions have been taken, the Municipality has applied regular monthly reporting on obligations to the MoF.	Implemented.
11	Low level of implementation of Recommendations	The Mayor should ensure that the implementation of the action plan is monitored on a continuous basis and reported on a regular monthly or quarterly basis with respect to the progress achieved in this regard. Recommendations that are not	Despite drafting an action plan, its monitoring is ineffective as this year the Municipality	Recommendation Closed.

		implemented within the foreseen deadlines should be reviewed and proactive actions taken against the barriers presented during the implementation.	has shown weaknesses in financial management, controls and reporting.	
12	Poor functioning of IAU and AC	The Mayor should ensure that the IAU scope covers to a possible extent the current period by assisting the on-going operational activities. Further on, to ensure a higher focus of management to make the AC operational, towards achievement of this goal.	Reports further do not cover the current period, despite the functionality of the Audit Committees most of the recommendations of this unit have not been implemented.	Partially implemented.
13	Weaknesses in Management Controls and Risk Management	The Mayor should ensure that a review has been carried through to determine the form of financial and operational reporting to senior management. Budgetary performance, 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.	Failure to execute budget at a satisfactory level by some categories, not compiling a list of risks, the high level of receivables, prove that there is no proper reporting been established and performed.	Implemented.
No	Audit Area	Recommendations given in 2018		
1	AFS	The Mayor should ensure that an analysis is undertaken to determine the causes for Emphasis of Matter. Actions should be taken to address key weaknesses in correct classification of expenditure, and to eliminate weaknesses for fair presentation of receivables and liabilities, disclosed in the Emphasis of Matter in Audit Opinion. Further on, the Mayor should ensure that effective processes are in place to confirm that the 2019 AFS production plan formally addresses all compliance issues related to the AFS. This should also 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 Executive Officer and Financial Officer should not be signed unless all necessary checks have been applied to the draft AFS.		
2	Budget Execution Level	The Mayor should ensure that budget performance is monitored systematically on a monthly basis, and that this review identifies and addresses obstacles for budget execution at a planned level. Budget planning should refer to real possibilities to secure funds from revenues, and to prioritize budget execution in settlement of outstanding liabilities.		

3	Collection of revenues from PT	The Mayor should establish sound controls that ensure effective collection of revenues by including and determining a fair assessment of the tax charge in accordance with the rules and real situation in the field by assignment of competent interviewers.
4	Revenues from Rent	The Mayor should review the reasons behind the existing situation and set appropriate measures so that the responsible departments within a reasonable timeframe will collect the arrears. Otherwise, the Municipality shall prohibit the use of public properties or the exercise of the activity for non-fulfilment of obligations towards the municipality.
5	Lack of fireman files	The Mayor should ensure the review the possibility for these officials to be transferred to the institutions where they work or to complete their files in the municipality, to establish legal basis for execution of their wages. Allowances are made only to officials foreseen by the Government's decision and the amounts obtained in violation of this decision are returned to the municipal budget.
6	Failure to update files	The Mayor should ensure that the Directors of Educational/Health Institutions and the Personnel Manager must complete the documentation about work experience in order to establish a legal basis for execution of the allowance based on experience. Further on, school directors should monitor staff leave requests and performance evaluations and to update personnel files with new documents.
7	Irregularities in recruitment for special services	The Mayor should ensure that the entry into the agreement for special services / contracts for specific duties is done in full compliance with the legal framework and the term of contract does not exceed the deadlines set by the laws. The Mayor must also ensure that such recruitments are made only in cases where there are specific needs.
8	Co-financing Agreements	The Mayor should ensure that measures are taken for supervision of the co-financing agreements including clear reporting requirements during the implementation and monitoring of the project, in accordance with the requirements of the agreements and the rules on expenditure of public money.
9	Capital Investments	The Mayor should ensure that the responsible persons perform checking of the necessary documentation prior to the execution of the payments, and strengthen control measures that the works or goods are received through relevant evidence or with reports on acceptance.
10	Capital Investments	The Mayor should develop policies and procedures to ensure that the implementation of the projects is fulfilled within specified time frame in the respective contract, and the execution of all payments shall be made in accordance with the contract and guaranteed with performance security, eliminating the possibility of entering into contract without sufficient funds available.
11	Capital Investments	The Mayor should ensure that the requesting units evaluate requirements correctly, and ensure to prevent initiation of any procurement procedure in the absence of an executive project, and should pay higher attention in determining positions for such errors are not repeated.
12	Capital Investments	The Mayor should ensure that the procurement office carries out additional controls so the signing of the contracts is made upon commitment of funds.
13	Capital Investments	The Mayor through the Procurement Manager should ensure that each procurement procedure is carefully analysed and evaluated by the evaluation committee in order to avoid potential mistakes during the procurement process, and also to ensure compliance with established legal criteria.

14	Capital Investments	The Mayor should ensure that drafting of executive projects is carried out in accordance with legal requirements and the Procurement Office is in possession of completed projects prior to initiating procurement procedures for execution of works.
15	Payments based on article 39.2 and based on Court Decisions	The Mayor should strengthen controls to ensure they have available funds needed to meet their financial obligations on time. Further on, should ensure that the Municipality handles all legal obligations to legal claimants, and take necessary actions to address them in order to eliminate additional unnecessary expenditures.
16	Shortcomings in Asset Inventory	The Mayor should ensure that the commission of inventory and valuation of non-financial assets makes the registration and evaluation of all assets in the possession of the Municipality and after the completion of the process prepares a final report on the condition of assets, which should be reconciled with the accounting registers of the municipality. Displayed differences should be clarified and registries should be updated according to the latest recorded data.
17	Management of vehicle parking	The Mayor should ensure drafting of an internal policy that clearly defines the requirements and responsibilities for use of vehicles. The persons responsible for supervision of the vehicle fleet must ensure that trip tickets for use of official vehicles are updated and that vehicles are used only upon approval of the authorised persons.
18	Receivables	The Mayor should ensure that all possible options are actively reviewed by setting policies, regulations and other mechanisms in order to increase the efficiency in collecting receivables. Further on, all measures in accordance with the law should be considered, against operators who do not meet their contractual obligations.
19	Outstanding Liabilities	The Mayor should strengthen controls in the payment management process to ensure that the Municipality does not enter into obligations without sufficient funds available, so that all invoices are paid within the legal deadline. Further on, should ensure that the reporting of the obligations is done on a monthly basis, in accordance with the legal requirements which should include their exact status.
20	IAU	To achieve maximum benefit from internal audit services, the Mayor should review the reasons for the limited actions undertaken by management in relation to internal audit recommendations, and to cooperate with the Audit Committee for establishment and improvement of the quality of internal control. Further on, to ensure that a quality control review will be applied to each audit file by the IAU Director.
21	Financial and Operational Reporting	The Mayor should ensure that a review has been carried out to determine the form of financial and operational reporting at senior management from which all relevant information that influences the quality and timely decision-making by the management. Budget performance, including revenues and expenditures, and implementation of the procurement plan should be subject to regular reporting and review by the management.

## 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.

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*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 1705<sup>19</sup> provides additional guidance on the specific language to use when expressing a modified opinion and describing the auditor's responsibility. It also includes illustrative examples of reports.

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

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

158. An Emphasis of Matter paragraph should:

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

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

## Annex II: Confirmation letter



Republika e Kosovës

Republika Kosovo / Republic of Kosovo

*Komuna e Rahovecit*



### LETËR E KONFIRMIMIT

Për pajtueshmërinë me të gjeturat e Auditorit të Përgjithshëm në Raportin e auditimit për vitin 2018 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 Rahovecit, për vitin e përfunduar më 31 dhjetor 2018 (në tekstin e mëtejme "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. *Artur* .....

Kryetar i Komunës,

Data: 05.Prill.2019, Rahovec,