



**MONTENEGRO**

**AUDIT AUTHORITY**

No: 3011-4-06-130/4  
Date: 13<sup>th</sup> March 2020

**ANNUAL AUDIT ACTIVITY REPORT**

**OF THE AUDIT AUTHORITY FOR**

**ANNUAL COUNTRY ACTION PROGRAMME FOR THE MONTENEGRO FOR THE YEAR 2014, ANNUAL  
COUNTRY ACTION PROGRAMME FOR THE MONTENEGRO FOR THE YEAR 2016 AND ANNUAL  
COUNTRY ACTION PROGRAMME FOR THE MONTENEGRO FOR THE YEAR 2017**

**FOR THE PERIOD FROM 01 JANUARY UNTIL  
31 DECEMBER 2019**

Podgorica, March 2020

## Contents

1. INTRODUCTION .....	5
1.1 Details of the responsible audit authority and other bodies that have been involved in preparing the report .....	5
1.2 Reference period (i.e. the year) and the scope of the audits (including the expenditure declared to the Commission for the year concerned) .....	5
1.3 Identification of the sector/policy area(s) covered by the report and of its/their operating structure and management structure .....	6
1.4 Description of the steps taken to prepare the report and to draw the audit opinion .....	7
2. SUBSTANTIAL CHANGES IN MANAGEMENT AND CONTROL SYSTEM .....	7
2.1 Personal changes .....	7
2.2 Organisational changes .....	7
3. CHANGES TO THE AUDIT STRATEGY .....	8
4. SYSTEMS AUDITS .....	8
4.1 Details of the bodies that have carried out systems audits, including the audit authority itself .....	8
4.2 Summary table of the audits carried out .....	8
4.3 Description of the basis for selection of the audits in the context of the audit strategy .....	14
4.4 Principal findings / Follow-up / Corrective measures applied or recommended and Conclusion .....	15
4.5 Description (where applicable) of specific deficiencies related to the management of financial instruments, detected during systems audits and of the follow-up given by the national authorities to remedy these shortcomings. ....	18
4.6 Level of assurance obtained following the system audits and justification. ....	18
5. AUDITS OF SAMPLES OF TRANSACTIONS .....	19
5.1 Authorities/bodies that carried out the sample audits, including the audit authority .....	19
5.2 Description of the sampling methodology applied and information whether the methodology is in accordance with the audit strategy .....	19
5.3 Indication of the parameters used for statistical sampling, materiality level, the confidence level, the expected error rate applied, calculation of the required sample and the interval, sampling unit, number of sampling units in the population, number of sampling units actually audited .....	20
5.4 Reconciliation of the expenditure declared to the Commission in the financial year to the sampled expenditure. Reconciling items include negative items where financial corrections have been made in the financial year, as well as differences between amounts declared in euro and amounts in national currency, where relevant .....	20
5.5 Where there are negative items, confirmation that they have been treated as a separate population .....	22
5.6 In case of the use of non-statistical sampling, indicate the reasons for using the method in line with Article 12 (2) of Commission Implementing Regulation (EU) No 447/2014, the percentage of actions/operations/expenditure covered through audits, the steps taken to ensure randomness of the sample (and its representativeness) and to ensure a sufficient size of the sample enabling the audit authority to draw up a valid audit opinion. A projected error rate is calculated also in case of non-statistical sampling. ....	22
5.7 Summary table (see below), broken down where applicable by programme indicating the eligible expenditure declared to the Commission during the year, the amount of expenditure audited, and the percentage of expenditure audited in relation to total eligible expenditure declared to the Commission for the last year, as well as the total number of sampling units in the population and the number of sampling units actually audited for the random sample. ....	23
5.8 Analysis of the principal results of the audits (sample items selected and audited, together with the respective amount and types of error by operation) as well as the nature of errors found, root causes and corrective measures proposed, including mitigating these errors in the future. ....	24
5.9 Details of the most likely error rate (total error rate) and, in case of statistical sampling method, the upper limit of the error rate as a result of the audits of operations, and the amount of irregular expenditure detected and the error rate resulting from the random sample audited. ....	26
5.10 Compare the total error rate with the set materiality level, in order to ascertain if the population is materially misstated or not. If so, analyse the significance of the total error rate for the audit opinion and report the recommended corrective measures. ....	26
5.11 Corrections relating to the current year implemented by the operating structure/management structure before submitting the final declaration of expenditure and financial statements to the Commission, and resulting from the audits of operations, including flat rate or extrapolated corrections. ....	26
5.12 Residual total error rate following the implementation of the above-mentioned corrections and significance for the audit opinion. ....	27
5.13 Information on the results of the audit of the complementary (e.g. risk based) sample, if any. ....	27
5.14 Information on the follow-up of irregularities, including revision of previously reported residual error rates, as a result of all subsequent corrective actions. ....	27
5.15 Details of whether any problems identified were considered to be systemic in nature, and the measures taken, including a quantification of the irregular expenditure and any related financial corrections. ....	27
5.16 Description (where applicable) of specific deficiencies or irregularities related with financial instruments. Where applicable, indication of the sample error rate concerning the audited financial instruments. ....	27
5.17 Analysis of the principal results of the audits of negative items, including conclusions as to whether the negative	

items audited correspond to the decisions of the country or of the Commission, and reconcile with the amounts included in the accounts on amounts withdrawn and recovered during the year and amounts to be recovered at the end of the year. ....	27
5.18 Conclusions drawn from the results of the audits with regard to the effectiveness of the management and control system. ....	27
6. AUDITS OF THE ANNUAL FINANCIAL REPORTS OR STATEMENTS/ANNUAL ACCOUNTS.....	28
6.1 Indication of the authorities/bodies that have carried out audits of the annual financial reports or statements/annual accounts. ....	28
6.2 Description of audit approach used to verify the elements of the annual financial reports or statements/annual accounts defined in Article 12(2) and Article 23(1)(b) of Commission Implementing Regulation (EU) No 447/2014. ...	28
6.3 Indication of the conclusions drawn from the results of the audits in regard to the completeness, accuracy and veracity of the declaration of expenditure and financial statements, including an indication on the financial corrections made and reflected in the declaration of expenditure and financial statements as a follow-up to the results of the audit on transactions/operations. ....	29
6.4 Indication of whether any problems identified were considered to be systemic in nature, and the measures taken. ....	29
7. FOLLOW-UP OF PREVIOUS YEARS' AUDIT ACTIVITY .....	30
7.1 Information on the follow-up of outstanding audit recommendations and on the follow-up of results of systems audits and audits of transactions/operations (including the audits done in regard to the complementary sample) from earlier years. ....	30
7.2 Subsequent events affecting the previous opinion and the previous annual audit activity report under Article 12(3) of Commission Implementing Regulation (EU) No 447/2014 .....	37
8. OTHER INFORMATION .....	37
9. OVERALL LEVEL OF ASSURANCE .....	37
9.1 Explanation on how the overall level of assurance on the proper functioning of the management and control system is obtained from the combination of the results of the system audits and audits of operations .....	37
9.2 Where the total error rate relating to the expenditure declared in the payment claims in a year is above the materiality level, analyse its significance and assess whether this indicates a serious deficiency(ies) in the functioning of the relevant management and control system during the year. Where relevant, take also account of the results of other national or Union audit work carried out in relation to the year. ....	38
9.3 Assessment of the corrective action necessary both from a system and financial perspective.....	38
9.4 Assessment of any relevant subsequent adjustments made and corrective actions taken such as financial corrections included in the declaration of expenditure and financial statements and assess the residual error rate and the need for any additional corrective measures necessary both from a system and financial perspective. ....	38
10. TABLE FOR DECLARED EXPENDITURE AND SAMPLE AUDITS .....	39

## List of abbreviations

AA	Audit Authority of Montenegro
AAAR	Annual Audit Activity Report
AAO	Annual Audit Opinion
AMD	Annual Management Declaration
CAP 2014	Annual Country Action Programme for Montenegro for the year 2014
CAP 2016	Annual Country Action Programme for Montenegro for the year 2016
CAP 2017	Annual Country Action Programme for Montenegro for the year 2017
CFCU	Central Finance and Contracting Unit
DMS	Directorate for Management Structure
EC	European Commission
EU	European Union
EUD	Delegation of the European Union
IA	Implementing Agency
IPA II	Instrument for Pre-Accession Assistance II perspective
IPA	Instrument for Pre-Accession Assistance
LTEC	Long Term Employment Contract
MCSS	Management, Control and Supervision System
MEC	Ministry of Economy
MF	Ministry of Finance
MoP	Manual of Procedures
MSDT	Ministry of Sustainable Development and Tourism
MTMA	Ministry of Transport and Maritime Affairs
NAO SO	NAO Support Office
NAO	National Authorising Officer
NFD	National Fund Division
NIPAC	National IPA Coordinator
OG MNE	Official Gazette of Montenegro
PIU	Project Implementation Units
PWA	Public Works Administration
TEC	Temporary Employment Contract
WLA	Work Load Analysis

## **1. INTRODUCTION**

### **1.1 Details of the responsible audit authority and other bodies that have been involved in preparing the report**

The Audit Authority of Montenegro, as an independent audit body, was established by the Law on Audit of EU Funds (OG 14/12,54/16, 37/17 and 70/17). The Audit Authority is responsible for audit of EU funds (IPA, Structural Funds after the accession of Montenegro to the European Union, and other EU funds). According to Article 3 of the Law on Audit of EU funds, the AA is functionally and operationally independent of all actors in EU funds management and control system.

The Law on Audit of EU Funds prescribes that auditees shall be public institutions and organisations, authorities and organisations of local self-government units, natural and legal persons who receive, use and manage EU funds respectively.

The functions and responsibilities of the Audit Authority are set out in the Framework Agreement between Montenegro and the European Commission on the arrangements for implementation of Union financial assistance to Montenegro under the Instrument for Pre-accession Assistance (IPA II)- (OG MNE, No 5/2015) and in Commission Implementing Regulation (EU) No 447/2014 on the specific rules for implementing Regulation (EU) No 231/2014 of the European Parliament and of the Council establishing an Instrument for Pre-accession Assistance (IPA II).

The Audit Authority is responsible for verifying:

- the completeness, accuracy and veracity of the annual financial reports or statements and the underlying annual accounts;
- the efficient and effective functioning of the management, control and supervision systems;
- the legality and regularity of the underlying transactions.

The Audit Authority submits an Annual Audit Activity Report (AAAR) and Annual Audit Opinion (AAO) following the model set out in Annexes D and E of the Framework Agreement.

This report has been prepared by the Audit Authority of Montenegro. Other bodies were not included in preparation of this report given that AA does not rely on work of other bodies in performing its functions.

### **1.2 Reference period (i.e. the year) and the scope of the audits (including the expenditure declared to the Commission for the year concerned)**

Pursuant to Article 3(f) of the Framework Agreement between Montenegro and the European Commission on the arrangements for implementation of Union financial assistance to Montenegro under the Instrument for Pre-accession Assistance (IPA II), reference period for this Annual Audit Activity Report is financial year and covers the period from 1 January to 31 December 2019.

In 2019 the Audit Authority carried out system audit for CAP 2014, CAP 2016 and CAP 2017 and audit of operations for CAP 2014. In the period covered by this report, the AA was not in a position to perform audit of operations for CAP 2016 and CAP 2017 because in the period from 1 January 2019 to 31 December 2019 there were no declared expenditures to EC for those Programmes.

As a part of a system audit in December 2019 the AA performed follow-up of the findings and recommendations given in the course of previous audits. In the period February-March 2020 AA conducted also Audit of accounts for CAP 2014, CAP 2016, CAP 2017 and CAP 2018.

### **1.3 Identification of the sector/policy area(s) covered by the report and of its/their operating structure and management structure**

The report covers Annual Country Action Programme for Montenegro for the year 2014 (No C (2014) 9837), Annual Country Action Programme for Montenegro for the year 2016 (No C (2016)8226) and Annual Country Action Programme for Montenegro for the year 2017 (No C (2017/040-216; 2017/039-816).

Within Annual Country Action Programme for Montenegro for the year 2014, 11 actions shall be implemented by indirect management which covers following policy areas: Democracy and Governance (5); Environment and Climate Action (1); Transport (2); Competitiveness and Innovation (3).

Financing Agreement for the Annual Country Action Programme for Montenegro (Objective 1 - part 1 and Objective 2- part 1) 2014/032-022 and 2014/032-803, for the year 2014 was signed on 10<sup>th</sup> December 2015.

The total estimated cost of Programme CAP 2014 is EUR 24,515,340.00 and the maximum Union contribution to this Programme is set at EUR 21,288,220.00.

By signing Addendum of the Financing Agreement for the Annual Country Action Programme for Montenegro (Objective 1 - part 1 and Objective 2- part 1) 2014/032-022 and 2014/032-803, for the year 2014 on 30/07/2018, the budget for Action 12 "Rehabilitation of the railway section Kos-Trebešica" is increased by 1.046.068,26 (national co-financing). According to that, the total estimated cost of Programme CAP 2014 is EUR 25,561,408.26 and the maximum Union contribution to this Programme is set at EUR 21,288,220.00.

Within Annual Country Action Programme for Montenegro for the year 2016, 2 actions shall be implemented by indirect management which covers following policy areas: Environment and Climate Action (1) and Competitiveness and Innovation (1).

Financial Agreement for the Annual Country Action Programme for Montenegro for the year 2016 was signed on 22<sup>nd</sup> December 2017. The total estimated cost of Programme CAP 2016 is EUR 26,544,530 and the maximum Union contribution to this Programme is set at EUR 22,948,900.

Within CAP 2017, 3 actions shall be implemented by indirect management which covers following policy areas: Democracy and Governance (2) and Transport (1).

Financing Agreement for the Annual Country Action Programme for Montenegro for the year 2017 was signed on 17<sup>th</sup> December 2018. The total estimated cost of Programme CAP 2017 is EUR 16,156,529 and the maximum Union contribution to this Programme is set at EUR 13,511,103.

Structures and bodies being part of the management, control and supervision system of those Programmes are, as follows:

- 1) The National IPA Co-ordinator (NIPAC)
- 2) The National Authorising Officer (NAO)
- 3) The Management structure:
  - The National Fund
  - The NAO support office
- 4) The Operating Structure:
  - The NIPAC office
  - Implementing Agencies: Central Finance and Contracting Unit (CFCU) and Public Works Administration (PWA)
  - PIUs of the line ministries: (MF, MSDT, MEC, MTMA for CAP 2014); (MSDT and MEC for CAP 2016); (MF and MTMA for CAP 2017).

## **1.4 Description of the steps taken to prepare the report and to draw the audit opinion**

The AAAR was prepared as a result of audit activities carried out during the 2019. During 2019 the AA carried out system audit for CAP 2014, CAP 2016 and CAP 2017 and audit of operations for CAP 2014. During performance of system audit in 2019, Audit Authority performed follow-up of the findings and recommendations given in the course of previous audits.

With a view to drawing up an audit opinion, Audit Authority assessed results of audit activities from the performed audit of management, control and supervision system (including follow-up), audit of operations, audit of accounts and the consistency of the management declaration with regard to performed audit work.

Based on the available information and Final Audit Reports the Audit Authority prepares the Annual Activity Audit Report and the Annual Audit Opinion.

The Audit Authority submits Annual Audit Activity Report and Annual Audit Opinion to the European Commission and the Government of Montenegro with a copy to the NIPAC and the NAO by 15 March each year.

## **2. SUBSTANTIAL CHANGES IN MANAGEMENT AND CONTROL SYSTEM**

AA regularly monitored and gathered information on changes in the Management, Control and Supervision System (MCSS) and we reported on significant changes in MCSS in our AAARs. In our last AAAR we reported about the significant changes in the Management, Control and Supervision System (MCSS) which occurred until the end of December 2018.

In this AAAR we described significant personal and organizational changes occurred in the period from 1<sup>st</sup> January to 31<sup>st</sup> December 2019.

### **2.1 Personal changes**

- Based on the Decision on appointment no. 01-004-574 from 11<sup>th</sup> February 2019, Mr Bojan Vujović was appointed Head of the NIPAC Office. NAO was informed about the change by the European Integration Office letter no. 01-004-708 to the NAO from 8<sup>th</sup> March 2019.
- By the Decision on appointment no. 01-004-813 from 19<sup>th</sup> March 2019 sent to the NAO, Ms Ivana Vujošević was appointed Deputy National IPA Coordinator.
- Based on the Decision on appointment from 1<sup>st</sup> April 2019 sent to NAO, Mr Velibor Damjanović was appointed the Head of NAO Support Office.

### **2.2 Organisational changes**

- The Government of Montenegro adopted the Decision on top up on salaries for IPA staff, which came into force on 9<sup>th</sup> March 2019. The Decision was published in the Official Gazette of Montenegro no. 13/19 on 1<sup>st</sup> March 2019.
- New Decision on the appointment of persons responsible for carrying the functions in relation to decentralised and/or indirect management of pre-accession funds of the European Union (EU) was adopted by the Government of Montenegro. The Decision was published in Official Gazette no. 33/19 on 14<sup>th</sup> June 2019.

All the changes are assessed by Audit Authority and we can confirm that all changes are in compliance with applicable regulations.

The changes that occurred in MCSS in 2019 do not have an impact on the audit work.

### **3. CHANGES TO THE AUDIT STRATEGY**

Audit Strategy 2019–2021 for the Annual Country Action Programme for Montenegro for the year 2014 and Annual Country Action Programme for Montenegro for the year 2016 was prepared in November 2018. The Auditor General of Audit Authority approved it and sent it to the European Commission, with a copy to National Authorising Officer, on November 29<sup>th</sup> 2018.

The reason for drawing up update of strategy is Financial Agreement which was signed on 17<sup>th</sup> December 2018. Having in mind that management and control system established for CAP 2014 and CAP 2016 is the same for CAP 2017, Audit Authority updated Audit Strategy 2019– 2021 for the Annual Country Action Programme for Montenegro for the year 2014 and Annual Country Action Programme for Montenegro for the year 2016 in compliance with Clause 5 of FWA. Updated Audit Strategy 2019-2021 for the IPA II 2014-2020 for the CAP 2014, CAP 2016 and CAP 2017 was submitted to European Commission - DG Near on 13<sup>th</sup> May 2019. Also, new risk assessment has been done.

According to the Update Audit Strategy we carried out system audit, audit of operations and audit of accounts.

### **4. SYSTEMS AUDITS**

#### **4.1 Details of the bodies that have carried out systems audits, including the audit authority itself**

In accordance with the Update Audit Strategy 2019-2021 for the IPA II 2014-2020 for the Annual Country Action Programme for Montenegro for the year 2014 (hereinafter: CAP 2014), Annual Country Action Programme for Montenegro for the year 2016 (hereinafter: CAP 2016) and Annual Country Action Programme for Montenegro for the year 2017 (hereinafter: CAP 2017) approved by Auditor General and submitted to EC on 13<sup>th</sup> May 2019, the AA of Montenegro conducted an audit of the management, control and supervision system (hereinafter MCSS) established in the bodies of Management structure: NAO/NAO support office, National Fund and in the bodies of Operating structure: Implementing Agencies: Central Finance and Contracting Unit (CFCU) and Public Works Administration(PWA) and Project Implementation Units of the line ministries: Ministry of Finance, Ministry of Sustainable Development and Tourism, Ministry of Transport and Maritime Affairs and Ministry of Economy.

#### **4.2 Summary table of the audits carried out**

During the strategic audit planning (Update Audit Strategy 2019-2021 for the IPA II 2014-2020 for the CAP 2014, CAP 2016 and CAP 2017 (May 2019)) for the purpose of defining audit areas the Audit Authority performed risk assessment for each body of CAP 2014, CAP 2016 and CAP 2017 at the key requirement/process/function level (further: process level). We identified and assessed issues and processes that are significant for the audit and that could be common for all or several bodies that are participating in management and implementation of programme.

Based on results of risk assessment performed during preparation of the Update Audit Strategy 2019-2021 we decided that during 2019 bodies whose total risk score is over 40% will be audited. According to the above mentioned, audit included the following bodies: NAO/NAOSO, NFD, CFCU, PWA, PIUs: MF, MTMA, MSDT and MEC, and with the general audit objective to verify the effective and efficient functioning of the management, control and supervision system.



The key requirements/ICFRs which were under the scope of audit are as follow:

- **NAO Support Office:** Control Environment, Control Activities, Information and Communication, Monitoring of Internal Control Framework
- **National Fund:** Control Environment, Control Activities, Information and Communication
- **CFCU/IA:** Control Environment, Control Activities
- **PWA/IA:** Control Environment, Control Activities
- **MTMA/PIU:** Control Environment ,Control Activities
- **MF/PIU:** Control Environment ,Control Activities
- **MEC/PIU:** Control Environment ,Control Activities
- **MSDT/PIU:** Control Environment ,Control Activities

Also in Updated Audit strategy 2019-2021 we stated that during the individual audit engagement planning auditors would define the key functions/processes within each key requirement which will be encompassed by the appropriate audit activities in particular body in 2019. The scope of each individual audit will depend on level of implementation of Programmes at the time of audit performing. Apart from that, follow-up of recommendations from the previous system audits is going to be conducted within the planned system audits for 2019.

In accordance with above mentioned, during preparation of system audit engagement we performed the risk assessment in order to identify whether the ICFR selected are still risky and to asses which sub-criteria will be covered by the audit and through which process.

Based on the audit strategy, understanding of audit environment and performed risk assessment (per each body), the following audit areas (ICFR, sub-criteria, processes) as well as specific audit/compliance objective per audit area, were covered during the system audit:

- **NAO/NAOSO**
  - 1(b) Supervision by management of tasks delegated to subordinates
  - 1(e) Accountability for allocated tasks and responsibilities
  - 3(a) Selection and development of control activities
  - 4(a) Information to support functioning of internal controls
  - 4(b) Internal communication
  - 4(c) External communication
  - 5(b) Assessment, recording and communication of internal control deficiencies.
- **NFD**
  - 1(b) Supervision by management of tasks delegated to subordinates
  - 1(e) Accountability for allocated tasks and responsibilities
  - 3(a) Selection and development of control activities
  - 4(a) Information to support functioning of internal controls
  - 4(b) Internal communication
  - 4(c) External communication.
- **CFCU – IA**
  - 1(b) Supervision by management of tasks delegated to subordinates
  - 1(e) Accountability for allocated tasks and responsibilities
  - 3(a) Selection and development of control activities
- **PWA - IA**
  - 1(b) Supervision by management of tasks delegated to subordinates
  - 1(c) Establishment of structures, reporting lines, and authorities and responsibilities
  - 1(e) Accountability for allocated tasks and responsibilities
  - 3(a) Selection and development of control activities

- PIUs: MF, MTMA, MEC and MSDT
  - 1(b) Supervision by management of tasks delegated to subordinates
  - 1(e) Accountability for allocated tasks and responsibilities
  - 3(a) Selection and development of control activities

Additionally, during each individual system audit the follow-up on recommendations from previous audits is regularly performed, which is then a constituent part of each individual system audit report. The AA performed follow-up of the findings and recommendations that remained opened from the previous audits.

Results of performed follow-up are that 4 out of 9 findings are closed.

Described in details in point 7 of this Report.

Summary of the audit carried out:

Audit period	Programme (CCI and title)	Audit Body	Audited Body(ies)	Date of the audit	Scope of the audit	Principal findings and conclusions	Problems of systemic character and measures taken	Estimated financial impact (if applicable)	State of follow-up (closed/or not)
01.01.2019-31.12.2019	Annual Country Action Programme for Montenegro for the year 2014 - C(2014) 9387	Audit Authority of Montenegro	NAO/ NAOSO	May to mid-December 2019.	-1(b) Supervision by management of tasks delegated to subordinates -1(e) Accountability for allocated tasks and responsibilities -3(a) Selection and development of control activities -4(a) Information to support functioning of internal controls -4(b) Internal communication -4(c) External communication -5(b) Assessment, recording and communication of internal control deficiencies.	n/a	n/a	n/a	n/a
	Annual Country Action Programme for Montenegro for the year 2016 - C(2016)8226		NFD	"	-1(b) Supervision by management of tasks delegated to subordinates -1(e) Accountability for allocated tasks and responsibilities -3(a) Selection and development of control activities -4(a) Information to support functioning of internal controls -4(b) Internal communication -4(c) External communication.	Accounting procedures ensuring complete, accurate and transparent accounting following internationally accepted accounting principles  ICFR: 3(a)  For details please see further below the section 4.4 of this AAAR.	n/a	n/a	Open

	Annual Country Action Programme for Montenegro for the year 2017 – C(2017/040-216;2017/039-816)		CFCU - IA	“	<p>-1(b) Supervision by management of tasks delegated to subordinates</p> <p>-1(e) Accountability for allocated tasks and responsibilities</p> <p>-3(a) Selection and development of control activities</p>	<p>Accounting procedures ensuring complete, accurate and transparent accounting following internationally accepted accounting principles</p> <p>ICFR: 3(a)</p> <p>For details please see further below the section 4.4 of this AAAR.</p>	n/a	n/a	Open
			PWA - IA	“	<p>-1(b) Supervision by management of tasks delegated to subordinates</p> <p>-1(c) Establishment of structures, reporting lines, and authorities and responsibilities</p> <p>-1(e) Accountability for allocated tasks and responsibilities</p> <p>-3(a) Selection and development of control activities</p>	<p>Accounting procedures ensuring complete, accurate and transparent accounting following internationally accepted accounting principles</p> <p>ICFR: 3(a)</p> <p>Inadequate performed control activities</p> <p>ICFR: 3(a)</p> <p>For details please see further below the section 4.4 of this AAAR.</p>	n/a	n/a	Open

			MF - PIU	“	-1(b) Supervision by management of tasks delegated to subordinates -1(e) Accountability for allocated tasks and responsibilities -3(a) Selection and development of control activities	Lack of segregation of duties  ICFRs: 1(b); 3(a)  For details please see further below the section 4.4 of this AAAR.	n/a	n/a	Open
			MTMA - PIU	“	-1(b) Supervision by management of tasks delegated to subordinates -1(e) Accountability for allocated tasks and responsibilities -3(a) Selection and development of control activities	n/a	n/a	n/a	n/a
			MSDT/PIU	“	-1(b) Supervision by management of tasks delegated to subordinates -1(e) Accountability for allocated tasks and responsibilities -3(a) Selection and development of control activities	n/a	n/a	n/a	n/a
			ME/PIU	“	-1(b) Supervision by management of tasks delegated to subordinates -1(e) Accountability for allocated tasks and responsibilities -3(a) Selection and development of control activities	n/a	n/a	n/a	n/a

#### **4.3 Description of the basis for selection of the audits in the context of the audit strategy**

During the strategic audit planning (Update Audit Strategy 2019-2021 for the IPA II 2014-2020 for the CAP 2014, CAP 2016 and CAP 2017) for the purpose of defining audit areas the Audit Authority performed risk assessment for each body of those programmes at the key requirement/process/function level (further: process level). We identified and assessed issues and processes that are significant for the audit and that could be common for all or several bodies that are participating in management and implementation of programme.

Based on results of risk assessment performed during preparation of the Update Audit Strategy 2019-2021 we decided that during 2019 bodies whose total risk score is over 40% will be audited. According to the above mentioned, audit included the following bodies: NAO/NAOSO, NFD, CFCU, PWA, PIUs: MF, MTMA, MSDT and MEC, and with the audit objective to verify the effective and efficient functioning of the management, control and supervision system.

Bearing in mind the current status of implementation of CAP 2014 (all contracts are signed), CAP 2016 (no activities have been implemented) and CAP 2017 (no activities have been implemented) we decided that precise scope of audits will depend on level of implementation of CAP 2014, CAP 2016 and CAP 2017 at the time of conducting each individual audit. Audits planned to be conducted during 2019, will include relevant key requirements (Internal Control Framework from Annex B of Framework Agreement) for each body. However, this approach will not be applicable if we cannot test operating effectiveness of controls related to certain key requirements. For those reasons, we will perform risk assessment at the beginning of each individual audit engagement in order to determine key requirements/process/functions which are possible to test operating effectiveness of designed procedures and controls.

During the individual audit engagement planning auditors have defined the key functions/processes within each key requirement which will be encompassed by the appropriate audit activities in particular body in 2019. The scope of each individual audit depended on level of implementation of Programmes at the time of audit performing. Apart from that, follow-up of recommendations from the previous system audits was conducted within the planned system audits for 2019.

Based on the audit strategy, understanding of audit environment and performed risk assessment (per each body), audit areas (ICFR, sub-criteria, processes) as well as specific audit/compliance objective per audit area, which were covered during system audit are:

IPA body Audit area	NAO/NAOSO	NFD	CFCU	PWA	MF	MTMA	MEC	MSDT
1(b)	X	X	X	X	X	X	X	X
1(c)	-	-	-	X	-	-	-	-
1(e)	X	X	X	X	X	X	X	X
3(a)	X	X	X	X	X	X	X	X
4(a)	X	X	-	-	-	-	-	-
4(b)	X	X	-	-	-	-	-	-
4(c)	X	X	-	-	-	-	-	-
5(b)	X	-	-	-	-	-	-	-

#### 4.4 Principal findings / Follow-up / Corrective measures applied or recommended and Conclusion

The outcome of the audit process is summarized in final system audit report that provides findings and recommendation which were identified during the audit process in bodies of Management Structure and Operating Structure. Findings were categorized according to level of importance to major, intermediate and minor findings. During this audit engagement we identified in total 3 findings as follows:

- **Finding No 1:** *Accounting procedures ensuring complete, accurate and transparent accounting following internationally accepted accounting principles*

**ICF requirement:** 3 (a)

**Level of priority:** Intermediate

**Body/-ies concerned by the finding:** NFD, CFCU and PWA

By the insight into bookkeeping record of the Managing and Operating structure (IAs) and relating to Country Action Programme for Montenegro for 2014 (Goal 1 - CRIS 2014/032-022 and Goal 2 - CRIS 2014/032-802), we have established the following:

Financing agreement CAP 2014 covers two goals and thus the reporting should be done per goal since different goals are financed from different financing sources (i.e. come from the different budgetary lines). Therefore, accurate financial data at the goal level should be ensured. Bookkeeping record of the Managing and Operating structure (IAs) does not give data per goal but collectively at the Program level. The reason for such record is one account at the program level. In accordance with the Article 4 of the Financing Agreement, National Fund and Operating Structure of IPA II of the beneficiary, i.e. the Contracting Authority for the program, open at least one banking account denominated in euros.

The necessity for more banking accounts depends on goals covered by the specific Financing Agreement. In case of FA which covers more than one goal, state authorities should open the appropriate number of banking accounts.

In accordance with the principles of the sound financing management, the reporting within program, including financial data, should be accurate and reliable and it is therefore important that national authorities have separate banking accounts per goal within CAP 2014.

It is also necessary to note that the first pre-financing for two goals of the Country Action Program for Montenegro for 2014 (2014/032-022 and 2014/032-803) is paid on one account.

As the bookkeeping record is the basis for annual financial reporting and financial data should be accurate and reliable, for Financing Agreement CAP 2014 with two financing sources (Goal 1 and 2), national authorities should open 2 separate banking accounts. It will allow state authorities to identify costs per goal and therefore, based on the accurate financial data to separate reporting between goals. It is necessary to note that NFD kept auxiliary record of payments per goals.

**Recommendation:** We recommend opening of another banking account for the goal 2 CAP 2014 as soon as possible and the appropriate funds for the Goal 2 should be transferred to that account. It is, thus, necessary to arrange the bookkeeping record so that the financial reporting could be per goals.

➤ **Finding No 2:***Inadequate performed control activities*

**ICF requirement:** 3 (a)

**Level of priority:** *Intermediate*

**Body/-ies concerned by the finding:** *PWA*

According to the requirements of Annex B – Internal Control Framework from Framework Agreement:

*3a (iii) "Procedures, including checklists, for each step of procurement and grant calls (e.g. technical specifications, evaluation committees, reporting of exceptions etc.) ensuring each member of staff is clear as to their responsibilities in these areas"*

*3a (xiii) "Segregation of duties ensuring that different tasks in the life of the same operation are allocated to different staff to ensure automatic cross-checking controls"*

Additionally, according to the MoP procedure V1.0, this was valid version at the time of performing contract procedures for Works contract – Rehabilitation of the railway section Kos-Trebešica:

*"Procedures specific to each type of procurement are detailed and are supported by checklists which should be applied before forwarding any documents to the EUD for ex-ante control"*

The detailed checklists are given as annexes in the MoP procedures V.1.0, depending on the type of contract.

During the audit performed and based on the insight into submitted documentation for Work contract – Rehabilitation of the railway section Kos-Trebešica, we determined the following:

- CL for Contract Notice is filled only by CM1. The CL is signed by CM1, CM2, QAS, Head of QAS but not signed by the Head of CD.
- CL for Tender Dossier is filled only by CM1. The CL is signed by CM1, CM2, QAS, but not signed by the Head of CD and Head of QAS.
- CL for EC composition is filled by CM1. The CL is signed by CM1, CM2, QAS, Head of QAS but not signed by the Head of CD.
- CL for Evaluation Report is filled by CM1. The CL is signed by CM1, CM2 QAS, Head of QAS but not signed by the Head of CD.
- CL for Contract Dossier is filled by CM1. The CL is signed by CM1, CM2 QAS, Head of QAS but not signed by the Head of CD.
- CL for Award notice is filled by CM1. The CL is signed by CM1, CM2 QAS, Head of CD but not signed by the Head of QAD.

According to the above mentioned, no check was performed adequately. Even though the segregation of duties was ensured, the procedure for cross-checking was not performed adequately.



**Recommendation:** We recommend respecting the procedures prescribed by the MoP and given Annexes, in order to ensure adequate cross-checking controls.

➤ **Finding No 3: Lack of segregation of duties**

**ICF requirements:**1(b) 3(a)

**Level of priority:**Intermediate

**Body/-ies concerned by the finding:**MF(PIU)

According to the requirements of Annex B – Internal Control Framework from Framework Agreement:

1b “Supervision by management of tasks delegated to subordinates

Ensuring that oversight procedures and structures are developed, including reporting from subordinate actors.

Ensuring that accountability is supported by proactive and continued supervision”

3a (iii) “Procedures, including checklists, for each step of procurement and grant calls (e.g. technical specifications, evaluation committees, reporting of exceptions etc.) ensuring each member of staff is clear as to their responsibilities in these areas”

3a (xiii) “Segregation of duties ensuring that different tasks in the life of the same operation are allocated to different staff to ensure automatic cross-checking controls”

According to the MoP procedure V.2.0, chapter Human resources and Internal organization functional segregation of duties has to be ensured so that the PIU could perform assigned functions.

Also, according to the MoP version V.1.0, chapter Human resources and Internal organization:

“Supervision is incorporated in operational procedures and ensured by applying »four eyes« principle and required double signature or signature by the SPO, and regular audits carried out by the responsible Internal Audit Unit.”

“Although having significant decision making rights, the SPO cannot undertake most actions on his/her own, but rather through the system of co-signature and implementation of checklists which prove the use of „4 eyes principle“.

Additionally, according to the same chapter, as well as Rulebook of Internal organization and systematization, the Ministry of Finance – Department for European integration acting as PIU, work posts Head/SPO, 1 programming manager and 2 implementation managers are foreseen.

During the audit performed and based on the insight into submitted documentation of MF/PIU we determined the following:

Only one person is employed, Head of Department/SPO;

Documents such as Annual Work Plan for 2019 and Annual Training Map for 2019 are prepared only by the SPO. However those documents are not verified or approved since the SPO is the only employee in the PIU.

Furthermore, CLs (Annex 2 of Contract Procedures) for service contracts Improvement of Budgeting System and PIFC and Improvement of Budget Department IT System are prepared and signed only by the SPO.

According to the above mentioned the segregation of duties was not ensured, nor was it possible to apply “four eyes principle” or cross-checking controls.

**Recommendation:** In order to ensure segregation of duties and four eyes principle we recommend filling the vacancies foreseen in the Rulebook of internal organization and systematization.

**4.5 Description (where applicable) of specific deficiencies related to the management of financial instruments, detected during systems audits and of the follow-up given by the national authorities to remedy these shortcomings.**

Not applicable

**4.6 Level of assurance obtained following the system audits and justification.**

Considering the assessment of the management, control and supervision systems established for IPA II CAP 2014, CAP 2016 and CAP 2017 we have reasonable grounds to state that the MCSS functions properly and in accordance with the requirements of the Framework Agreement. Our assessment of the MCSS for this Programme is **works, but some improvement(s) are needed**. Therefore, the level of assurance obtained from the system is average.

Based on the individual score for each audited system body, an overall conclusion on the MCSS of the Programmes is made. The assessment is presented in the table below:

IPA Body	Works well. No or only minor improvement(s) are needed	Works, but some improvement(s) are needed	Works partially; substantial improvement(s) are needed	Essentially does not work
NAO/NAOSO	X			
NFD		X		
CFCU		X		
PWA		X		
MF		X		
MTMA	X			
MEC	X			
MSDT	X			
CAP 2014 and CAP 2016 Follow-up		X		

## **5. AUDITS OF SAMPLES OF TRANSACTIONS**

### **5.1 Authorities/bodies that carried out the sample audits, including the audit authority**

The audit of samples of transaction in the framework of IPA II 2014-2020 for the Annual Action Programme for Montenegro (CAP 2014) was conducted by the Audit Authority of Montenegro according to updated Audit Strategy 2019-2021 for Annual Country Action Programme for Montenegro for the year 2014, Annual Country Action Programme for Montenegro for the year 2016 and Annual Country Action Programme for Montenegro for the year 2017.

### **5.2 Description of the sampling methodology applied and information whether the methodology is in accordance with the audit strategy**

The sampling was performed by the Audit Authority in accordance with the method described in the Updated Audit Strategy 2019-2021 and in accordance with the EC Guidance on sampling methods for audit authorities – Programming periods 2017-2013 and 2014-2020 (EGESIF 16-0014-01).

The population consists of declared expenditures for five actions in the reference period 01.01.2019-31.12.2019. Within these actions there was the same number of projects (actions/operations/contracts) for which the expenditures are declared. Therefore, the sampling unit for the audit of transactions for the year 2019 (reference period) was the project (action/operation/contract).

In the reference period, the total amount of EUR 673.823,58 for five projects was declared to the European Commission. Therefore, for the declared amount, the materiality level (tolerable error) is EUR 13.476,47 (2%).

Out of these five projects, one project with declared expenditure in the amount of EUR 12.025,00 (or 1,78% from the total amount), relates to the project for which the Audit Authority is also the end recipient (together with State Audit Office). Taking into account that the Audit Authority is the end recipient of the project, and the total declared expenditure for this project is below materiality (2%), we decided that it was appropriate to treat this project separately.

Therefore, we decided that we would firstly audit 100% of the remaining population, i.e. four projects with total expenditure declared in the amount of EUR 661.798,58 or 98,21% of the total population. Then, depending on the testing and the evaluation of the results of the audit of these four projects (identified error), we would consider if appropriate further audit activities would be undertaken. If no or low error was found in these four projects, which together with the declared amount for the fifth project for which the Audit Authority is end recipient was below the materiality level, i.e. less than 2%, testing would be finished, as we would have reasonable assurance that the total error was below the materiality level. If that amount was above materiality level (2%), then the testing would be extended to this remaining (fifth) contract, and the approach for the independent audit of this contract would be considered.

During the audit of these four projects in the total amount of EUR 661.798,58, which was audited 100%, one error in the amount of EUR 262,50 (0,04%) was identified.

Therefore, as the total amount of the identified error (EUR 262,50) together with the declared amount for the remaining (fifth) project for which the Audit Authority is end recipient (EUR 12.025,00) is EUR 12.287,50<sup>1</sup>, or 1,82% (less than the materiality level), we may reasonably conclude that the total declared expenditure in the reference period is free of material error, and there is no need for further audit of the expenditure declared for the project for which the Audit Authority is end recipient.

**5.3 Indication of the parameters used for statistical sampling, materiality level, the confidence level, the expected error rate applied, calculation of the required sample and the interval, sampling unit, number of sampling units in the population, number of sampling units actually audited**

Not applicable bearing in mind that AA used non-statistical method.

**5.4 Reconciliation of the expenditure declared to the Commission in the financial year to the sampled expenditure. Reconciling items include negative items where financial corrections have been made in the financial year, as well as differences between amounts declared in euro and amounts in national currency, where relevant**

For the period from 01/01/2019 to 31/12/2019, NAO submitted one Declaration of expenditure for CAP 2014 to the European Commission in total amount of EUR 673.823,58, out of which EUR 600.301,08 is EU part and EUR 73.522,50 is national co-financing.

No negative items were present in the amounts declared to the Commission during 2019.

---

<sup>1</sup> Here, just for the calculation purposes (to determine if it is necessary to audit expenditure for the remaining fifth project), we applied the most conservative (prudent) approach comprising that the whole expenditure for the remaining fifth project is non-eligible. However, in reality it is reasonable to assume that the same error rate found in the audited four projects (0,04%) would be expected in the remaining project. Therefore, when calculating the total (extrapolated) error rate for the whole population, we applied the same error rate (0,04%) identified for the audited four projects. Please see also section 5.6 below.

The population considered for drawing up the sample for the audit of operations consisted of five projects. Population is given in the table below:

<b>Sector/Action/Project/</b>	<b>Total expenditure declared (EUR)</b>	<b>Union contribution (EUR)</b>	<b>National contribution (EUR)</b>	<b>Sampled (audited) expenditure</b>
<u>Sector 1</u> <i>Democracy and Governance</i> <u>Action 1</u> <i>Support to the Tax Administration</i> <u>Project</u> <i>Support to the Tax Administration</i>	345 258,72	310 732,85	34 525,87	345 258,72
<u>Sector 1</u> <i>Democracy and Governance</i> <u>Action 2</u> <i>Improvement of the public finance management policies</i> <u>Project</u> <i>Supply for the development and strengthening of the capacities of State Audit Institution and Audit Authority</i>	12 025,00	10 822,50	1 202,50	n/a
<u>Sector 3</u> <i>Environment and climate actions</i> <u>Action 9</u> <i>Strengthening the capacity for air quality management in Montenegro</i> <u>Project</u> <i>Strengthening the capacity for air quality management in Montenegro</i>	95 000,00	80 750,00	14 250,00	95 000,00
<u>Sector 4</u> <i>Transport</i> <u>Action 11</u> <i>Development of a road network database and ma safety assessment Programme</i> <u>Project</u> <i>Study of traffic counters location</i>	4 950,00	4 207,50	742,50	4 950,00
<u>Sector 6</u> <i>Competitiveness and innovation</i> <u>Action 14</u> <i>Support to regulation of financial services</i> <u>Project</u> <i>Support to regulation of financial services</i>	216 589,86	193 788,23	22 801,63	216 589,86
<b>Total</b>	<b>673 823,58</b>	<b>600 301,08</b>	<b>73 522,50</b>	<b>661.798,58</b>

Sample size for expenditures declared was four projects (out of five projects at population).

Overall amount of sample size of four projects was EUR 661.798,58, which presents 80% of the total number of units in the population and 98,21% of total amount of declared costs.

**5.5 Where there are negative items, confirmation that they have been treated as a separate population**

Not applicable.

**5.6 In case of the use of non-statistical sampling, indicate the reasons for using the method in line with Article 12 (2) of Commission Implementing Regulation (EU) No 447/2014, the percentage of actions/operations/expenditure covered through audits, the steps taken to ensure randomness of the sample (and its representativeness) and to ensure a sufficient size of the sample enabling the audit authority to draw up a valid audit opinion. A projected error rate is calculated also in case of non-statistical sampling.**

According to EGESIF\_16-0014-01 "Guidance on sampling methods for audit authorities Programming periods 2007-2013 and 2014-2020" of 20<sup>th</sup> January 2017, the sampling unit when designing the sampling methodology may be the operation, project partner or payment claim.

In the reference period (01.01.2019-31.12.2019) the total amount of EUR 673.823,58 for five projects (actions/operations/contracts) is declared to the European Commission. Therefore, sampling unit for the audit of transactions is project. According to the fact that there is small and limited number of sampling units (five projects) in reference period, we used a non-statistical sampling method (point 4.1, 4.2, 4.3 and 6.4 of Guidance)<sup>2</sup>.

As described in more detail above in point 5.2, we audited four out of five projects. Overall sample encompassed four projects in the total amount of EUR 661.798,58, which represents 80% (4/5) of the total number of units (projects/actions/operations/contracts) in the population and 98,21% of the total amount of declared costs. Therefore, during the audit of transactions the adequate number of projects (80%) and the declared amount (98,21%) for drawing up a valid audit opinion is covered. Based on the audit results, the projected (extrapolated) error rate was calculated (please see the following 5.7 and 5.9 sections).

---

<sup>2</sup> Guidance on sampling methods for audit authorities Programming periods 2007-2013 and 2014-2020

5.7 Summary table (see below), broken down where applicable by programme indicating the eligible expenditure declared to the Commission during the year, the amount of expenditure audited, and the percentage of expenditure audited in relation to total eligible expenditure declared to the Commission for the last year, as well as the total number of sampling units in the population and the number of sampling units actually audited for the random sample.

<b>Country Annual Programme for Montenegro for year 2014</b>	
Amount of declared expenditure	673.823,58 €
No of units in population	5 operations
Value of the sample tested	661.798,58€
Value of the sample tested in %	98,21%
No of units in sample	4 operations
No of units in sample in %	80%
Materiality 2% of expenditure declared in reference period (tolerable misstatement) (673.823,58* 2%)	13.476,47
Error amount determined by the audit	262,50€
Error rate	0,04%
Extrapolated error	269,53€

Information relating to the random statistical sample is distinguished from that related to other samples if applicable (e.g. risk-based complementary samples).

Not applicable.

**5.8 Analysis of the principal results of the audits (sample items selected and audited, together with the respective amount and types of error by operation) as well as the nature of errors found, root causes and corrective measures proposed, including mitigating these errors in the future.**

The overall audit objective was to verify the legality and regularity of declared expenditures, in accordance with AA competencies established by the Law on Audit of EU Funds and functions and the responsibilities set out in Annex A of the Framework Agreement concluded between the Government of Montenegro and the European Commission (Official Gazette of Montenegro 5/2015).

The audit was performed on sample of four projects. Details about projects we have selected are given in the table below:

<b>Sector/Action/Project/</b>	<b>Total expenditure declared (EUR)</b>	<b>Union contribution (EUR)</b>	<b>National contribution (EUR)</b>	<b>Expenditure audited (EUR)</b>	<b>Audited/ Declared expenditure (%)</b>
<u>Sector 1</u> <i>Democracy and Governance</i> <u>Action 1</u> <i>Support to the Tax Administration</i> <u>Project</u> <i>Support to the Tax Administration</i>	345 258,72	310 732,85	34 525,87	345 258,72	100%
<u>Sector 3</u> <i>Environment and climate actions</i> <u>Action 9</u> <i>Strengthening the capacity for air quality management in Montenegro</i> <u>Project</u> <i>Strengthening the capacity for air quality management in Montenegro</i>	95 000,00	80 750,00	14 250,00	95 000,00	100%
<u>Sector 4</u> <i>Transport</i> <u>Action 11</u> <i>Development of a road network database and ma safety assessment Programme</i> <u>Project</u> <i>Study of traffic counters location</i>	4 950,00	4 207,50	742,50	4 950,00	100%
<u>Sector 6</u> <i>Competitiveness and innovation</i> <u>Action 14</u> <i>Support to regulation of financial services</i> <u>Project</u> <i>Support to regulation of financial services</i>	216 589,86	193 788,23	22 801,63	216 589,86	100%
<b>Total</b>					<b>100%</b>



Following bodies have been covered during the audit:

- Ministry of Finance – Directorate for Finance and Contracting of the EU Assistance Funds (CFCU) - Implementing Agency (IA);
- Ministry of Finance – PIU
- Ministry of Sustainable Development and Tourism – PIU
- Ministry of Transport and Maritime Affairs – PIU
- National Fund Division (NFD).

During the audit, we have identified and documented one transaction finding with financial impact (one error which relate to the eligibility issue and which we treated as random error). No system findings were identified.

**Finding:** Ineligible twinning management costs

**Audit area:** C - Eligibility of expenditures

**Operation:** Twinning contract-MN 14 IPAFI 0116

**Project name and number:** Support to the Tax Administration – MN 14 IPAFI 01 16

*Total amount claimed:* 345 258,72€

*EU contribution:* 310 732,85€

*National contribution:* 34 525,87€

*Amount audited:* 345 258,72€

*Ineligible expenditure:* 262,50€

According to the article 5.8.3 of the Twinning Manual as well as to the article 3.5 Twinning management Costs of the Twinning Contract Support to the Tax Administration:

“In the Budget (Annex A3) and within each activity, every budget item corresponding to fees for work performed in the BC is immediately followed by a budget item entitled ‘twinning management costs compensation’ and quantified at 150% of the preceding item. These amounts are indicative: payment will be based on the actual number of days of work performed in the BC”.

Therefore, expert has the right to twinning management cost as 150% of the fees.

For one expert, the Mission Certificate as well as supporting documentation was delivered to the CFCU for the II Interim Report. In the Mission Certificate of an expert, 4,5 days for fees (fee 350,00 €) are reported, in total amount of 1575,00 €.

Reviewing the II Interim report and supporting documents, as well as Written Approval of CFCU for II Interim Report we noticed that CFCU deemed ineligible the amount of 175,00 € (half of fee). CFCU noticed, through the checks of the exact time of arrival and departure of the expert, that he spent 4 days working in the BC instead of 4,5.

However, the CFCU did not take into account that Twinning Management costs are calculated as 150,00% of fees and did not deduct the amount 262,50 € as 150,00% of ineligible fee. It means that the declared expenditures are not fully adjusted with article 10 of Implementing Regulation 447/2014.

The amount 262,50€ (EU part 236,25€, national contribution 26,25€) is considered ineligible.

*Conclusion (including Financial consequences, if applicable):* We have determined the ineligible amount 262,50€.

*Recommendation:* The expenditure in the overall amount of 262,50€ is considered ineligible for being financed from IPA programme and should be recovered.

*Management response:*

CFCU noted the omission and deducted this expense through the Final report, which was sent to the DEU for ex-ante approval on 29.01.2020.

As we have not yet received approval from the DEU, we are not able to issue Written approval through which beneficiary will be informed in regard to the deducted ineligible amount through the Final report.

As a proof, we enclose a letter sent to the DEU with the Final report for ex-ante control.

It should be noted that conducting recovery of the ineligible amount from the beneficiary during the implementation of the project is not possible unless if it is a case of contract termination or after final payment is finalized, in this case CFCU already implemented all necessary activities (deduct ineligible amount through the Final report).

*Final conclusion:*

We will monitor the implementation of the recommendation.

**5.9 Details of the most likely error rate (total error rate) and, in case of statistical sampling method, the upper limit of the error rate as a result of the audits of operations, and the amount of irregular expenditure detected and the error rate resulting from the random sample audited.**

In the reference period the total amount of EUR 673.823,58 for five projects is declared to the European Commission. During the audit of four contracts in the total amount of 661.798,58 €, one random error in the amount of 262,50 € (0,04%) was identified. As this one error is treated as random error, it is projected (extrapolated) to the whole population, and the projected (extrapolated) error is 269,53 € (0,04%).

**5.10 Compare the total error rate with the set materiality level, in order to ascertain if the population is materially misstated or not. If so, analyse the significance of the total error rate for the audit opinion and report the recommended corrective measures.**

Based on the audit work performed we have obtained reasonable assurance that the expenditure declared in the amount of 673 823,58 € in the period 01/01 – 31/12/2019 is in all material aspects, legal and regular, except expenditures described in the point 5.8. When evaluating the results of the audit of operations, the total projected (extrapolated) error rate is 0,04% which is below the materiality threshold (2%).

**5.11 Corrections relating to the current year implemented by the operating structure/management structure before submitting the final declaration of expenditure and financial statements to the Commission, and resulting from the audits of operations, including flat rate or extrapolated corrections.**

During the audit of transactions one error in the amount of EUR 262,50 € (EU part 236,25 €, national contribution 26,25 €) was identified. However, due to the fact that the audit report was issued on 20<sup>th</sup> February 2020, financial corrections have not been made in the current financial year (please see also section 6.3 of this AAAR).

**5.12 Residual total error rate following the implementation of the above-mentioned corrections and significance for the audit opinion.**

As mentioned above in section 5.11, due to the fact that the financial correction is not implemented in the current financial year, residual total error rate is the same as projected (extrapolated) error rate (269,53 € or 0,04%).

**5.13 Information on the results of the audit of the complementary (e.g. risk based) sample, if any.**

Not applicable.

**5.14 Information on the follow-up of irregularities, including revision of previously reported residual error rates, as a result of all subsequent corrective actions.**

Not applicable.

**5.15 Details of whether any problems identified were considered to be systemic in nature, and the measures taken, including a quantification of the irregular expenditure and any related financial corrections.**

Not applicable.

**5.16 Description (where applicable) of specific deficiencies or irregularities related with financial instruments. Where applicable, indication of the sample error rate concerning the audited financial instruments.**

Not applicable.

**5.17 Analysis of the principal results of the audits of negative items, including conclusions as to whether the negative items audited correspond to the decisions of the country or of the Commission, and reconcile with the amounts included in the accounts on amounts withdrawn and recovered during the year and amounts to be recovered at the end of the year.**

Not applicable.

**5.18 Conclusions drawn from the results of the audits with regard to the effectiveness of the management and control system.**

The conclusions of the audit are based on the information and documents gathered during the audit from beneficiaries and management, control and supervision system bodies, interviews conducted in the audited bodies and tests performed following the working papers and checklists for specific audit areas. Based on the audit work performed we have obtained reasonable assurance that the expenditure declared in the amount of 673 823,58€ in the period 01/01 – 31/12/2019 is in all material aspects, legal and regular.

In accordance with the prescribed methodology for system audits, the AA has assessed the MCSS in Category 2 ('works, but some improvements are needed'). When evaluating the results of the audit of operations (transactions) and taking into account that the determined error rate is 0,04% (which is below the materiality threshold of 2%), it can be concluded that the results of the system audit is confirmed by the result of the audit of operations (transactions).

## **6. AUDITS OF THE ANNUAL FINANCIAL REPORTS OR STATEMENTS/ANNUAL ACCOUNTS**

### **6.1 Indication of the authorities/bodies that have carried out audits of the annual financial reports or statements/annual accounts.**

In accordance with the Update Audit Strategy for the IPA II 2014-2020 for the Annual Country Action Programmes for Montenegro for the years 2014, 2016 and 2017 submitted to European Commission - DG Near 13<sup>th</sup> May 2019 the Audit Authority of Montenegro has carried out an audit of completeness, accuracy and veracity of the annual financial reports or statements (audit of accounts) for above mentioned programmes for the reference financial year 2019, i.e. the accounting year from 1<sup>st</sup> January to 31<sup>st</sup> December 2019, issued by NAO on 14<sup>th</sup> February 2020 (Final Report on Audit of Accounts).

### **6.2 Description of audit approach used to verify the elements of the annual financial reports or statements/annual accounts defined in Article 12(2) and Article 23(1)(b) of Commission Implementing Regulation (EU) No 447/2014.**

In the context of the audit of accounts, and for the purposes of the audit opinion, in order to reach a conclusion on the completeness, accuracy and veracity of the annual financial reports or statements, the Audit Authority verifies whether all submitted accounting information to the Commission is correct and includes assessment whether the annual financial reports or statements/annual accounts are prepared, in all material respects, in accordance with the applicable financial reporting framework.

In order to achieve the overall objective, the Audit Authority took into account the results from the system audits regarding effective and efficient functioning of the management, control and supervision system (MCSS) in the process of preparing and submitting of the Annual Financial Report (AFR) carried out in the National Fund Division (NF) and Implementing Agencies (CFCU and PWA) as well as the results of the audit on operations for CAP 2014.

For the purpose of expressing the Annual Audit Opinion, in order to conclude that the Annual Financial Report gives a true and fair view, the Audit Authority verified that all elements required by models stipulated in Annex IV of the Financing Agreements concerning the CAP for the year 2014, 2016, and 2017, i.e. cumulative amounts declared from the Programme's, are correctly included in the accounts and correspond to the supporting accounting records maintained by bodies in the National Fund Division (NF) and Implementing Agencies / Directorate for Finance and Contracting of the EU Assistance Funds (CFCU) and Public Work Administration (PWA).

The Audit Authority, on the basis of the Annual Financial Report as well as all required documentation, provided to it by the National Fund Division (NF) and Implementing Agencies/ CFCU and PWA verified that:

- the total amounts submitted in the Annual Financial Report (contracted and addendums signed, amounts disbursed, total costs recognised, amounts of open pre-financing, invoices received, payments made and recoveries requested, and the relevant percentages based on appropriate total amounts submitted to the Commission in accordance with the Annex IV of the Financing Agreements) correspond to the amounts entered in the accounting systems of NF and IAs;
- the total amounts submitted in the Annual Financial Report correspond to the amounts in the electronic database for each contract
- the bank accounts statement for each programme balances corresponds to the year-end balances in the accounting systems of the National Fund Division (NF);
- Reconciliation of the accounting records and cash flow statements of the NF and Implementing Agencies.

Total amounts of recoveries correspond to supporting documents.

**6.3 Indication of the conclusions drawn from the results of the audits in regard to the completeness, accuracy and veracity of the declaration of expenditure and financial statements, including an indication on the financial corrections made and reflected in the declaration of expenditure and financial statements as a follow-up to the results of the audit on transactions/operations.**

The Audit Authority engagements (audit of operations) have resulted in financial corrections regarding the reference period for CAP 2014. The audit finding issued within the Audit of operations report No: 3011-2-06-71/3 from 20<sup>th</sup> February 2020, with financial correction in amount of 262,50€ (EU part 236,25€, national contribution 26,25€). Bearing in mind that Final Report on audit of operations was issued on 20<sup>th</sup> February 2020, annual accounts are not corrected in relation with determined financial correction by AA. Therefore, this financial correction must be included in next declaration/financial reports.

Audit conclusion is based on the analysis of procedures, information, data, documents, reports, adequately documented in check lists and working papers related to the audit of accounts.

Based on the above mentioned, we conclude that the annual accounts (financial reports and statements) submitted to the European Commission for financial year 2019 for CAP 2014 (2014/032/022 and 2014/032-803), CAP 2016 (2016/037-896), and CAP 2017(2017/040-216 and 2017/039-816)are complete, accurate and veracious in all material aspects. Financial reports and statements have been prepared in accordance with the requirements.

**6.4 Indication of whether any problems identified were considered to be systemic in nature, and the measures taken.**

Not applicable.

## **7. FOLLOW-UP OF PREVIOUS YEARS' AUDIT ACTIVITY**

### **7.1 Information on the follow-up of outstanding audit recommendations and on the follow-up of results of systems audits and audits of transactions/operations (including the audits done in regard to the complementary sample) from earlier years.**

According to the AA's Manual of Procedures "The objective of the follow-up process is to determine whether the issues rose in the audit have been adequately addressed and the audit report recommendations are implemented in a timely manner. In general, the follow-up of the audit findings and errors shall be performed annually and the information provided in the Annual Audit Activity Report. The follow-up can be performed as a part of another audit engagement, or as a separate activity before issuing the Annual Audit Activity Report and Annual Audit Opinion. Follow-up by AA is defined as a process by which it determines the adequacy, effectiveness, and timeliness of actions taken by management on reported errors and audit findings, including corrective and preventive measures applied, application of any financial adjustments and remedial action plans. AA should ascertain that actions taken on audit findings remedy the underlying conditions. The same standards for audit evidence shall be applied to follow-up work as those used for documenting original audit work. The results of the follow-up shall be documented in the "Audit recommendation status report".

During system audit in 2019, the follow-up of findings and recommendations from previous audit was performed, and the result of the follow-up is the constituent part of system audit report. Therefore, the follow up as a part of system audit in all bodies was performed regarding the findings and recommendations given in system audit report conducted in these bodies during 2017 and 2018. After receiving the responses and the documentation on the fulfilment of recommendations from all bodies, we conducted interviews with the employees responsible for the management and implementation of the operational programme in bodies in which the interview was needed. After analyses and reviewing the submitted documentation, we assessed the status of the individual recommendation with the respective explanation.

In the period November – December 2019 the AA performed follow-up of the findings and recommendations that remained opened from the previous audits. Results of performed follow-up are that 4 out of 9 findings are closed, and given as follows:

#### **Results of performed follow-up – closed findings (4)**

- Written Procedures related to chapter Annual Management Declaration
- Planning of EU and national contributions
- Written Procedures related to chapter Financial management
- Organising of Monthly Meetings with SPOs/PIUs

#### **Results of performed follow-up – still open findings (5)**

- Lack of staff, recruitment and retention policy
- IT Policy - Backup of data
- Contingency plan developed
- Internal audit capacities
- Reports on implementation

Further below we outline the description of the most important findings identified and conclusions reached through audits, recommendations provided for correcting the findings as well as information on the measures undertaken for the purpose of resolving the findings with regards to the audited processes and individual bodies and authorities within the system.

Principal findings identified in the particular audit areas are as follows:

- **Written Procedures related to chapter Annual Management Declaration**

**ICF requirement:** 3 (c) Policies and procedures related to control activities

**Level of priority:** Minor

**Body/-ies concerned by the finding:** all IPA bodies

During the audit engagement we determined that AMD Check lists for NAO and IPA Bodies are not harmonized with the procedures described in the MoP

The Annexes 5 and 6 of the MoP (Chapter Annual Management Declaration – AMD), Checklist for the NAO and AMD Checklist for the Head of the IPA OS Body are not in line with the procedures described in the MoP. Template for Check list does not cover all relevant resources which need to be used. It does not contain the KPI and the verifications performed by NAO as resources. It means that there are no adequate trails that those two resources are also used.

We recommended harmonizing template with procedures in a way that the checklist contains all relevant resources.

*The chapter Annual Management Declaration and the Annexes 5 and 6 are harmonized. We consider this finding **closed, with one comment.***

*The CL for Head of IPA body (Annex 6) consists the check “The Heads of IPA OS Bodies AMD Checklists have been filled-in, approved and signed.” which is related to the same CL. Therefore, it would be desirable to remove this check from the CL.*

- **Planning of EU and national contributions**

**ICF Requirements:** 1 (c) Establishment of structures, reporting lines, and authorities and responsibilities; 3 (a) Selection and development of control activities

**Level of priority:** Minor

**Body/-ies concerned by the finding:** CFCU

During the audit performed we determined that specific operational procedures in respect to planning of EU and national contributions are not fully implemented and respected by relevant authorities.

The Head of CFCU submitted to the SPO/PIUs request with relevant documentation in respect to process of issuing Budget plan. Based on the insight into submitted documentation by SPO in the PIU/Ministry of Economy and PIU/Ministry of Finance, it is evident that Checklists for Three Years Disbursement Forecasts (which are main part of supporting documents) have not been submitted to the Head of CFCU.

Procedures in respect to submission of documents for final approval to the relevant authorities are generally respected. CFCU staff performed controls, prepared Request for allocations of budgetary funds and submitted it to the relevant authorities. It is evident that Checklists for Request for allocation of budgetary funds have been prepared and signed in accordance with the written procedure. Nevertheless, they have not been submitted, as part of documentation package, to the NAO and Budget Directorate.

Additionally, SPOs/PIUs have not been informed about Final Budget plan by CFCU (Notification letter in respect to planning of EU contributions).

Inadequate application of defined procedures in respect to financial management may cause deficiencies and non-proper flow of information between relevant entities.

We recommended respecting written procedures in respect to the planning of EU and national contributions.

*By reviewing the submitted documentation, we found that the IA, in process of planning budget for year 2020, followed the procedures required by the Manual of procedures (Chapter "Financial Management", version 2.0). We have noticed that the IA submitted all documentation and information to all participants involved in the planning of the annual budget, as prescribed in the manual. Also, the IA submitted to the NAO the final budget information agreed with the Budget Directorate. **We consider this finding closed.***

- **Written Procedures related to chapter Financial management**

**ICF requirements:** 3 (a) Selection and development of control activities; 3(c)(1) Ensuring that written policies and procedures exist establishing what is expected at all levels and specifying detailed actions; 4(a)(1) Ensuring that processes are in place at all levels to identify the information required and expected to support the functioning of the other components of internal control and the achievement of the organisation's objectives.

**Level of priority:** Intermediate

**Body/-ies concerned by the finding:** NF/IAs/PIUs

During audit we identified that MOP chapter Financial management with annexes has some deficiencies:

The new information system developed within MCS which includes procedures for financial management and accounting are not aligned with MOP chapter financial management which has been in usage during audit.

According to the MOP, for the purpose of monthly reconciliation (page 6 of MOP of IA, paragraph note) "State Treasury Directorate prepares and submits to the IA filtered report related to the transactions i.e. payments of the IA during the day" which is not in line with the Directions on State Treasury Operations (OG MN No. 20/14).

Our recommendation was to align procedures with new information system and relevant regulation.

*The new version 2.0 MoP was introduced on July 1 this year. The new manual is in line with the established Information System in practice for IPA II (SAP system). In addition, we found that the sentence, "State Treasury Department prepares and submits to filtered PU report related to transactions i.e. IA payments during the day" (Chapter FM, MoP version 1.0) related to the work of State Treasury Directorate, had been removed from Chapter, Financial Management. **Based on the above, we consider this finding closed.***



- **Organising of Monthly Meetings with SPOs/PIUs**

**ICF requirement:** 5 (a) *On-going and specific monitoring*

**Level of priority:** *Intermediate*

**Body/-ies concerned by the finding:** *NIPAC Office*

According to the Article 9 of the Decree on organisation of the indirect management for implementation of Union financial assistance under Instrument for pre-accession assistance NIPAC Office organises monitoring meetings with the PIUs to discuss the actual progress of actions implementation against planned and monitoring visits. MoP Chapter Programme/Action Monitoring in details prescribes procedures related to NIPAC Office responsibilities in order to organise monthly meetings with the SPOs/PIUs. During the audit performed and based on the insight into submitted documentation, we determined that monthly meetings have not been organised by NIPAC Office. Inadequate application of defined procedures in respect to organising monthly meetings may cause deficiencies and non-proper flow of information between relevant entities and may cause delays in identification of potential risks and problems that may occur. All relevant information must be distributed to all interested parties in order to ensure efficient and effective system functioning.

We recommended that Head of NIPAC Office organise regularly monthly meetings with SPOs/PIUs.

*The new version (V2.0) of Manual of Procedures has been in use since 01/07/2019. The Chapter, Program/Action monitoring, is changed and instead of a monthly coordination meeting, NIPAC and PIUs will have Quarterly Coordination meetings. Based on the documentation submitted, quarterly coordination meeting was held, after adoption of new version of MoP. **Based on the above, we consider this finding closed.***

- **Lack of staff, recruitment and retention policy**

**ICF requirement:** 1 (d) *staff planning, recruitment, retention, training and appraisal*

**Level of priority:** *Intermediate*

**Body/-ies concerned by the finding:** *all IPA bodies*

During the audit we determined, based on the internal acts on systematisation and organisation of job positions and WLA that in all bodies of managing and operating structure, dealing with OP - Annual Country Action Programme for Montenegro for the year 2014, the number of permanently employed executors is insufficient. We also noted difficulties in retaining staff who during the work in bodies acquired appropriate knowledge and experience.

During the audit we noticed that there have been changes on key positions in IPA bodies. Apart from the above stated, we determined a significant employees' turnover during 2016 and 2017 in all IPA bodies, dealing with CAP 2014. It ultimately leads to the fact that particular IPA bodies function based on substitution plans while at some of them, because of the insufficient number of staff it is impossible to apply substitution plan in order to respect segregation of duty.

Envisaged work posts related to IPA jobs by Rulebook, result of WLA/2017 and number of the currently employed on the date of the audit is given in the table below:

Auditee	Envisaged Work post related to IPA jobs by Rulebook	Result of WLA/2017	Currently employed
NF/NAOSO	8 - including NAO	10	7 (LTEC)
NIPAC Office	11 - Including NIPAC	9 <sup>3</sup>	7 (6 – LTEC, 1-TEC)
CFCU	21 - Including Head of IA	37	19 (18-LTEC; 1-TEC)
DPW	30 - Including Director (Head of IA)	27	22 (21-LTEC;1-TEC)
MF	4 - including SPO	4	3(LTEC) <sup>4</sup>
MSDT	8 - including SPO	8	6 (5-LTEC;1-TEC)
MTMA	5 - Including SPO	7	3 (LTEC)
MEC	5 - including SPO	5	5(3-LTEC; 2-TEC)

Our recommendation was to take necessary measures and accelerating activities with a view to recruiting lacking number of employees which would further influence better and more efficient management and use of IPA funds. In order to prevent outflow of the key employees and problems created by their leave from IPA bodies, it is necessary to develop factually established policy of staff retention. Such policy would improve systems of promotion, award, professional training as well as other aspects of work. Therefore, we recommend making of additional efforts in order to establish policy of staff retention which can respond to the expected scope of work and fluctuation of employees.

*According to the responses from the auditees and available documentation the envisaged work post related to IPA jobs by Rulebooks, result of WLAs and number of the currently employed is given in the table below:*

Auditee	Envisaged work post related to IPA jobs by Rulebook	Result of WLA/2019	Currently employed
NF/NAO SO	13 - including NAO	13	11 (8- LTEC;3 TEC)
NIPAC Office	12 - Including NIPAC	12	10 (9 – LTEC; 1-TEC)
CFCU	37 - Including Head of IA	37	31 (20-LTEC;11-TEC)
DPW	39 - Including Director (Head of IA)	39	31 (16-LTEC;15-TEC)
MF	4 - including SPO	4	1 (LTEC)
MSDT	9 - including SPO	9	6 (5-LTEC;1-TEC)
MTMA	6 - Including SPO	6	6 (5 – LTEC;1-TEC)
MEC	5 - including SPO	5	4 (3-LTEC; 1-TEC)

*In comparison, we noticed that the number of work posts envisaged in the Rulebooks of IPA Bodies increased or remained the same, as well as in WLAs for 2019.*

*Also when we compare the situation in 2017 (when the finding was determined) and results of follow up, the number of employees in IPA bodies increased, except for the Ministry of Finance (PIU) where the situation is very risky since there is only one employee.*

*The progress is evident in the most of the auditees, since the auditees beside other efforts, undertake measures in order to mitigate risk of lack of employees and engage additional staff. However, the significant number of employees is employed on temporary basis contracts, which is acceptable to mitigate the risk of lack of employees for a short time, but not as a permanent solution.*

**Finding remained open with the intermediate level of priority, except Ministry of Finance where we increased the level of priority to High.**

*The significant efforts were evident in the field of retention policy. Since the Decision on the addendum on basic salary for work posts in indirect/direct and shared management of pre-accession assistance (IPA) is adopted by the Government and its implementation started in March 2019, we consider this part of the finding closed.*

- **IT Policy - Backup of data**

**ICF requirement:** 3 (b) Security control activities

**Level of Priority:** Intermediate

**Body/-ies concerned by the finding:** all IPA bodies

On the basis of performed on-the-spot checks and conducted interviews, we have found that archiving and backup of data is not performed in accordance with prescribed procedures. There is no properly defined back up storage. So, there is a risk of loss of data in case of error in information systems in which information is destroyed by failure or negligence in storage, transmission, or processing. To mitigate the risk of losing data, the staff from IPA bodies use external hard disks and USB disks for archiving data from their computers. They perform this periodically. Previously mentioned external hard disks are stored in the premises of each IPA body. However, archiving data in this way is not secure enough and is not in accordance with prescribed procedures for back up and archiving data which are described in MoP, chapter IT policy.

We recommended providing adequate archiving and back-up of data according to the procedures described in MoP Chapter IT policy in order to prevent data loss or ensure restoring of lost data.

*Action Plan ISO 27002 which contains integrated measures related to adequate information security asset management, information security awareness and trainings in this respect as well as business continuity management and back-up, has been submitted to the EC for final comments and opinion before Government adoption which is expected in December 2019.*

*Significant efforts, in order to provide the above mentioned, are evident. Besides that, this **finding remains open**, since the AP has not been adopted yet.*

- **Contingency plan developed**

**ICF requirement:** 3 (a) (viii) Procedures for continuity of operations ensuring that significant risks to continuity (e.g. concerning loss of data, absence of individuals etc.) are identified and contingency plans put in place

**Level of Priority:** Intermediate

**Body/-ies concerned by the finding:** all IPA bodies

*According to the Article 34 of the Government Decree for Information security (OG MNE No. 58/10; 55/15), business continuity plan should be developed and approved.*

All bodies of Operating Structure and Management structure of IPA II do not have contingency plan developed. There is a risk for continuity of operations concerning loss of data, absence of individuals, and some other unpredictable situations.

Our recommendation was to develop the contingency plan with clear responsibilities and procedures.

*Business contingency plan will be part of the Action Plan, which has not been adopted yet. **Finding remains open.***

- **Internal audit capacities**

**ICF requirement:** 5 (a) On-going and specific monitoring

**Level of priority:** Intermediate

**Body/-ies concerned by the finding:** MSDT/MTMA/MEC/MF/CFCU/NF

During audit we identified that there is a lack of capacities within IADs in all IPA bodies and this fact may have an impact on the quantity and/or quality of audits that are envisaged in annual audit plans. There is a risk that some of the systems, processes or procedures with high impact on overall system will not be subject of the audit and that managers would not have additional assurance about functioning of their systems or independent review on effectiveness and efficiency of the system.

Our recommendation was related to increasing capacities of internal audit in order to ensure timely and effective execution of internal audit function described in their procedures and plans and with a view to increasing coverage of audit areas which has a high impact on implementation of IPA funds.

*Decree on establishment of the Internal Audit in the Public Sector was adopted by the Government on the session held on November 21<sup>st</sup> 2019. By the provisions of this Decree Ministry of Finance will be in charge to determine separate Internal Audit Unit in charge of audit of EU funds, which shall cover all line ministries involved in indirect management and their work shall be coordinated by NAO.*

*By the provisions of this Decree Ministry of Finance will be in charge of determining separate Internal Audit Unit in charge of audit of EU funds, which shall cover all line ministries involved in indirect management and their work shall be coordinated by NAO.*

*Significant progress is made, especially with the new Decree on establishment of the Internal Audit in the Public Sector and its provisions to determine separate Internal Audit Unit in charge of audit of EU funds.*

*The finding remains open, we will further monitor the implementation of the above mentioned.*

- **Reports on implementation**

**ICF requirement:** 5 (a) On-going and specific monitoring

**Level of priority:** Intermediate

**Body/-ies concerned by the finding:** NIPAC, Head of NIPAC Office, SPOs

During the audit performed and based on the insight into submitted documentation, we determined that procedures in respect to preparation of Annual Implementation Report for 2016 have not been fully implemented and respected. Namely:

Annual Implementation Report for 2016 was prepared and submitted to the European Commission in prescribed deadline (by 15<sup>th</sup> February 2017). However, Annual Implementation Report for 2016 has not been submitted for the reviewing and examination to the Sectoral Monitoring Committee and IPA Monitoring Committee by NIPAC Office;

Annual Implementation Reports for 2016 have not been prepared based on all information, which should be submitted by SPOs/PIUs (Quarterly and Semi-Annual Monitoring Reports have not been prepared).

During 2016 Semi-Annual Implementation Reports have not been prepared by NIPAC Office;

In addition to the above, it is evident that procedures in respect to quality information checks and coordination of the reporting requirements have not been implemented. Namely, Quarterly and Semi-Annual monitoring Reports Checklists have not been prepared and signed and Time-Schedule, Guidelines and Instructions have not been issued and submitted to the SPOs/PIUs by NIPAC Office.

We recommended respecting procedures in relation to the preparation and submission of Annual Implementation reports, as well as improving communication between NIPAC Office and PIUs.

*Based on the review of the submitted documentation and the conducted interview, we have determined that the procedures related to the preparation of the Annual Implementation Report are still not respected. The Annual Implementation Report for 2018 has been prepared and submitted on time. However, we note that when drafting the Annual Implementation Report, the procedures from the manual and are still not followed. The 2018 Annual Implementation Report has not been submitted for review to the Sectoral Monitoring Committee and the IPA Monitoring Committee by NIPAC and also this report does not contain information received from PIUs (Quarterly and Semi-Annual Monitoring Reports). The semi-annual implementation reports for 2019 have not been prepared by the NIPAC Office, because Quarterly Monitoring Reports are not submitted by PIUs. We consider this **finding open**.*

## **7.2 Subsequent events affecting the previous opinion and the previous annual audit activity report under Article 12(3) of Commission Implementing Regulation (EU) No 447/2014**

Not applicable.

## **8. OTHER INFORMATION**

Not applicable.

## **9. OVERALL LEVEL OF ASSURANCE**

### **9.1 Explanation on how the overall level of assurance on the proper functioning of the management and control system is obtained from the combination of the results of the system audits and audits of operations**

The assurance on the proper functioning of the management and control system is based on the combined results of both the system audit (system assessment – please see section 4 above) and the audit of operations (total error rate – please see section 5 above).

As a result of the system audit (and taking into account the results of the follow-up of the findings from previous years), the management, control and supervision system established for IPA II CAP 2014, CAP 2016 and CAP 2017 is assessed as works, but some improvement(s) are needed. The positive assessment resulting from the system audit is confirmed also by the results of the audit of operations, as the determined total error rate is below materiality level. Therefore, as the management, control and supervision system works and the total error rate is below the materiality level, it is appropriate to issue an unqualified opinion on the proper functioning of the system and on the legality and regularity of expenditure.

The assurance on the accounts is based on the results of the audit of accounts as described in section 6.3 of this AAAR. Therefore, as it is concluded that the annual accounts (financial reports and statements) are complete and give a true and fair view, it is appropriate to issue an unqualified opinion on the reliability of the annual financial reports or statements/annual accounts.

**9.2 Where the total error rate relating to the expenditure declared in the payment claims in a year is above the materiality level, analyse its significance and assess whether this indicates a serious deficiency(ies) in the functioning of the relevant management and control system during the year. Where relevant, take also account of the results of other national or Union audit work carried out in relation to the year.**

Not applicable.

**9.3 Assessment of the corrective action necessary both from a system and financial perspective.**

The audit entity announced an improvement in its responses to the identified findings and recommendations in the System Audit and Audit Operations Reports. The further implementation of the recommendation will be monitored.

**9.4 Assessment of any relevant subsequent adjustments made and corrective actions taken such as financial corrections included in the declaration of expenditure and financial statements and assess the residual error rate and the need for any additional corrective measures necessary both from a system and financial perspective.**

Bearing in mind that Final Report on audit of operations was issued on 20<sup>th</sup> February 2020, which resulted in a financial correction of 262.50€, annual accounts are not corrected in relation to determined financial correction by AA. Therefore, this financial correction must be included in next declaration/financial reports. The further implementation of the recommendation will be monitored.

# 10. TABLE FOR DECLARED EXPENDITURE AND SAMPLE AUDITS

			A	B		C	D	E		F	G	H=F-G	GI	JH
Fund	Reference (CCI)	Programme	Expenditure declared to the Commission in reference to the year	Expenditure in reference to financial year audited for the random sample		Total number of units in the population	Number of sampling units for the random sample	Amount and percentage (error rate) of irregular expenditure in random sample		Total projected error rate	Corrections implemented as a result of the total error rate	Residual total error rate	Other expenditure audited	Amount of irregular expenditure in other expenditure sample
				Amount	%			Amount	%	%				
	C(2014) 9387	Annual Country Action Programme for Montenegro for the year 2014	673 823,58	661.798,58	98,21	5	4	262,50	0,04	269,53	0,00	/	n/a	n/a
	C(2016)8226	Annual Country Action Programme for Montenegro for the year 2016	/	/	/	/	/	/	/	/	/	/	/	/
	C(2017) (2017/040-216 and 2017/039-816)	Annual Country Action Programme for Montenegro for the year 2017	/	/	/	/	/	/	/	/	/	/	/	/