



**MONTENEGRO**  
**AUDIT AUTHORITY**

No: 3016-06-129

**ANNUAL AUDIT ACTIVITY REPORT**  
**OF THE AUDIT AUTHORITY**  
**FOR PROGRAMME**  
**AGRICULTURE AND RURAL DEVELOPMENT OF**  
**MONTENEGRO - IPARD II**

FOR THE PERIOD FROM 01 JANUARY UNTIL  
31 DECEMBER 2019

Podgorica, March 13<sup>th</sup>, 2020

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## **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 Law on Audit of EU funds, the AA is functionally and operationally independent of all of other stakeholders involved in the system of EU funds management and control.

The Law on Audit of EU Funds prescribes that auditees are public authorities and organizations, bodies and organizations of local government units, natural persons and legal entities receiving, using or managing EU funds.

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.

This report has been prepared solely by the Audit Authority of Montenegro, department for audit of agriculture and rural development fund, following the Annex D Annual Audit Activity Report (AAAR) of the FWA.

### **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<sup>st</sup> January to 31<sup>st</sup> December 2019.

The audit activities performed in the audit period for the financial year were governed by the Audit Strategy. Audit period began on 18<sup>th</sup> April 2019, and ended on 4<sup>th</sup> March 2020, when the last audit report was issued together with the finalization of activities on verification of the management declaration, audit of annual accounts and finalization of follow up activities.

For the reference period the following audit activities were performed: System Audit, Audit of transactions/operations, Audit of Accounts including verification of AMD and Follow-up activities.

**In the context of system audit**, in accordance with the Audit Strategy 2019-2021, AA performed system audit with objective to determine whether the MCS established in the Managing Authority, IPARD Agency, NF and NAO support office, for financial year 2019, is in line with the requirements set out in the Implementing Regulation 447/2014, Framework Agreement, Sectoral Agreement, Financing Agreement and IPARD Programme as well as other underlying regulations and to verify the efficient and effective functioning of the management, control and supervision systems. System Audit of MCS was based on written procedures (test of procedures) and compliance testing (test of controls) in DMS (NAO/SO and NF), Managing Authority and IPARD Agency. Following audit areas were examined:

No	Scope of the audit		
	Assessment criteria and sub criteria (ICFR) (AC)	Auditee	Process / sub-process
1.	1(a,b,c,d,e)	NAO/SO, NF, MA, IA	Human resources
2.	2 (a,b)	NAO/SO, IA	Risk management
3.	3(a)	NAO/SO, NF	Verifications checks, Financial Management and Accounting
4.	3(a,b)	IA	IT Policy, Authorisation of projects, Authorisation of payments, Execution of payments, On the spot control and Accounting.
5.	4(a,b,c)	MA	Monitoring, evaluation and reporting; Programming; Coordination and public relations.
6.	5(a,b)	IA	Internal audit
7.	5(a,b)	NAOSO	AMD

**In the context of audit of operational transactions**, in accordance with the Audit Strategy 2019-2021, AA performed test of transactions with objective to confirm the legality and regularity of declared expenditures in financial year 2019. This was achieved through two audits of operation, one related to the first three quarters (D1 – Q1, Q2 and Q3) and second related to last quarter (D1 – Q4).

Seq. Number	Public Call	Quarter in 2019	Number of executed payments in quarter	Amount of executed payments (EU + National part) €	Amount of executed payments (EU/IPA part) €
1	2	3	4	5	6
1	First call M1	Q1	1	7.302,48	5.476,86
2	First call M1	Q2	0	0,00	0,00
3	First call M1	Q3	1	312.418,96	234.314,22
4	First call M1 First call M3	Q4	6	1.503.213,27	1.127.409,95
<b>Total</b>			<b>8</b>	<b>1.822.934,71</b>	<b>1.367.201,03</b>

Considering the small number of items (executed payments), for audit of operations AA did not apply any sampling method and audits covered 100 % of expenditures declared. In addition there were not any negative amounts during the FY 2019 and consequently gross declared expenditures are equal to the net declared expenditures.

**In the context of audit of accounts**, in accordance with the Audit Strategy 2019-2021, AA performed comprehensive reconciliation with objective to confirm the completeness, accuracy and veracity of the annual accounts.

**In the context of follow up**, in accordance with the Audit Strategy 2019-2021, AA performed follow up on recommendations issued in AAAR for 2018 as well as on the remaining recommendations from DG AGRI Final Report in line with the letter of closure with recommendations from 25<sup>th</sup> October 2017, on observations and recommendations issued by DG AGRI letter from 16<sup>th</sup> February 2018 and on observations and recommendations issued by DG AGRI letter from 22<sup>nd</sup> November 2019 related to substantial changes of version 2.0 of IPARD Agency's working arrangements.

### **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 the Programme for the Development of Agriculture and Rural Areas in Montenegro (hereinafter: IPARD II Programme) for period 2014-2020.

The IPARD II Programme for Agriculture and Rural Development for Montenegro for 2014-2020 was adopted by Commission Implementing Decision C(2015)5074 of 20 July 2015 and the total indicative costs for the implementation, including EU, national and private contributions, amount to EUR 86.8 million for the period 2014-2020, while the indicative contribution of the EU is € 39 million.

The IPARD II Management and control system has been entrusted with budget implementation tasks under the following measures of the IPARD II Programme:

- Investments in physical assets of agricultural holdings;
- Investments in physical assets concerning processing and marketing of agricultural and fishery products.

Structures and bodies being part of the Management and control system for IPARD II Programme are, as follows:

- The National IPA Coordinator (NIPAC)
- The National Authorizing Officer (NAO)
- The Management Structure (DMS):
  - The National Fund (NF)
  - The NAO support office (NAOSO)
- The Operating structure:
  - Managing Authority (MA)
  - IPARD Agency (IA)

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

To prepare the Annual Audit Activity Report, the Audit Authority processes, summarises and assesses the findings and recommendations included in the reports on performed audits and carries out a follow-up to assess the time proportional to implementation of action plans prepared on the basis of audit recommendations.

The Annual Audit Activity report sets out, inter alia, any deficiencies found in the management, control and supervision systems and any corrective measures taken or planned by the NAO, management structure and/or the operating structures concerned, and details of any substantial changes in the management and control system.

In accordance with Art.59 (2) of the Framework Agreement between the Commission and Government of Montenegro, for the Programme IPARD II the NAO has submitted the Annual Management Declaration and Annual financial report for 2019<sup>1</sup> to the Commission with a copy to the NIPAC and AA.

With a view to drawing up an audit opinion, Audit Authority assessed results of audit activities from the performed audits of management and control system, audits on legality and regularity of transactions, audits of completeness and accuracy of annual accounts and assessed the consistency of the management declaration with regard to performed audit work.

Based on the available information the AA prepares the Annual Activity Audit Report and the Annual Audit Opinion.

The AA 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<sup>th</sup> of March each year.

## 2. SUBSTANTIAL CHANGES IN MANAGEMENT AND CONTROL SYSTEMS

### 2.1 Details of any substantial changes in the management and control systems and dates from which these changes apply, as well as the impact of these changes on the audit work

During 2019, the NAO regularly informed the European Commission and Audit Authority about substantial and planned changes in the system.

Changes in management and control system during the reference period are as follows:

- **Key staff**
  - Mr Bojan Vujović was appointed as **Head of NIPAC Office** (Decision on appointment No. 01-004-574 from February 11<sup>th</sup> 2019)

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<sup>1</sup> On 14th February 2020 (Ref. 01-2291/4)

- Ms Ivana Vujošević was appointed as **Deputy of National IPA Coordinator** (Decision on appointment No. 01-004-813 from March 19<sup>th</sup> 2019)
- Mr Velibor Damjanović was appointed as **Head of NAO Support Office** (Decision on appointment No 01-1/48 from April 1<sup>st</sup> 2019)
- Mr Blagota Radulović terminated his engagement as **Head of the Directorate for Payments (IPARD Agency)** within MARD (Change occurred on Government session held on November 28<sup>th</sup> 2019)
- Ms Danka Perović started her engagement as **acting Director General in the Directorate for Payments (IPARD Agency)** within MARD (Change occurred on Government session held on November 28<sup>th</sup> 2019)
- **Manual of procedures**
  - **Manual of Procedures v. 1.2** for IPARD II Programme for measures 1 and 3 was adopted on July 8<sup>th</sup> 2019.
- **Legal acts**
  - **Decision on top up on salaries for IPA staff**, which came into force on 9<sup>th</sup> March 2019 (Decision published in the Official Gazette of Montenegro No 13/19 on 1<sup>st</sup> March 2019);
  - **New version of IPARD II Programme** adopted on 7<sup>th</sup> May 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)** adopted by the Government, June 2019;
  - Amendment to the **Decree on the implementation and procedures** for use of Funds from the Instrument for Pre-Accession Assistance (IPARD II Programme) - ("Official Gazette of Montenegro" No. 46/2019), August 7<sup>th</sup> 2019.

All above listed changes, in possible extent, were covered by audits performed by the Audit Authority. The adoption of the Decision related to IPA staff salaries aims to motivate the employees that deal with IPA funds and to prevent brain drain. The AA confirms that, in addition to all substantial changes, the MCS remains in compliance with Article 7 of Regulation (EU) No 447/2014.

## 2.2 Exceptions applied in the approved procedures during the 2019

During financial year 2019 seven exceptions were approved by the NAO, five of them for IPARD Agency and two for DMS, as listed below:

1. DP DPAP -00 Manual of DPAP, Chapter 5 Description of the working procedure, Subchapter 5.8. Ranking of application<sup>2</sup>

The process of verifications of first public call for M1, both administrative and on the spot was time consuming, since there was parallel verification process of applications submitted within first public call for M3. Having in consideration above mentioned, in order to have successful

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<sup>2</sup> Deputy NAO approval on February 8<sup>th</sup> 2019

realization of eligible projects from the first public call for M1, the IPARD Agency started with contracting of eligible projects from Measure 1 with no previously performed ranking procedure.

2. DP-DAB 00-02 Accounting main entries<sup>3</sup>

Main entry no 7 – additional accounting step is included, closure of accounts 914 and 964 for amounts of difference between contracted and approved amounts. Main entries no 8, 9 and 10, DAB used Request for funds to record only the EU part.

3. DP-DPAP-00-29 Invitation for offers/quotations<sup>4</sup>

This exception is applied in order to avoid delays in the realization of contracted projects. Namely, the procedure for procurement – precisely the provision prescribed in the annex DP-DPAP-00-29 Invitation for the offers/quotations: 'Note that the highest price for listed items is \_\_\_\_\_ EUR and that only the offers with the lowest or the same price will be selected for the evaluation procedure' presented limitation and difficulty for procurement process and realization of contracted investments since the suppliers were not interested and willing to provide offers up to contracted amount approved by the IPARD Agency.

According to the approved exception, the applicants were allowed to submit three independent offers with the prices provided by suppliers and the Agency to pay the grant support only up to the contracted amount, already stated in the contract.

4. DP-DPAP-00-20 Contract for allocation of funds/Sector for structural support<sup>5</sup>

This exception is related to announcement of performance by recipients and postponing control of hidden works (for projects under first call for measure 1 and 3). Concretely, for recipients, who do not report on hidden works, as well as recipient where controllers are unable to conduct on-the-spot control, control of hidden works to be checked after the payment request is submitted, through Final Report on Professional Supervision and the Construction Book by comparing the entered data in the construction books with the approved quantities and type of material.

5. DP-DAB-00-11 List of all payments DP-DAB-00-05 Monthly checklist DP-DEP-00-24 List of all payments Sector for accounting, budget and execution of payments<sup>6</sup>

This exception is related to amendments of referent annexes/documents (DP-DAB-00-11 List of all payments, DP-DAB-00-05 Monthly checklist, DP-DEP-00-24 List of all payments, DAB MoP, chapter 5.5.D1- Declaration of expenditure and revenue and D2-Annual declaration of accounts for financial year) within Manual of procedures version 1.2 of the IPARD Agency, in order to present more information about the payments

6. Manual of Procedure for DMS, Chapter Accounting, request for involvement of new procedures related to accounting records/accounting entries<sup>7</sup>

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<sup>3</sup> Deputy NAO approval on March 12<sup>th</sup> 2019

<sup>4</sup> NAO Approval on June 12<sup>th</sup> 2019

<sup>5</sup> Approved by Deputy NAO on September 9<sup>th</sup> 2019

<sup>6</sup> Approved by Deputy NAO on December 12<sup>th</sup> 2019

<sup>7</sup> NAO approval on January 23<sup>rd</sup> 2019



## 7. DMS MoP 2.0 Chapter: Financial Management<sup>8</sup>

This exception relates to preparation of quarterly instead of monthly Progress reports on contracts and payments by IAs

The AA confirms that, all above listed exceptions are recorded and approved at appropriate level and aim at the successful implementation of IPARD tasks. In addition AA will take into account all exceptions during risk analysis and following audits.

### 3. CHANGES TO THE AUDIT STRATEGY

Not applicable. The Audit Strategy has not been changed in the reference period to which this report relates.

### 4. SYSTEMS AUDITS

#### 4.1. Details of the bodies that have carried out system audit, including the audit authority itself

The audit body that has carried out the system audits is Audit Authority of Montenegro. The Audit Authority of Montenegro, as an independent audit body, was established by the Law on Audit of European Union funds ("Official Gazette of Montenegro" N° 14/12, 54/16, 37/17 and 70/17). Audit Authority of Montenegro is responsible for carrying out the audit function for IPARD II Programme in line with the functions and responsibilities set out in Clause 5 of Annex A to the Framework Agreement.

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<sup>8</sup> December 24th 2019

**4.2. Summary table of the audits carried out, with the indication of the authorities/bodies audited, the assessment of the key requirements for each authority/body, issues covered and a comparison to the audit planning**

Audit period	1. Programme (CCI and title)	2. Audit Body	3. Audited Body(ies)	4. Date of the audit	5. Scope of the audit	6. Principal findings and conclusions	7. Problems of systemic character and	8. Estimated financial impact (if applicable)	9. State of follow-up (closed /or not)
01.01.2019.-30.11.2019. i.e. FY 2019	Programme for Agriculture and Rural development of Montenegro - IPARD II No CCI: 2014ME06I4NP001	Audit Authority of Montenegro	Directorate for Management Structure IPARD Agency Managing Authority	April – November 2019	System Audit encompassed DMS (National Fund and NAO Support Office) and OS (Managing Authority and IPARD Agency) and the following audit areas were examined: • Human Resources - all bodies (ICFR 1a, 1b, 1c, 1d, 1e) • Risk management – IA and NAO support office (ICFR 2a, 2b) • Verifications by the NAO – NAO support office (ICFR 1b, 5a, 5b) • Financial management - NFD (ICFR 3a) • Accounting – IA and NFD (ICFR 3a) • Publicity and authorization of projects-IA (ICFR 3a) • Authorization of payments- IA (ICFR 3a) • On the spot control-IA (ICFR 3a) • Execution of payments-IA (ICFR 3a) • IT Policy – IA (ICFR 3a - viii, 3b) • Internal audit – IA (ICFR 5a) • Monitoring, evaluation and reporting – MA (ICFR 4b, 4c) • Programming – MA (ICFR 4c) • Coordination and public relations – MA (ICFR 4b, 4c) • Review of procedures for preparation of AMD – NAO support office (5a, 5b)	1. Unjustified extension of deadline for completing the application and ineligible general cost 2. Deficiencies in process of administrative verification and ineligible beneficiary 3. Inappropriate interpretation of term "young farmer" and aid Intensity 4. Deficiencies within administrative control of application ID no. 18-01-3-0019 5. Deficiencies within administrative control of application ID no. 18-01-1-0125 6. Deficiency in content of Annex – Invitations for the offers/quotations and non-acting in accordance with approved exception request 7. Non-compliance between IPARD Programme, Decree and Public call 8. Uneven approach in verifying reasonableness of costs 9. Inefficiency in application processing phase 10. Deficiencies in procedure of justifying reference price variation 11. Inadequate control of rule of origin 12. Deficiencies of confirmation on verifiability and controllability 13. Mismatch between Matrix of modification and IPARD II Programme (1.2) 14. Non-fulfilment of tasks from Evaluation plan 15. Inadequate internal tables 16. Guideline for recipients 17. Written procedures concerning responsibility of MA 18. KPI content 19. Non-existence of contingency plan 20. Shortcomings in IPARD Monitoring Committee work 21. Modifying procedure of visibility requirements 22. Deficiencies in information and communication channels 23. Shortcomings in Recruitment plan and Training Needs Analysis 24. Deficiencies regarding HR * For more specific details for particular findings see Annex no. 1 – Findings and recommendations	/	288,78 € (216,58 € EU part) related to the finding 10 (4.2.4)	Please see part I of annex 1

There were no changes in the audit strategy and audits are performed in accordance with audit plan.

During reference period comprehensive system audit was performed, which includes:

### **1) Test of procedures**

The audit was performed using the methodology prescribed in manual of procedures developed by the AA and based on the guideline 2 “Audit Strategy” issued by DG AGRI. The audit examined the set up and reviewed the documentation provided by the relevant bodies and the information that was available until the time of finalizing the report.

Verifications made by AA in IPARD Agency, Managing Authority and DMS in respect of this system audit are as follows:

- We have verified that Manuals of procedures are in line with Framework, Sectoral and Financing Agreement as well as other appropriate national and EU regulation, and whether they are applied in practice;
- We have verified adequacy of staff actually in place for performing delegated tasks as well as whether organizational structure is adequate for the efficient and effective implementation of all tasks and responsibilities;
- We have verified that all employees have demonstrated commitment to integrity and ethical values;
- We have verified whether the H&R process functions effectively (WLA, organisational structure, job descriptions, AWP, recruitment plan, etc.);
- We have verified retention policy measures;
- We have verified responsibilities related to the irregularity procedures as well as procedures prescribed and number of recorded irregularities;
- We have verified whether anonymous reporting on irregularities is enabled and whether the “whistle-blowers” enjoy legal protection;
- We have verified appropriate assurance role from NAO/SO including timely preparation and execution of annual on-the-spot checks plan;
- We have verified whether appropriate publicity measures are taken and whether all information concerning the activities related to IPARD Programme 2014-2020 is published on the official website of the DP/ MARD and in the media;
- We have verified whether the internal control system for calculation of the economic viability of recipient (procedure for assessment of a business plan) and for checking of reasonableness of costs (including reference price database) is set up appropriately;
- We have verified whether the accounting procedures are established in accordance with the internationally accepted accounting standards as well as accountability and reliability the accounting system;
- We have evaluated accounting system within Department for Accounting and Budget (main accounting functions including process of recording of debts to be recovered and preparation of periodic summaries of expenditure as well as preparation of quarterly and annual declarations to the Commission);
- We have verified adequacy of the risk assessment process and implementation in practice;
- We have verified whether the reporting lines are established in a way that provides a good and efficient flow of information including procedures for collection of data for monitoring and reporting.

## **2) Compliance testing**

During FY 2019, under IPARD II Programme 2014-2020, IPARD Agency has continued with the process of implementation (signing of contracts and executing payments to recipients) of public calls published in FY 2018 (one call for applications for allocation of funds for measures 1, and one call for applications for allocation of funds for measures 3). At the moment of announcement of audit and preparation of engagement plan, 100 contracts were signed and 1 payment was executed for measure 1 as well as 20 contracts were signed and no payments were executed for measure 3, which were the base for sampling for compliance testing. The sample covered 10 contracts signed and 1 rejected application for support. The sample is oriented to cover a variety of transactions (different sectors, types and codes of investments) so relevant key functions were assessed under different circumstances.

The audit was performed using the methodology prescribed in manual of procedures developed by the AA and based on the guideline 2 "Audit Strategy" issued by DG AGRI.

To confirm the compliance of the IPARD Agency with the ICFR-3 Control activities, through compliance testing the AA performed different type of verifications. The compliance test includes following:

- 1) Compliance test to confirm the functioning of controls and determine whether the undertaken activities are in compliance with the written working procedures and whether they have been performed in accordance with the set deadlines as well as to determine dynamics of the approval of applications process;
- 2) Compliance test to confirm eligibility of the recipients and investments;
- 3) Compliance test to confirm whether the templates and deadlines for issuing the documents by technical bodies have been respected.

The outcome of the audit process is summarized in the Final system audit reports that provide findings and recommendations which were identified during the audit process in DMS, IPARD Agency and Managing Authority. Findings were categorized according to the level of importance to major, intermediate and minor findings. During system audit we identified 24 findings, out of which 5 findings are major, 14 findings are intermediate and 5 findings are minor. We have identified one finding with financial impact in amount of 216,58 € (see finding 4.2.4 from annex 1, part I) and none of the findings indicate any problems of systemic nature. As presented in Annex 1, out of 24 recommendations for FY 2019, IPARD Agency implemented 5 recommendations, while 7 are partially implemented and 12 are still opened.

Detailed description of the findings and recommendations as well as auditee's response are laid down in Annex 1 "Findings and recommendations", PART I as a part of this report.

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

For the purpose of detailed defining of the scope of the audit, during the preparation of Audit Strategy for period 2019-2021 the Audit Authority performed a detailed risk assessment to determine the bodies and priority processes in conducting system audit.

The Audit Authority's methodology for risk assessment is based on the:

- International Standards on Auditing (and in particular ISA 300, 315, 320, 330, 500),
- EC Guidance document on a common methodology for the assessment of management and control systems in Member States and

- DG AGRI Guideline 2 IPARD II audit strategy.

Risk assessment approach is applied in order to understand and select the high risk areas for performing system audit. The AA carries out its own risk assessment to compose the annual audit plan of systems audit. The risk assessment results are used for prioritizing and selecting the bodies/processes/ICFR to be audited.

During risk assessment, risks were identified and taken into account at the authorities and process/ ICFR level. Specific inherent and control risk factors were assessed for each body and process/ICFR. Each risk factor, including inherent and control risks, was assessed as low, medium or high, considering both the significance and likelihood of the risk, and was evaluated in 5-points scale: the highest risk gets highest points and vice versa. In order to distinguish between the factors with varying importance, the weight were given to the specific risk factors. After assessment, all bodies and processes were ranked according to the total score.

According to the results of performed risk assessment we identified processes and ICFRs within DMS (NAO/SO and NF) and OP (IPARD Agency and Managing Authority) which were covered by the system audit.

For the purpose of compliance testing within system audit, sample for testing is based on professional judgment of audit team. Compliance testing was carried out on 10 contracts signed (out of which, at the moment of audit, there were only 2 payments executed<sup>9</sup>) as well as 1 rejected request for support. The sample is oriented to cover a variety of transactions (different sectors, types and codes of investments) so relevant key functions were assessed under different circumstances.

#### **4.4 Description of the principal findings and conclusions drawn from the audit work for the management and control system and their functioning**

Key weaknesses identified during this system audit refer to the IPARD Agency and process of authorization of commitments. During audit we identified errors with potential financial impact which, after further analysis performed by IA resulted with financial impact, as well as significant delay in overall process of authorization of commitments which could negatively impact on overall IPARD reputation and absorption rate. Average time necessary for signing contract with recipients, based on the sample of 10 transactions, is more than 400 days from the date of submitting request for support.

We also identified inconsistency between IPARD II Programme, Decree on implementation of IPARD Programme and announced public calls, as well as different interpretation of some provisions which negatively impact on efficiency of the process. Namely, according to the public call, recipient can submit just one request for support within prescribed deadline. Having in mind that there is no document or process related to the amendment/annex of request for support all further changes in requested structure of investment require new request for support which is not allowed, especially if the new request for support is submitted after deadline prescribed by public call. Moreover, the Decree in Article 27, last paragraph defines "Untimely requests for support, as well as requests that have not been submitted with all the necessary documentation requested by a public call, will not be considered". During audit we identified number of vague and inconsistent requests for

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<sup>9</sup> The second payment was executed in the third quarter of FY 2019.

supports for which IPARD Agency allowed changes which require additional time and capacities.

We recommended to the top management to immediately take appropriate corrective measures in order to speed up the overall process of implementation of IPARD Programme with the aim of increasing efficiency and effectiveness, increasing absorption rate and mitigating risk of de-commitment of unused funds. Among others, this could be achieved by more frequent publishing public calls (first call for measure 1 was published on 23/02/2018 and second call for measure 1 was published after **two years** on 24/02/2020) in order to allow potential recipients to correct inconsistency in vague request for support and apply new request as soon as possible which would significantly save time and capacities related to the particular project.

Considering the results of system audit and continuously observing the system's functioning during 2019, we conclude that the management and control system functions appropriately, although further improvements are necessary as presented in recommendations.

Detailed description of the findings and recommendations as well as auditee's response are laid down in Annex 1 "Findings and recommendations", PART I as a part of this report.

#### 4.5 Description of specific deficiencies related to the management of financial instruments

Not applicable.

#### 4.6 Level of assurance obtained following the system audit (low/average/high) and justification

During audit AA performed comprehensive testing of written procedures defined in the audit scope as well as performed detail compliance testing, which provides **reasonable assurance** for **overall conclusion** obtained from the system audit and relevant MCS.

#### Overall assessment – Matrices

The overall conclusion on the ICS is presented in the following matrices:

Matrices - IPARD Agency

		MATRIX - Assessment of the ICF (IPARD AGENCY)																					
		Assessment Component Procedure		Control environment						Risk management	Control activities				Information and Communication		Monitoring of the internal control framework				Evaluation at assessment criteria		General conclusion
				Organisation		Human Resources		Delegation			Control activities		IT Security				Monitoring		Internal audit				
Weighting / Scoring		S	T at 15%	S	T at 5%	S	T at 5%	S	T at 5%	S	T at 50%	S	T at 10%	S	T at 5%	S	T at 5%	S	T at 5%	W	T	Weighted total	
Operations	Validation and authorization	Administrati ve controls	2	0.30	2	0.10			3	0.15	2	1.00	3	0.30	2	0.10	2	0.10	2	0.10	20%	2.00	0.40
		On-the-spot controls	3	0.45	3	0.15			3	0.17	3	1.50	3	0.30	3	0.15	2	0.10	3	0.15	20%	2.97	0.59
Payments	Execution of payments		4	0.6	4	0.2			3	0.15	4	2	4	0.4	4	0.2	3	0.15	3	0.15	20%	3.85	0.77
	Accounting		4	0.6	3	0.15			3	0.15	3	1.5	3	0.3	4	0.2	3	0.15	3	0.15	20%	3.20	0.64
	Advances (*)																				0%	0.00	0.00
	Debts management		4	0.6	4	0.2			3	0.15	4	2	4	0.4	4	0.2	3	0.15	3	0.15	20%	3.85	0.77
											General conclusion											3.17	
											Assessment of ICF						works (medium impact)						
<b>LEGEND:</b>																							
1 to 1.5 = not working																							
1.51 to 2.5 = working partially (significant impact)																							
2.51 to 3.5 = works (medium impact)																							
3.51 above = works well (minor impact)																							

Overall conclusion on the ICS in IPARD Agency, based on the results of system audit, is Works (medium impact) with the score of 3.17.

Matrices -NF

MATRIX - Assessment of the ICF (NATIONAL FUND)									
	Assessment component Procedure	Control environment			Risk management	Control activities		Information and communication	Monitoring of the internal control framework
		Organisation	Human resources	Delegation		Control activities	IT Security		
Managing functions	Management of IPA II accounts and financial operations	4	3	n/a	3	4	4	4	4
Paying functions	Authorisation and control of payments	4	3	n/a	4	4	4	4	4
	Accounting for commitment and payment	4	4		3	4	3	4	4
	Debt management	4	4	n/a	4	4	4	4	4
	Treasury	4	4	n/a	4	4	4	4	4

Please introduce the scores in the table

Overall average	3.857142857
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LEGEND:

1	to	1.5	=	not working
1.51	to	2.5	=	working partially (significant impact)
2.51	to	3.5	=	works (medium impact)
3.51	above		=	works well (minor impact)

Overall conclusion on the ICS in National Fund, based on the results of system audit, is Works well (minor impact) with the score of 3.85.

Matrices -NAOSO

MATRIX - Assessment of the ICF (NAO SUPPORT OFFICE)									
	Assessment component Procedure	Control environment			Risk management	Control activities		Information and communication	Monitoring of the internal control framework
		Organisation	Human resources	Delegation		Control activities	IT Security		
Implementing functions	Provide assurance on the effective functioning of	4	3	n/a	4	3	4	4	3

Please introduce the scores in the table

Overall average	3.571428571
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LEGEND:

1	to	1.5	=	not working
1.51	to	2.5	=	working partially (significant impact)
2.51	to	3.5	=	works (medium impact)
3.51	above		=	works well (minor impact)

Overall conclusion on the ICS in NAO Support Office, based on the results of system audit, is Works well (minor impact) with the score of 3.57.

MATRIX - Assessment of the ICF (MANAGING AUTHORITY)					
	Assessment component	Control environment			Information and communication
	Procedure	Organisation	Human resources	Delegation	
Managing functions	Selection of measures	3	4	n/a	3
	Programme monitoring	4	4	n/a	4
	Evaluation	4	4	n/a	3
	Reporting	3	4	n/a	3
	Coordination	4	3	n/a	3
Implementing functions	Publicity	4	4	n/a	4

Please introduce the scores in the table in line with the AA assesment

Overall average	3.611111111
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LEGEND:

1 to	1.5 =	not working
1.51 to	2.5 =	working partially (significant impact)
2.51 to	3.5 =	works (medium impact)
3.51 above	=	works well (minor impact)

Overall conclusion on the ICS in Managing Authority, based on the results of system audit, is Works well (minor impact) with the score of 3.61.

## 5. AUDITS OF SAMPLES OF TRANSACTIONS

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

As stated above in point 1.2., AA performed test of transactions within two audits of operation, one related to the first three quarters (D1 – Q1,Q2 and Q3) and second related to last quarter (D1 – Q4). Both audits were performed solely by the Audit Authority of Montenegro and we did not rely on any third party in carrying out the audit activities.

The Audit Authority of Montenegro, as an independent audit body, was established by the Law on Audit of European Union funds ("Official Gazette of Montenegro" No 14/12, 54/16, 37/17 and 70/17). Audit Authority of Montenegro is responsible for carrying out the audit function for IPARD II Programme in line with the functions and responsibilities set out in Clause 5 of Annex A to the Framework Agreement.

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

As there were only eight payments within audited period, AA decided to audit 100% of declared expenditures, and it was not necessary to perform sampling as envisaged by the DG AGRI guideline no 2 "Audit Strategy". All transactions were fully tested, both administratively and on-the-spot.



In line with the DG AGRI guideline no 2 "Audit Strategy", materiality level<sup>10</sup>, i.e. maximum deviation that can be accepted, in monetary terms is set up at max 2% of gross<sup>11</sup> certified expenditure declared to the Commission and amounted to 27.344,02 €.

**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.**

As mentioned above AA tested all the declared expenditures due to the very small population, so the statistical sampling was not applicable.

**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.**

Total amount of expenditure declared to the Commission for FY 2019 equal to 1.367.201,03 € (EU part) within four quarterly declarations submitted by NAO. First one (D1 – Q1) was declared on 25<sup>th</sup> April 2019 in amount of 5.476,86 €, second (D1 – Q2) was declared on 18<sup>th</sup> July 2019 in zero amount, third (D1 – Q3) was declared on 25<sup>th</sup> October 2019 in amount of 234.314,22 € and fourth (D1 – Q4) was declared on 20<sup>th</sup> January 2020 in amount of 1.127.409,95 €. There were no negative items as there were no deductions made in the D2 for recoveries and other 'negative' amounts during the financial year. Total declared amount was the subject of our audit work, i.e. we tested 100% of expenditures declared to the EC during FY 2019.

As our national currency is euro, we have no differences in declared amounts coming from the exchange rates.

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

There were not any negative items as there were no deductions made in the D2 for recoveries and other 'negative' amounts during the financial year.

**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.**

As stated above AA tested all the declared expenditures due to the very small population, so the non-statistical sampling was not applicable.

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<sup>10</sup> For the purpose of error evaluation we used only EC part of gross expenditures.

<sup>11</sup> Having in mind that there were not any negative amounts during the FY 2019 gross declared expenditures are equal to the net declared expenditures.

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

The results of Audit of transactions are shown in table presented in Chapter 10. The table indicates the eligible expenditure declared to the Commission and the amount of expenditure audited. Having in mind that eight payment requests from recipients were executed / paid during FY 2019, the audit scope included the total population, i.e. AA has examine all transactions or 100% of the expenditure declared.

**5.8 Analysis of the principal results of the audits (sample items selected and audited, together with the respective amount and types<sup>12</sup> of error by operation) as well as the nature<sup>13</sup> of errors found, root causes and corrective measures proposed, including mitigating these errors in the future.**

Table with financial errors identified during audit of operational transactions:

Application ID	Expenditure declared €	Amount of Error €	Type of error (random, known, systemic anomalous)	Nature of error	Financial impact (Yes/No)	Status (open/closed)
1	2	3	4	5	6	7
18-01-1-0127	234.314,22	99,85	known	Irregularity	Yes	Open
18-01-3-0005	489.207,28	309,37	known	Irregularity	Yes	Open
18-01-1-0228	48.900,00	48.900,00	known	Irregularity	Yes	Open

As presented in the table above, whole project under application ID no 18-01-1-0228 is identified as ineligible for support which significantly impacts on overall conclusion and audit opinion (there were 8 payments in total out of which 1 is ineligible). The specifics of the project and vague eligibility requirements (LEE) related to the manure handling equipment and machinery as well as lack of experience of employees in IPARD Agency caused the error identified.

Detailed description of the findings and recommendations as well as auditee's response are laid down in Annex 1 "Findings and recommendations" Part II as a part of this report.

**5.9 Details of the most likely error rate (total error rate<sup>14</sup>) 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.**

<sup>12</sup> Random, systemic, anomalous

<sup>13</sup> For instance: eligibility, public procurement, state aid

<sup>14</sup> As defined in Article 28(14) of Commission Delegated Regulation (EU) No 480/2014.

Having in mind that AA examine all transactions or 100% of the expenditure declared, total error rate is known. During audits in 2019 we identified 4 findings with financial impact, out of which 1 finding is identified during system audit and 3 findings are identified during audit of transactions. Total error is calculated by adding all known errors identified and equal to **49.525,80 €**, and consequently error rate is equal to 3.62%.

**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.**

Total error rate is above materiality level which impacts on audit opinion related to the legality and regularity of expenditures declared, but not on the reliability of the annual financial reports or statements having in mind that due to irregularities identified IPARD Agency should initiate procedure for recovery of funds, i.e. to act in accordance with the article 50 from Sectoral Agreement.

Main corrective measures refer to the strengthening capacities of IPARD Agency and organising adequate trainings for employees within IPARD Agency, particularly newcomers which don't have adequate experience in dealing with IPARD funds.

In accordance with the DG AGRI Guideline no 2 on the Audit Strategy, error evaluation is presented in Annex 4 "Error evaluation" as a part of this report.

**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<sup>15</sup>, including flat rate or extrapolated corrections.**

Taking into account that for FY 2018 there weren't expenditures declared to the EC and audit of transactions performed as well as that for FY 2019 AA identified findings with financial impact due to irregularities identified, operating/management structure didn't have obligation for correction of the final declaration of expenditures and financial statements.

**5.12 Residual total error rate<sup>16</sup> following the implementation of the above-mentioned corrections and significance for the audit opinion.**

Not applicable having in mind that there weren't any corrections of financial statements.

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

Not applicable, AA didn't perform audit of the complementary sample.

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<sup>15</sup> This concerns both corrections on the audited sample units and corrections implemented as a result of the total error rate.

<sup>16</sup> Total errors minus corrections referred to in paragraph 5.11, divided by the total population.

**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.**

Taking into account that for FY 2018 there weren't expenditures declared to the EC and audit of transactions performed by AA as well as that for FY 2019 AA issued final reports of audit of operational transaction on 10<sup>th</sup> February and on 04<sup>th</sup> March 2020, operating/management structure didn't perform corrective actions. However, from management response we can conclude that IPARD Agency will take corrective measures and initiate procedure for recovery of funds as soon as possible.

**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.**

AA considers that findings identified are not systemic in nature.

**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. There were not any negative items as there were no deductions made in the D2 for recoveries and other 'negative' amounts during the financial year.

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

Results of the audit of transactions confirm assessment presented in matrices, part 4.6 of this report. Management and control system functions effectively, but further improvements are necessary, particularly for the functions authorisation and control of commitments and payments as well as on the spot control. During first public calls for measure 1 and 3, IPARD Agency received a large number of applications which, due to the lack of staff, significantly impact on workload of functions mentioned above.

IPARD Agency should take appropriate actions in order to strengthen capacities by additional employment and by organizing adequate and comprehensive trainings for employees with the aim of increasing effectiveness, efficiency and overall reputation of IPARD II Programme in Montenegro.

## **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 account**

The audit body that has carried out audit of the annual financial reports/annual accounts is Audit Authority of Montenegro. The Audit Authority of Montenegro, as an independent audit body, was established by the Law on Audit of European Union funds ("Official Gazette of Montenegro" N° 14/12, 54/16, 37/17 and 70/17). Audit Authority of Montenegro is responsible for carrying out the audit function for IPARD II Programme in line with the functions and responsibilities set out in Clause 5 of Annex A to the Framework Agreement and for issuing an annual opinion on the annual financial reports or statements and the underlying annual accounts for the preceding financial year, covering their completeness, accuracy and veracity. All audit activities, including the audit of accounts, were performed by the Audit Authority of Montenegro. We did not rely on the work of other bodies in performing our functions and with regard to our responsibilities.

## **6.2 Description of audit approach used to verify the elements of the annual financial reports or statements/annual accounts**

The Audit Authority performs the audit of accounts as defined in Article 12(2) and 23(1) (b) of Commission Implementing Regulation (EU) No 447/2014.

The audit of accounts was carried out in line with the Audit Strategy following requirements from the DG AGRI Guideline no 2 on the Audit Strategy and Audit Authority's manual of procedures, taking into consideration Guideline no 5 IPARD II Annual Accounts.

As regard non-operational transactions, taking into consideration that there were no irregularities/debts presented in annual accounts and no advances paid, audit covered only transactions in the IPARD Euro account. AA carried out verification of movements in the IPARD Euro account, in order to establish the legality and regularity of the declared principal and interest amounts. Considering the small number of transactions (8 debit and credit transactions in total), the AA checked all movements made in the IPARD Euro Account. The audit covered only the correctness of the principal amounts, since there was no interest for FY 2019.

The audit process comprised following steps:

- 1) Planning and preparation of the audit
  - collecting, introducing into and analysing legal basis and related documentation for the audit of accounts in order to gain understanding of the annual accounts, including information gained during system audit and audit of operations
- 2) Fieldwork
  - meetings with responsible bodies (NAO/NF/IPARD II Agency),
  - collecting and analysing documentation,
  - Testing and reconciliations
- 3) Reporting
  - preparation and issuance of the draft audit report on accounts,
  - receipt of management response and incorporation into report,
  - preparation and issuance of the final report on accounts

In the table below we present overall review of the annual accounts and reconciliation:

Description	Amount of gross expenditure declared		National part	Recoveries / Corrections		Amount of net expenditure declared	
	Public contribution	EU part only (75%)		Public contribution	EU part only	Public contribution	EU part only
Quarterly Declaration of Expenditure D1							
M1	7.302,48	5.476,86	1.825,62	0,00	0,00	0,00	0,00
M3	0,00	0,00	0,00	0,00	0,00	0,00	0,00
1st quarter	7.302,48	5.476,86	1.825,62	0,00	0,00	0,00	0,00
M1	0,00	0,00	0,00	0,00	0,00	0,00	0,00
M3	0,00	0,00	0,00	0,00	0,00	0,00	0,00
2nd quarter	0,00	0,00	0,00	0,00	0,00	0,00	0,00
M1	312.418,96	234.314,22	78.104,74	0,00	0,00	0,00	0,00
M3	0,00	0,00	0,00	0,00	0,00	0,00	0,00
3rd quarter	312.418,96	234.314,22	78.104,74	0,00	0,00	0,00	0,00
M1	78.654,15	58.990,61	19.663,54	0,00	0,00	0,00	0,00
M3	1.424.559,12	1.068.419,34	356.139,78	0,00	0,00	0,00	0,00
4th quarter	1.503.213,27	1.127.409,95	375.803,32	0,00	0,00	0,00	0,00
Sum of quarterly declarations (D1s)	1.822.934,71	1.367.201,03	455.733,68	0,00	0,00	0,00	0,00
Annual Declaration D2							
M1		298.781,69		0,00	0,00	0,00	0,00
M3		1.068.419,34		0,00	0,00	0,00	0,00
Annual declaration (D2)		1.367.201,03		0,00	0,00	0,00	0,00
Difference between D1s and D2		0,00		0,00	0,00	0,00	0,00
List of Payments							
M1		298.781,69					
M3		1.068.419,34					
List of payments		1.367.201,03					
Difference between D2 and list of pavments		0,00					

Audit checks related to completeness, accuracy and veracity of the amounts reported in the accounts comprised the following reconciliations:

### 1) Reconciliation of Quarterly Declarations of Expenditure and Annual Declaration of IPARD Accounts for IPARD II

In order to conclude on the completeness, accuracy and veracity of the Annual Accounts in accordance with the DG AGRI Guideline No 2 – Audit Strategy we have checked whether there were any differences between the

expenditure and the revenues declared with the interim quarterly declarations (D1s) and the eligible expenditure declared with the Annual Declaration (D2) for the FY 2019 for IPARD II and we have reconciled the Annual declaration (D2) with the interim quarterly declarations (D1s).

The reconciliation is presented in the table below:

	Amount of expenditure declared	
	Public contribution	EU part only
<b>Quarterly declarations</b>		
1st quarter	7.302,48€	5.476,86€
2nd quarter	0,00€	0,00€
3rd quarter	312.418,96€	234.314,22€
4th quarter	1.503.213,27€	1.127.409,95€
<b>Sum of quarterly declarations</b>	1.822.934,71€	1.367.201,03€
<b>Annual declaration (D2)</b>	1.367.201,03€	1.367.201,03€
<b>Difference</b>	455.733,68€	0,00€

We can confirm that there are no differences between the expenditure and the revenues declared with the interim quarterly declarations (D1s) and the eligible expenditure declared with the Annual Declaration (D2) related to the EU part for the FY 2019. Difference, shown in the table above, between the expenditure and the revenues declared with the interim quarterly declarations (D1s) and the eligible expenditure declared with the Annual Declaration (D2) related to public contribution is a result of formal error within annual declaration D2, more precisely NAO submitted D2 with EU part only and therefore difference of 455.733,68 € refers to national co-financing part. The details are presented in part III of the annex 1 "Finding and Recommendations".

## 2) Reconciliation of Annual Declaration of Expenditure with the expenditure paid recorded in the accounts of the Agency and the Management Structure for IPARD II

We reconciled annual declaration (D2) with the list of payments provided by the NAO in line with Article 45(d) of the SA.

The reconciliation is presented in the table below:

	EUR (EU part only)
Amount of gross expenditure declared in the annual declaration D2	1.367.201,03€
Sum of payments stated in the list of payments	1.367.201,03€
<b>Difference</b>	0,00€

We can confirm that in FY 2019 there were no differences between the payments made and registered in the List of payments and gross expenditure declared in the Annual Declaration (D2), so the Annual Declaration (D2) is reconciled with the List of payments.

## 3) Roll forward of the debtors' ledger

We checked whether the closing balance of the debtors ledger was equal to its last year's opening balance plus the transactions (new debts, recoveries and written off amounts).

The reconciliation is presented in the table below:

Debtors' ledger year n	Amount EU part		
(a) Opening balance year n	0,00€	0,00€	Debtors' ledger - Closing balance year n-1
(b) New cases	0,00€		
(c) Recoveries	0,00€		
(d) Written-off debts	0,00€		
(e) Corrections	0,00€		
Closing balance year n a+b-c-d+/-e	0,00€	0,00€	Closing balance as declared in the annual declaration for year n

We can confirm that there are no differences between closing balance of the debtor's ledger and its last year's opening balance plus the transactions.

#### 4) Reconciliation of the declared principal amount and interest of the IPARD Euro Account

On December 13<sup>th</sup> 2019 the Commission transferred to the IPARD II Euro Account amount of 900.000,00 € as Community contribution of pre-financing as well as two payments on the basis of quarterly declarations in total amount of 239.791,08 €. On December 31<sup>st</sup> 2019, on the IPARD II Euro Account there was an amount of 5.172.590,05 €.

In the course of FY 2019 there was no interest, and balance of interest by December 31<sup>st</sup> 2019 was 0,00 €. The deposit account is not opened and therefore there is no realized interest income.

The reconciliation is presented in the table below:

	Principal amount (EUR)	Interest (EUR)
Opening balance of the IPARD Euro Account	<b>5.400.000,00€</b>	
Current account [account number]	5.400.000,00€ [907-0000000086001-40]	0,00€
Deposit account [account number]	0,00€	0,00€
Other amounts deposited in the banks for the purpose of accrual of interest	0,00€	0,00€
[Deposit number] / [due date]	n/a	n/a
[Deposit number] / [due date]	n/a	n/a
Transactions in the financial year	<b>-227.409,95€</b>	
Amounts received from the Commission in the financial year	1.139.791,08€	



- for pre-financing	900.000,00€	
- for covering expenditure executed in the previous FY	0,00€	
- for covering expenditure executed in the current FY	239.791,08€	
Interest accrued on the IPARD Euro Account during the financial year		0,00€
Amount of expenditure	1.367.201,03€	<i>[this cell is to be filled in only if some part of EU expenditure has been bridge financed from interest]</i>
Amount of national contribution financed from interest		0,00€
Recovered amounts	0,00€	
Written-off amounts	0,00€	
Other transactions (to be broken down in detail)	<b>0,00€</b>	<b>0,00€</b>
Expenditure excluded from the declarations of expenditure	n/a	n/a
- financial adjustments made by the NF	n/a	
Payment of financial corrections made by the Commission	n/a	
Bridge financing	n/a	n/a
- funds transferred from state budget	n/a	
- funds transferred to the state budget	n/a	
Closing balance of the IPARD euro account	<b>5.172.590,05€</b>	
Current account	5.172.590,05€	0,00€
Deposit account	0,00€	0,00€
Other amounts deposited in the banks for the purpose of accrual of interest	0,00€	0,00€
<i>[Deposit number] / [due date]</i>	n/a	n/a
<i>[Deposit number] / [due date]</i>	n/a	n/a

Taking into consideration performed verifications during the audit of accounts and statement of expenditures for 2019, we can confirm that the closing balance of the IPARD II Euro Account declared in the Annual Declaration (D2) reconciles with the cash flows through the IPARD II Euro Account.

In accordance with the DG AGRI Guideline no 2 on the Audit Strategy, transactions verified are presented in Annex 5 “Non-operational transaction” as a part of this report.

##### 5) General reconciliation of data for the purpose of testing the correctness of the whole declaration (expenditure, debtors ledger and IPARD Euro account)

General reconciliation of data is carried out to compare if several balances reconcile with each other. In this context it is vital to reconcile the transactions of the IPARD Euro Account with the amount of payments from the list of payments, amounts of recoveries and written-off debts to the Debtors Ledger.

By the audit of accounts in NAO/MS and in the IPARD Agency we made reconciliations of all data presented in the accounting records of the IPARD Agency and accounting records in NAO/MS and data presented in the Annual Accounts and Statement of Expenditure for FY 2019.

The reconciliation is presented in the table below:

	IPARD Euro account			
	<u>Principal amount</u> (EUR)	<u>Interest</u> (EUR)		
Opening balance of the IPARD Euro Account	5.400.000,00€	0,00€		
Current account [account number]	5.400.000,00€ [907-0000000086001-40]	0,00€		
Deposit account [account number]	0,00€	0,00€		
Other amounts deposited in the banks for the purpose of accrual of interest	0,00€	0,00€		
[Deposit number] / [due date]	n/a	n/a		
[Deposit number] / [due date]	n/a	n/a		
Transactions in the financial year	-227.409,95€	0,00€		
Amounts received from the Commission in financial year	1.139.791,08€			
- for pre financing	900.000,00€			
- for covering expenditure executed in the previous FY	0,00€			
- for covering expenditure executed in the current FY	239.791,08€			
Interest accrued on the IPARD Euro Account during the financial year		0,00€	Annual declaration amount of expenditure declared	Difference

Amount of expenditure	1.367.201,03€	<i>[only if some part of EU expenditure has been bridge financed from interest]</i>	0,00€		0,00€
Amount of national contribution financed from interest		0,00€	Debtors' ledger - EU part only		Difference
			Principal amount	Interest	
Recovered amounts	0,00€		0,00€	0,00€	0,00€
Written-off amounts	0,00€		0,00€	0,00€	0,00€
Other transactions [to be broken down in detail]	<b>0,00€</b>	<b>0,00€</b>			
Expenditures excluded from the declarations of expenditure	n/a	n/a			
- financial adjustments made by the NF	n/a				
Financial corrections made by the Commission	n/a				
Bridge financing	n/a	n/a			
- funds transferred from state budget	n/a				
- funds transferred to the state budget	n/a				
Closing balance of the IPARD Euro Account	<b>5.172.590,05€</b>	<b>0,00€</b>			
Current account	5.172.590,05€	0,00€			
Deposit account	0,00€	0,00€			
Other amounts deposited in the banks for the purpose of accrual of interest	0,00€	0,00€			
<i>[Deposit number] / [due date]</i>	n/a	n/a			
<i>[Deposit number] / [due date]</i>	n/a	n/a			

As results of the audit of the Annual Accounts, and the reconciliations made for IPARD II, no deviations were found regarding completeness, accuracy and veracity of the amounts, stated in the Accounts.

### **6.3 Indication of the conclusions drawn from the results of the audit 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**

On the basis of work performed we can conclude that annual financial reports were prepared in accordance with templates set out in the Financing Agreements and that the amounts declared in the accounts are true, complete, accurate and credible. This concerns not only the information provided in the accounts on the expenditure, but also the information provided in the accounts on the IPARD Euro account and on the debtor ledger.

There were no financial corrections done by the NAO which should be reflected in the declaration of expenditure and financial statements for financial year 2019 as a follow-up to the results of the audit on transactions/operations. Also, as by the end of financial year 2019 there were no debtors recorded in the accounts and there were no respective recoveries which should be presented in the declaration of expenditure and financial statements.

As regards follow up of audit recommendations, in financial year 2018 there were no payments to recipients and consequently the AA did not perform audit of transactions/operations. For financial year 2019, audit of transactions/operations resulted in four financial findings related to four projects, where non-eligible amounts were paid to the recipients (described in detail in section 5 of this Report). The follow-up of these findings, recovery procedure and presentation of recovered amounts shall be in the scope of following audits.

Deficiencies in the preparation of the annual accounts (financial reports and statements) as several formal errors identified during the audit of accounts are communicated to the responsible bodies. Respective findings and recommendations have been presented and delivered to management response.

Detailed description of the findings and recommendations as well as auditee's response are laid down in Annex 1 "Findings and recommendations" Part III as a part of this report.

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

Not applicable. AA did not identify any problem of systematic nature.

### **6.5 Review of Annual Management Declaration issued by NAO for 2019 for IPARD II Programme**

Pursuant to Article 9(4) of Commission Implementing Regulation (EU) No 447/2014 and Annex C from the FwA, by 15 February of the following FY, the NAO shall, with a copy to the NIPAC and the AA, provide the Commission with an Annual Management Declaration per programme drawn up in accordance with Annex C to the FwA and covering:

- the overall responsibility for the financial management of EU funds and for the legality and regularity of the underlying transactions;

- the responsibility for the effective functioning of the management and internal control systems under IPA II;
- the conformity of the system and the effective functioning of the management and control system in the previous year.

According to the submitted Annual Management Declaration for FY 2019 for IPARD II by NAO to EC, No. 01-2291/4 from 14 February of 2020, NAO declared that:

- the information in the Annual Financial reports or statements is properly presented, complete and accurate in accordance with Article 23 (1) (b) of Commission Implementing Regulation (EU) N° 447/2014;
- the expenditure entered in the Annual Financial reports or statements was used for its intended purpose, in accordance with Commission Implementing Regulation (EU) N° 447/2014, and the principle of sound financial management;
- the management and control system put in place for the programme gives the necessary guarantees concerning the legality and regularity of the underlying transactions;
- operation of the internal control system relating to the implementation of IPA II and related to the Financing Agreement has been supervised.

We reviewed AMD and supporting documents issued by NAO. In this respect we made the following verifications:

- Results from on the spot checks and controls performed by Management Structure;
- Summary of the findings from the Internal Audit Reports;
- Information on the findings from the audit reports given by EC and follow-up actions in that respect;
- Information on irregularity policy and reporting;
- Information on risk management activities and mitigation measures;
- Exceptions from procedures requested;
- Overview of changes occurred in the financial and management control system;
- Staffing overview and statistics;
- Overview of results of KPI measurement for IPARD II Programme 2014-2020 (measure 1 and 3);
- Overview of results of KRI measurement;
- Overview of AA findings.

After performed verifications, the AA confirmed the following:

- The Annual Management declaration was submitted according to the article 59 (2) and Annex C of the Framework agreement for IPA II;
- The process of preparation of AMD was in line with NAO internal procedures. The AMD was supported by the NAO Assessment Report on functioning of MCS for the year 2019 and additional supporting annexes;
- The audit work carried out does not put in doubt the assertions made in the management declaration.

Beside positive opinion about AMD, we identified some deficiencies within annexes which should support AMD. These are mostly formal errors related to the NAO Assessment report for IPARD II where many parts of the report refer to CBC Programme, CBC Bodies and other programs and also there is inconsistency of information within different part of report. In addition some of the annexes contain vague information which can't be adequate base for issuing of AMD (overview of irregularity reports, overview of AA findings, etc.). During following system audit AA will cover process of issuing of AMD by NAO and present mentioned deficiencies in the audit report.

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

AA performed follow-up on the remaining recommendations from DG AGRI as well as follow-up on the findings of previous year audit activity (2018). Results are presented in Annex 2 – “Follow-up on remaining DG AGRI Recommendations AAAR 2019”, which presents outstanding recommendations issued by DG AGRI and Annex 3 – “Follow up on AA Recommendations” which presents status of recommendations issued by AA during audits for FY 2018.

Annex 2 contains three parts as follows:

- I part - Reiterated observations raised in the letters of observations regarding the entrustment request under IPARD submitted by Montenegro in December 2015 (letter of closure with recommendations from 25th October 2017 – Ares (2017)5220251 - 25/10/2017; Ares (2016)5055192 dated 06/09/2016 and Ares (2017)2326805 dated 05/05/2017) – 2 recommendations are still open.
- II part - Follow up on the observation and recommendation issued by DG AGRI letter Ares (2018)910511 from 16/02/2018 – no open recommendations, i.e. all recommendations are implemented.
- III part - Follow up on the observation and recommendation issued by DG AGRI letter Ares (2019)7226447 from 22/11/2019 – out of 5 recommendations, 2 recommendations remains open, 2 are partially implemented and 1 recommendation is implemented.

When it comes to the follow up on AA recommendations, IPARD Agency took appropriate actions and out of 22 recommendations issued during 2018, 19 are implemented, 2 partially implemented and 1 remains open. Main reason for open recommendations is their non-acceptance by IPARD Agency as presented in Annex 3.

## **8. OTHER INFORMATION**

The IPARD Agency has adopted version 2.0 of the Manual of procedures on 31<sup>st</sup> January 2020. AA will take into account these changes during following audits. The part of changes was covered within follow up on the observation and recommendation issued by DG AGRI letter Ares (2019)7226447 from 22/11/2019.

## **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.**

Based on scope of audit performed we have obtained reasonable assurance for the results presented within this Report. The overall level of assurance on the proper functioning of the management and control systems is the result of the system audit and the audit of operations including the results of the audit of accounts carried out for the expenditure declared to the European Commission for the FY 2019:

- By auditing the accounts, we have obtained a reasonable assurance that the amounts stated in the annual accounts are correct, accurate and true (described in Chapter 6 of this Report).
- Since we audited all operations within population, we have obtained a reasonable assurance on the legality and regularity of the expenditure declared to the Commission (described in Chapter 5 of this Report).

- As a result of audit of the management and control system and the audit of the operations we have obtained a reasonable level of assurance for overall conclusion and the system has been rated as "Works" (Medium impact). All risks are adequately addressed by controls which are likely to operate effectively with deficiencies having a moderate impact on the functioning of the accreditation criteria. Recommendations have been formulated and issued to the management and operating structure as described in annex 1 of this Report.

**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.**

Since we audited all operations within population, we defined total amount of error as known which is above the materiality level. However, we don't assess errors identified in population as serious deficiencies in the functioning of the management and control system during the year. Amount of the error is mainly affected by one operation, wholly identified as ineligible which don't present systematic nature of error (see finding no 2, part II of Annex 1 of this Report ).

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

The corrective actions to be taken with regard to the improvement of the management and control systems and the correction of errors arising from both system audit and audit of operations are set out in Chapters 4 and 5 of this report.

With regard to irregular expenditure, relevant provisions of the Sectoral and Framework Agreements should be followed in the efficient manner.

**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.**

There were no subsequent adjustments made and corrective actions taken.

## 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 the 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	%	%	%		

	2014ME0614 NP001	Programme for Agriculture and Rural development of Montenegro - IPARD II	1.367.201,03	1.367.201,03	100	8	8	49.525,80	3.62	3.62	/	3.62	/	/
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## 11. ABBREVIATION AND ANNEXES

**Annex 1 – Findings and recommendations**

**Annex 2 – Follow up on remaining DG AGRI recommendations**

**Annex 3 – Follow up on previous AA recommendations**

**Annex 4 – Error evaluation**

**Annex 5 – Non-operational transaction**

List of abbreviation

AA	Audit Authority
AAAR	Annual Audit Activity Report
AAO	Annual Audit Opinion
AFCOS	Anti - fraud Coordination Service
AMD	Annual Management Declaration
AWP	Annual Work Plan
CFF	Cash flow forecast
CHU	Central Harmonization Unit
DAB	Department for Accounting and Budget
DAP	Department for Authorisation of Payments
DEP	Department for Execution of Payments
DG AGRI	Directorate-General for Agriculture and Rural Development
DMS	Directorate for Management Structure
DOSC	Department for On-the-spot control
DP	Directorate for Payments
DPAP	Department for Publicity and Authorisation of Projects
EC	European Commission
EU	European Union
FA	Financing Agreement
FY	Financial Year
FwA	Framework Agreement
HNFD	Head of National Fund Division



IA	IPARD Agency
IAD	Internal Audit Department
IPA	Instrument for Pre-accession Assistance
ICFR	Internal Control Framework Requirement
IPARD II Programme	Programme for the Development of Agriculture and Rural Areas in Montenegro
KPIs	Key Performance Indicators
LEE	List of eligible expenditures
MA	Managing Authority
MARD	Ministry of Agriculture and Rural Development
MCS	Management Control System
MF	Ministry of Finance
MIDAS	Montenegro Institutional Development and Strengthening project
MOP	Manual of Procedures
MPA	Ministry of Public Administration
NAO	National Authorising Officer
NAOSO	The NAO Support Office
NF	National Fund Division
NIPAC	National IPA coordinator
OG	Official Gazette of Montenegro
OTSC	On the spot control
RC	Risk Coordinator
RfF	Request for Funds
RM	Risk Manager
RMP	Risk Management Panel
RPD	Reference price Database
SA	Sectorial Agreement
SSOs	System Supervision Officers
WLA	Work Load Analysis