



MONTENEGRO
AUDIT AUTHORITY

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ANNUAL AUDIT ACTIVITY REPORT
OF THE AUDIT AUTHORITY FOR
ANNUAL COUNTRY ACTION PROGRAMME FOR
THE MONTENEGRO FOR THE YEAR 2014

FOR THE PERIOD FROM 01 JANUARY UNTIL
31 DECEMBER 2017

Podgorica, March 2018

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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
CFCU	Central Finance and Contracting Unit
DMS	Directorate for Management Structure
DPW	Directorate for Public Works
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
RAF	Risk Alert Form
RMP	Risk Management Panel
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 should submit 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.

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 on 1 January to 31 December 2017.

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

In the period January – February 2018 the AA performed follow-up of the findings and recommendations given in the course of audit conducted in the period covered by this report. Follow-up was performed as a separate activity before issuing the AAAR and the AAO.

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). Within this Programme 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 December 2015.

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

Structures and bodies being part of the management and control system of this Programme are, as follows:

- National IPA Coordinator,
- The National Authorising Officer,
- The Operating structure consisting of:
 - the NIPAC office;
 - Implementing Agencies: Central Finance and Contracting Unit (CFCU) and Directorate for Public Works (DPW);
 - PIUs in the Line Ministries (MF, MSDT, MEC, MTMA)
- The National Fund Division acting as the management structure and performing the functions and tasks of the National Fund and the support office for the NAO.

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 2017. During 2017 the AA carried out system audit. In the period from January - February 2018 AA performed follow-up of the findings and recommendations given in the course of audit conducted in the period covered by this report and audit of the annual financial reports for 2017.

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 and the consistency of the management declaration with regard to performed audit work.

Based on the available information 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

2.1. Personal changes

- Ms Marija Radenović requested from the Government of Montenegro to be dismissed from the General Director. This request was issued at the session of the Government of Montenegro held on 23rd February 2017. At the same session, Mr Katarina Živković was appointed as the acting General Director of Directorate for Financing and Contracting of the EU Assistance Funds –CFCU. The NAO informed the EC about this change on 27th February 2017 (letter No 06-1044/1/1).
- Head of National Fund Division, Ms Dunja Nelević left her position on 22nd March 2017. By the letter no 06-1044/1 from 27th February 2017, NAO informed EC on planned leave of the head of National Fund Division.
- At the session of the Government of Montenegro held on 18th May 2017, Director of Directorate for Public Works (Head of IA) Mr Milan Martinović was replaced by Mr Almer Kalač. NAO informed EC about this change.
- Government of Montenegro at the session held on 16th June 2017 appointed Ms Emina Mujević Kara as Acting Director of Directorate for International Cooperation and EU Funds (SPO of MTMA/PIU). The NAO informed the EC about this change on 3rd August 2017 (letter No 06-3882/1).
- Government of Montenegro at the session held on 14th September 2017 adopted Decision on termination of the mandate of the Ms Marija Vukčević, Director General of the Directorate for EU integration and International Cooperation within Ministry of Sustainable Development and Tourism (PIU) who performed function of SPO. Based on official authorization made by Minister of MSDT, SPO function was taken over by Mr Saša Radulović, State Secretary in charge of policies in the area of environment. The NAO informed the EC about this change on 11th October 2017 (letter No 01-17646/1).
- Ms Dragica Sekulić was replaced by Mr Radosav Babić in June 2017 as a SPO/Acting Director General in the Directorate for Transformation and Investments in the MEC/PIU. The NAO informed the EC about this change on 3rd August 2017 (letter No 06-3882/1).
- At the session held on 14th September 2017 the Government of Montenegro adopted the Decision on termination of term of office of Katarina Živković acting director of Directorate for financing and contracting of EU funds in the Ministry of Finance (CFCU acting as IA), due to termination of 6 months' period. At the same session the Government of Montenegro adopted the Decision on appointment of Bojan Paunović as acting director of Directorate for financing and contracting of EU funds in the Ministry of Finance (CFCU acting as IA). The NAO informed the EC on the replacement of General Director of Directorate for Finance and Contracting of the EU Assistance Funds by the Letter No 01-17646/1, from October 11th 2017.
- Change of NAO - By the Decision no. 01-06-5101/1 from 09/10/2017 the Minister of Finance Darko Radunović appointed Mr Nemanja Katnić – state secretary in the

Ministry of Finance as a National Authorising Officer (NAO). EC was informed about this change by letter No. 01-17646/1 from October 11th 2017.

- By letter No.01-21222/1 from 1st December 2017 the NAO, Mr Nemanja Katnić, has informed EC that IPA activities of General Director of the Directorate for Management Structure (Deputy NAO) will be performed by Ms Ivana Maksimović. Ms Maksimović is appointed by the Government of Montenegro on November 16th 2017 as Acting Director General of the Directorate for Management Structure.

2.2. Organizational changes

- In March 2017 the Government of Montenegro adopted Amendments of Decree on changes and amendments of the Decree on the public administration and manner of work (OG MN 19/2017) by which the Directorate of Public Works (DPW/IA) is organised as a separate body within Ministry of Sustainable Development and Tourism (MSDT/PIU). NAO informed EC about this change.
- Rulebook on internal organization and systematization of the Ministry of Sustainable Development and Tourism was adopted in April 2017. By the new Rulebook MSDT (PIU) in part related to DPW/IA (separate body within MSDT), internal organizational units of DPW are: Sector for planning and preparation of projects, sector for contracting and financing projects and sector for monitoring of projects realization. Overall number of systematized job positions for carrying out activities from the scope of competence of the Directorate of Public Works is 50. 30 out of 50 job positions have been envisaged for IPA activities. NAO informed EC about this change.
- The Government of Montenegro on its session held on March 30th 2017 adopted a new Rulebook on internal organization and systematization of the Ministry of Transport and Maritime Affairs (MTMA/PIU). Comparing the previous and the new Rulebook we determined that Department for Management of EU Funds becomes Directorate for international cooperation and EU Funds. Envisaged numbers of job positions are raised from 3 to 7 including Director of Directorate (SPO). The NAO informed the EC about this change on 3rd August 2017 (letter No 06-3882/1).
- Rulebook on internal organisation and systematisation of the Ministry of Economy (PIU) was adopted in May 2017, and PIU was transferred from Directorate for Energy Efficiency to Directorate for Transformation and Investments. The NAO informed the EC about this change on 3rd August 2017 (letter No 06-3882/1).
- By the new Rulebook on internal organization and systematization of the Ministry of Finance which was adopted on 26 October 2017 Directorate for managing structure is established. Within this Directorate there are two divisions: Division for System Supervision (for the support to the NAO) and Division for National Fund (for financial issues). The NAO informed the EC about this change on 1st December 2017 (letter No.01-21222/1).

Lack of respect of procedures, relating to planning and implementation of changes in MCSS, in the previous period caused significant problems in system functioning. Namely, in April 2016 there was a change of systematisation and organisation act in DPW (IA for CAP 2014 and IB for OPRD 2012-2013- IPA component III). AA audited this issue through system audit on functioning in NF (Final audit Report from November 2016) and recommended that NAO should undertake activities in order to provide respect of the prescribed procedures in relation to changes in MCSS by all bodies in MCS and impede implementation of changes without prior approval. Also, we recommended that NAO, in compliance with his responsibilities and available mechanisms, ensure proper functioning of reporting and information system in order to, inter alia, be able to keep under constant surveillance IPA bodies for which he is directly responsible and thus monitor permanent fulfilment of all requirements so that this accreditation could be kept.

During audit activities we determined that the progress was made in respect of the prescribed procedures in relation to changes in MCSS occurred in 2017 as well as that certain activities were taken regarding change of procedures related to informing on changes in the system.

Bearing in mind the frequency of changes, especially in the key positions of the system and that it represents a risk that may affect its functioning, this process will be subject of audit engagement in the forthcoming period.

The changes that occurred in MCSS in 2017 do not have an impact on the audit work.

3. CHANGES TO THE AUDIT STRATEGY

There was no change in Audit Strategy 2017-2019 for the IPA II 2014-2020 for the Annual Country Action Programme for Montenegro for the year 2014 of the Audit Authority, approved by Auditor General and submitted to EC on 29 November 2016.

According to the Audit Strategy we carried out system audit.

4. SYSTEMS AUDITS

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

In accordance with the Audit Strategy 2017-2019 for the IPA II 2014-2020 for the Annual Country Action Programme for Montenegro for the year 2014 (hereinafter: CAP 2014), approved by Auditor General and submitted to EC on 29 November 2016, the AA of Montenegro conducted an audit of the management, control and supervision system (hereinafter MCSS) established in the bodies of Management structure: National Fund/NAO support office and in the bodies of Operating structure: NIPAC office; Implementing Agencies: Central Finance and Contracting Unit (CFCU) and Directorate for Public Works (DPW) 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

Based on risk assessment performed during preparation of the Audit Strategy 2017-2019 for the purpose of defining audit areas for each body of CAP 2014 at the key requirement/process/function level (further: process level) audit engagement encompassed all bodies dealing with CAP 2014.

In the period from January – March 2018 AA carried out follow-up of the findings and recommendations given from the performed system audit in 2017. Follow-up was performed as a separate activity before issuing the AAAR and the Annual Audit Opinion (AAO).

Summary of the audit carried out is in the following table:

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)
01.01.2017. -31.12.2017	Annual Country Action Programme for Montenegro for the year 2014 - C(2014) 9387	Audit Authority of Montenegro	All bodies	February to mid-July 2017	Human recourses and internal organization	<u>Lack of staff, recruitment and retention policy</u> Given that there is a lack of staff in all IPA bodies caused by staff leaving, improvements are needed in terms of recruitment of staff, as well as appropriate implementation of retention policy in practice in order to prevent loss of quality staff, because leaving of trained employees can have a great impact on the quality and continuity of business operation.		n/a	Open
						<u>Organizational structure NFD and NAO SO</u> NF and NAO SO have been established within the same Division within Ministry of Finance and not operationally and functionally separated and independent.		n/a	Closed
			All bodies	"	IT Policy	<u>Backup of data</u> IPA bodies do not have adequate data backup. Therefore, data storage is not properly secured and some improvements are needed.		n/a	Open
						<u>Contingency plan developed</u> All bodies of Operating Structure and Management structure of IPA II do not have contingency plan developed. There is a risk of continuity of operations concerning loss of data, absence of individuals, and some other unpredictable situations.		n/a	Open
			All bodies	"	Risk Management	<u>Risk Management</u> In all audited bodies the risk management relating to IPA II CAP 2014 was not satisfying. Some improvements are needed in terms of more serious approach related to risk management activities by all actors in the system.		n/a	Open
			MSDT/MTM A/MEC/MF/ CFCU/NF	"	Internal Audit	<u>Internal audit capacities</u> Internal audit capacities in all IPA bodies are insufficient 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 top managers will not have additional assurance about functioning of their systems or independent review on effectiveness and efficiency of the system.		n/a	Open
			<i>NIPAC Office</i>			<u>Lack of internal audit function</u> Internal audit function has not been established within Ministry for European Affairs in any manner prescribed by The Law on the System of Internal Financial Control in Public Sector.		n/a	Closed

			NF/IAs/PIUs	“	Financial Management	<p><u>Written Procedures related to chapter Financial management</u></p> <p>MOP chapter Financial management with annexes has some deficiencies.</p>		n/a	Open
			NIPAC, Head of NIPAC Office, SPOs	“	Programme/ Action Monitoring	<p><u>Reports on implementation</u></p> <p>Procedures in respect to preparation of Annual Implementation Report for 2016 have not been fully implemented and respected.</p>		n/a	Open
			NIPAC Office			<p><u>Organising of Monthly Meetings with SPOs/PIUs</u></p> <p>Monthly meetings have not been organised by NIPAC Office.</p>		n/a	Open
						<p><u>SMC Rules of Procedures</u></p> <p>Sectoral Monitoring Committee Rules of Procedures have been drafted, but procedure of its adoption has not been finished.</p>		n/a	Open
			IAs, PIUs	“	Contract Procedures	<p><u>Inadequate performing of Contract Procedures</u></p> <p>There are deficiencies in the design and tendering phase of the contracting process. The deadlines for design and tendering phase are not respected, furthermore some of them even have not started, which may have an impact on the signing and the implementation of the contracts.</p>		n/a	Open

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

By the strategic audit planning (Audit Strategy 2017-2019 for the IPA II 2014-2020 for the Annual Country Action Programme for Montenegro for the year 2014) for the purpose of defining audit areas the Audit Authority performed risk assessment for each body of Annual Country Action Programme for Montenegro for the year 2014 at the key requirement/process/function 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.

In order to distinguish between the factors with varying importance, we gave the weight to the specific risk factors and calculated the total score for each process in each body. First, we identified horizontal processes in all bodies and we calculated the total score for each identified horizontal process at the level of individual body. Second, we identified specific processes in each body and calculated the total score for those processes in each body. After that, we calculated the total score for each horizontal and specific process within OP.

On the basis of results of risk assessment the audit engagement encompassed all bodies dealing with CAP 2014 and the following audit areas were examined: Human resources and internal organization, IT policy, Risk management, Process of planning, assessment and approval of changes in MCSS, Internal audit and AMD- all bodies; Financial management – PIUs (MTMA, MSDT, MF MEC); IAs (CFCU, DPW) and NF; Accounting – IAs (DPW, CFCU) and NF; Programme action monitoring – NIPAC office; Contract procedures – PIUs (MTMA, MSDT, MF, MEC) and IAs (CFCU, DPW); Bank accounts system – NF and Verifications by the NAO – NAO support office.

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 recommendations which were identified during the audit process in each body 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 15 findings: 1 of them is major, 12 are intermediate and 2 is minor.

Further below there is a description of the principal findings (major and intermediate) identified, corrective measures undertaken by auditees and audit conclusions.

➤ Human Recourses and Internal organization

Regarding this audit area we identified one (1) major and one (1) intermediate finding.

Finding - Lack of staff, recruitment and retention policy

Finding with major level of priority which refers to lack of staff, recruitment and retention policy is identified in all bodies dealing with CAP 2014.

Namely, 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.

Apart from the above stated, we determined a significant employees' turnover during 2016 and 2017 in all IPA bodies, dealing with CAP 2014, which 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.

Therefore, we recommended taking necessary measures as urgently as possible and accelerating activities with a view to recruiting lacking number of employees which would further influence on 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 necessity of additional efforts in order to establish policy of staff retention which can respond to the expected scope of work and fluctuation of employees.

Results of follow-up

We determined through follow-up that all bodies had actively participated in implementation of recommendations and had taken corrective actions. The number of employees dealing with CAP 2014 has increased since our audit engagement as stated in table below:

Auditee	Envisaged Work post related to IPA jobs by Rulebook	Result of WLA/2017	Employed June 2017	Results of follow-up in February 2018	
				Envisaged Work post related to IPA jobs by Rulebook	Currently employed
NF/NAO SO	8 - including NAO	10	7 (LTEC)	12-including NAO	8(LTEC)
NIPAC Office	11 - Including NIPAC	9	7 (6 – LTEC, 1-TEC)	11 - Including NIPAC	7 (6 – LTEC, 1-TEC)
CFCU	21 - Including Head of IA	37	19 (18-LTEC; 1-TEC)	37 - Including Head of IA	24 (17-LTEC; 7-TEC)
DPW	30 - Including Director (Head of IA)	27	22 (21-LTEC;1-TEC)	30-Including Director (Head of IB)	21 (20-LTEC; 1-TEC)
MF	4 - including SPO	4	3(LTEC)	4 - including SPO	3(LTEC)
MSDT	8 - including SPO	8	6 (5-LTEC;1-TEC)	9-including SPO	9 (7-LTEC;2-TEC)
MTMA	5 - Including SPO	7	3 (LTEC)	5 - Including SPO	5 (LTEC)
MEC	5 - including SPO	5	5(3-LTEC; 2-TEC)	5 - including SPO	5(3-LTEC; 2-TEC)

When it comes to retention and motivation policy, according to information obtained from DMS during follow-up, certain steps in finding the best model for this issues for IPA staff at high management level have been undertaken. Having in mind that the progress in implementation of recommendations is noted, level of priority is decreased to intermediate and **finding remains open.**

Finding - Organizational structure NFD and NAO SO

The management structure is established in the way that function of NF and NAO SO are performed by the same Division for National Fund within Ministry of Finance which means that NF and NAO SO are not operationally and functionally separated and independent. The cause of this is that valid Rulebook of internal organisation and systematisation predicts that all tasks within the competence of NF and NAO SO are organised within the same Division, i.e. Division for National Fund and managed by Head of National Fund who performs final verifications in most important processes. It may have an impact on overlapping the functions, may lead to a conflict of interest of a staff member, and may limit the implementation of the "four eye" principle and adequate performance of tasks and duties of National Fund and NAO Support Office.

Therefore, we recommended organizational and functional separation between National Fund and NAO Support Office in order to ensure efficiency and regularity in fulfilling the tasks within their competence.

Results of follow-up

By new Rulebook on internal organisation and systematisation of the Ministry of Finance which was adopted on 26 October 2017, new Directorate for managing structure is established. Within this Directorate there are two divisions: Division for System Supervision (for the support to the NAO) and Division for National Fund (for financial issues). **This finding is closed.**

➤ IT Policy

Regarding this audit area we identified two (2) intermediate findings.

Finding - Backup of data

This finding is identified in all bodies dealing with CAP 2014. Namely, 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. Therefore, there is a risk of loss of data in case of error in information systems in which information is destroyed by failures 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.

Therefore, 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.

Results of follow-up

With a view to improving the IT security of IPA management national authorities started with preparation of an individual Action plans for the implementation of a framework of 17 baselines of information security. On the basis of this Action Plan relevant indicators and goals will be measured.

Compared to the previous period a significant progress is made towards raising awareness on IT security and providing adequate archiving and back-up of data. However, this **finding remains open**.

Finding - Lack of contingency plans

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.

Therefore, we recommended that it be necessary to develop a contingency plan with clear responsibilities.

Results of follow-up

Business continuity plans is not developed. **Finding remains open**.

➤ **Risk Management**

Regarding this audit area we identified one intermediate finding. Finding concerning risk management in all audited bodies was based on the fact that management of risks relating to IPA II CAP 2014 is not satisfying.

Risk relating to lack of staff is identified as general in all IPA bodies. However, assessment and management of risk, in relation to the functioning of the system, caused by lack of staff in MF-PIU, are not taken into consideration. Also, Risk manager has not been appointed and SPO has attended no Risk Management Panel. In this specific case, having in mind role of PIU in tendering, evaluation of tenders, contracting, implementation of contracts, reporting, monitoring at action level, lack of adequate risk management finally leads to serious problems in implementation of the largest number of actions under CAP 2014.

Additionally, by the insight into the Action Plans of IPA Bodies we determined that certain high level risks were identified, for which mitigating actions overcome the competence of the IPA body. Also the number of risks identified in the Action Plans is present for a long period. For example, risk regarding the CFCU premises, which is important for all components/areas, has been assessed as high and present since July 2015. CFCU is still in the same premises.

Also, the outflow of trained staff, both at managing and operative level has been identified at the very beginning of programs implementation from IPA I perspective and constantly present in all institutions up to now, affecting the programs from IPA II perspective, including CAP 2014. Therefore it has been determined that no adequate measures have been taken with a view to conducting retention policy. Inadequate management of this risk led to outflow of staff with the proper knowledge and experience, which significantly affects the smooth implementation of the programme CAP 2014.

Bearing in mind that the process of risk management is one of the key processes in organisation because of its role in achieving objectives of organisation, we recommended convoking ad-hoc RMP meeting, in order to discuss detected risks that have severe impact on the effective functioning of the management and control system and proposing relevant corrective actions.

Also, we recommended filling the RAF in line with procedures, that Risk Manager or his/her substitution attend all RMPs, that new Risk manager in MTMA should be provided with the trainings for performing his tasks and that Risk manager in MF-PIU should be appointed.

Results of follow-up

During performed follow-up we determined that progress was made in implementation of our recommendations.

Based on the review of documentation, we determined that it was decided to introduce quarterly meeting at the top management level (this obligation is included in the national Decision on appointment of persons responsible for decentralised and/or indirect management of EU funds), as well as proposal for the ad hoc meetings upon need.

During January 2018, NAO/DMS initiated coordinative meetings with all IPA structures in respect to critical points and key risks that should be maintained and resolved at the level of IPA management. Meetings were held with all IPA stakeholders and relevant conclusions were made and will be monitored through additional risk assessment.

Risk Manager of the PIU MF has been appointed.

Awareness of the risks is raised to a higher level, but not to the extent that the very risk identification is sufficient but that the key to successful risk management is consideration and resolution of problems before it is too late to address them effectively. **Finding remains open.**

➤ **Internal Audit**

Regarding this audit area we identified two (2) intermediate finding.

Finding - Internal audit capacities

This finding is identified in MSĐT/MTMA/MEC/MF/CFCU/NF 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 will not have additional assurance about functioning of their systems or independent review on effectiveness and efficiency of the system.

In order to ensure timely and effective execution of internal audit function described in their procedures and plans, our recommendation was related to increasing capacities of internal audit with a view to achieving higher coverage of audit areas. It would have a high impact on implementation of IPA funds which would provide management with additional assurance of functioning of the IPA MCSS.

Results of follow-up

During follow up we identified that capacities of internal audit did not increase. **This finding remains open.**

Finding - Lack of internal audit function

Internal audit function has not been established within Ministry for European Affairs in any manner prescribed by The Law on the System of Internal Financial Control in Public Sector. Namely Internal Audit Unit is not foreseen within Ministry by Rulebook on internal organization and systematization nor was agreement signed with another entity in order to ensure conducting of internal audit function by internal audit unit of that entity.

Therefore, we recommended establishment of internal audit function in accordance with Article 18 of The Law on the System of Internal Financial Control in Public Sector.

Results of follow-up

Ministry of European Affairs concluded the Agreement on entrusting the internal audit tasks with the Ministry of Finance which ensures conducting of internal audit function. **This finding is closed.**

➤ **Financial Management**

Regarding this audit area we identified one intermediate finding. Finding which refers to Written Procedures related to chapter Financial management is identified in NF/IAs/PIUs. The MOP chapter of the Financial Management with annexes was not in accordance with the new information system and relevant regulations. Alignment of procedures with new information system and relevant regulation is necessary.

Results of follow-up

New version of the MoP (version: 2.0) is under preparation. This version will include new Information system that is used and alignment of procedures. **The finding remains open.**

➤ **Programme/Action Monitoring**

Regarding this audit area we identified three (3) intermediate finding.

Finding - Reports on implementation

Finding is identified in 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.

Therefore, 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.

Results of follow-up

Procedures in relation to the preparation and submission Annual Implementation reports are not conducted and communication between NIPAC Office and PIUs is not improved. Therefore, **this finding remains open.**

Finding - Organising of Monthly Meetings

During the audit performed and based on the insight into submitted documentation, we determined that monthly meetings with SPOs/PIUs had 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 the relevant information must be distributed to all interested parties in order to ensure efficient and effective system functioning.

Therefore, we recommended that the Head of NIPAC Office organise regularly monthly meetings with SPOs/PIUs.

Results of follow-up

The NIPAC Office has launched an initiative for changing of the MoP Chapter Programme/Action Monitoring. Namely, new version of the MoP (version: 2.0) is under preparation and quarterly meetings with SPOs will be foreseen, instead of monthly meetings (since there are already monthly meetings on CAP contracting, held between the CFCU and EUD, with participation of NIPAC Office). **The finding remains open.**

Finding - SMC Rules of Procedures

During the audit performed, we determined that Sectoral Monitoring Committee Rules of Procedures had been drafted, but procedure of its adoption had not been finished. Therefore, we recommended to NIPAC Office to initiate the procedure for approval and adoption of Sectoral Monitoring Committee Rules of Procedures.

Results of follow-up

Bearing in mind that the auditee did not submit evidence on the fulfilment of the recommendation, **the finding remains open.**

➤ **Contract Procedures**

Regarding this audit area we identified one (1) intermediate finding in IAs, PIUs which refers to Inadequate performing of Contract Procedures.

There are deficiencies in the design and tendering phase of the contracting process. The deadlines for design and tendering phase are not respected, furthermore some of them even have not started, which may have an impact on the signing and the implementation of the contracts.

Taking into consideration that in the period under review neither one contract is signed, the fact that Financing Agreement was signed in December 2015 and the final date for concluding procurement and grant contracts is 3 years following the date of conclusion of the Financing Agreement, it is very important to improve correspondence between the bodies included in contracting process in order to avoid risk of failing to conclude the contracts within the deadlines.

Therefore, we recommended respecting the procedures and significantly improving the communication and coordination between the bodies included in contracting in order to conclude the contracts within the deadlines, which influences on better and more efficient management and use of IPA funds at disposal of Montenegro.

Results of follow-up

Progress has been made in terms of the number of contracts concluded (three contracts were signed in December 2017). Taking into consideration breaching of deadlines set for contracting, it is evident that improvements and capacity building on each level is necessary. Coordination and communication between IAs with PIUs and PIUs with beneficiaries should still be improved in order to shorten the long processes of tendering and evaluation. **The finding remains open.**

4.5 Level of assurance obtained following the system audits and justification.

Considering the assessment of the management, control and supervision systems established for IPA II Annual Country Action Programme for Montenegro for the year 2014, 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.**

5. AUDITS OF SAMPLES OF TRANSACTIONS

The AA was not in a position to perform audit of operations, because in the period from 1 January 2017 until 31 December 2017 there were no declared expenditures to EC.

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

It should be noted that under IPA II CAP 2014 the contracts were signed (Total Amount Contracted - 1,288,318.25€). However, no payments were made to the contractors and no expenditure were declared to the European Commission in the financial year 2017.

Having in mind that Montenegro received advance payment for the Programme CAP 2014 in the amount of 8.631.998,96 € our audit was limited, i.e. focused only on the volume of Union funds on the MF – NF CAP 2014 Account and related procedures.

In line with above mentioned, Audit Authority has performed reconciliation of the balance of the CAP 2014 Euro Account declared in the Annual financial report with the bank statement of the CAP Euro account and has verified that amount stated in the Annual financial report

corresponds to the amount on the bank statement. We have identified that advance payment is recorded in accounting books.

7. FOLLOW-UP OF PREVIOUS YEARS' AUDIT ACTIVITY

Not applicable.

8. OTHER INFORMATION

Not applicable.

9. OVERALL LEVEL OF ASSURANCE

The Audit Authority performed system audit in 2017. The Audit Authority did not perform audit of operations in the reference period since no expenditure were declared to the European Commission in the financial year 2017.

Regarding the above mentioned, the AA does not have all necessary elements to express overall assurance on the proper functioning of the management and control system.

10. TABLE FOR DECLARED EXPENDITURE AND SAMPLE AUDITS

Not applicable.

