

# 2013

Republic of Macedonia

Ministry of Finance

Public Internal Financial  
Control Department

**2013 ANNUAL REPORT**  
**ON THE FUNCTIONING OF PUBLIC INTERNAL FINANCIAL CONTROL SYSTEM**

Skopje, July 2014

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## SUMMARY

2013 Annual Report on the Functioning of Public Internal Financial Control is a report on the functioning of the system of financial management and control and internal audit in the public sector in the Republic of Macedonia in 2013. It is prepared in line with intent 11, Article 48 of the Law on Public Internal Financial Control ("Official Gazette of the Republic of Macedonia", Nos. 90/2009, 12/2011 and 188/2013) and the Rulebook on the Form and the Contents of Reports and Statement on Quality and Status of Internal Controls of the Annual Financial Report ("Official Gazette of the Republic of Macedonia", Nos. 147/20 10 and 34/2011).

In 2013, 87% of public sector institutions at the central level and 72% of public sector entities at the local level met the obligation for submission of annual report on **financial management and control** functioning, and compared with 2012, accounts for 4 percentage points decrease at the central level and 5 percentage points increase at the local level.

Data provided in the submitted annual reports on financial management and control functioning show the following progress achieved in 2013: new Financial Affairs Units were established in 22% of the entities (17) at central level and Heads of Financial Affairs Units were appointed in 6.6% of entities (5) at central level.

Progress was also achieved in implementing the decentralised public funds management system in terms of adopted decisions on internal distribution of total approved budget and conferred general mandates. In 2013, compared with the previous year, progress achieved at both central and local level accounted for 26 percentage points and 29 percentage points respectively.

In 2013, 75% of public sector entities at the central level and 64% of public sector entities at the local level met the obligation for submission of Annual Report on Audits and **Internal Audit** Activities.

Data provided in the submitted annual reports on audits and internal audit activities in 2013 and records of the Central Harmonization Unit show the following progress achieved: number of internal audit units increased by 4% at the central level and by 1.5% at local level, number of internal auditors increased for 3% at the central level and by 6.7% on a local level. Percentage of implementation of recommendations at central level remained unchanged compared to 2012, while it increased by 4% at local level. In addition, percentage of implemented ad-hoc audits surged by 19% at central level.

In the course of 2013, number of appointed Heads of Internal Audit Units at central level increased by 7%, i.e. from 44 in 2012 to 47 in 2013.

Recommendations not being implemented decreased by 7.4 percentage points at central level, while percentage of partially implemented recommendations increased by 8%. In 2013, efficiency and effectiveness in carrying out audits intensified, as indicated by the reduced number of auditing days per audit.

At local level, number of reports submitted in 2014 increased by 6% compared to 2012, as well as the number of carried out audits, which grew by 24%. Percentage of partially implemented recommendations increased by 3%, while number of recommendations for which there is no information about their implementation dropped by 14%.

"Training of Internal Auditors in the Public Sector" Project was implemented in 2013, whereby 45 auditors acquired CIPFA International Certificate in Public Sector Internal Auditing.



## INTRODUCTION

In the recent several years, Republic of Macedonia has been intensively implementing reforms for development of public finance management.

Most of these reforms are being implemented as a result of the need to adapt and improve the existing systems for management and control of public funds in line with the EU requirements.

The reforms are aimed not only at meeting the requirements for European Union membership, but also at improving the management and the control of public funds, thus enabling us to better use the possibilities for utilization of EU funds and, as a future member state, to be ready to deal with the challenges the EU membership entails.

Establishment and development of the Public Internal Financial Control System in the Republic of Macedonia is among these reforms.

Its aim is development of a comprehensive system of internal financial control in the public sector, which will provide for establishment of a sound financial management of public funds. The reform is part of the preparatory process of our country for successful EU access negotiations under Chapter 3.32 Financial Control.

Managers of public sector entities are obliged to establish a public internal financial control system. Ministry of Finance, i.e. Public Internal Financial Control Department, as Central Harmonization Unit, is in charge of coordinating the development, establishment, implementation and maintenance of public internal financial control system.

Objective of the 2013 Annual Report on the Functioning of Public Internal Financial Control System is to inform the Government of the Republic of Macedonia about the activities carried out in 2013 in the field of development of internal financial controls, as well as the current state of play and future guidelines for development of this system. At the same time, European Commission is being informed through the General Section in this Report, since development of this system is of essential importance as regards assessment of the country's readiness to efficiently manage public funds, regardless of their sources, i.e. whether it is a matter of national or EU funds.

### 1.1 Legal Basis and Obligation to Prepare the Report

Pursuant to indent 11, Article 48 of the Law on Public Internal Financial Control ("Official Gazette of the Republic of Macedonia", Nos. 90/2009, 12/2011 and 188/2013), Central Harmonisation Unit is obliged to prepare Annual Report on the Functioning of Public Internal Financial Control System, on the basis of the annual financial reports submitted by the entities.

Ministry of Finance submits this Report to the Government of the Republic of Macedonia by the end of July in the current year at the latest for the previous year. After being considered and approved, its General Section, without the conclusions and the attachments, is also submitted to DG Budget of the European Commission.

Rulebook on the Form and the Contents of the Reports and the Statement on Quality and Status of Internal Controls of the Annual Financial Report defines the manner of preparing the annual financial statements

which are to be submitted to the Central Harmonization Unit no later than 10<sup>th</sup> May in the current year for the previous year.

Following are obliged to prepare and submit Annual Financial Report:

- first line budget users from the legislative, executive and judicial branches (except for the State Audit Office),
- the Funds and
- municipalities and the City of Skopje.

Annual Report on the Functioning of Public Internal Financial Control System includes the following:

- Annual Report on the Activities for Establishment and Development of Financial Management and Control
- Annual Report on Audits and Internal Audit Activities
- Concluding Observations on the Status of Public Internal Financial Control System
- Individual reports on the status of public internal financial control system, separately for each institution as regards financial management and control and internal audit

Annual Report on the Functioning of Public Internal Financial Control System contains data from the annual financial reports of the budget users for the period from 1<sup>st</sup> January to 31<sup>st</sup> December 2013.

156 budget users are obliged to submit Annual Financial Report, 75 out of which are at central level and 81 at local level (80 municipalities and the City of Skopje).

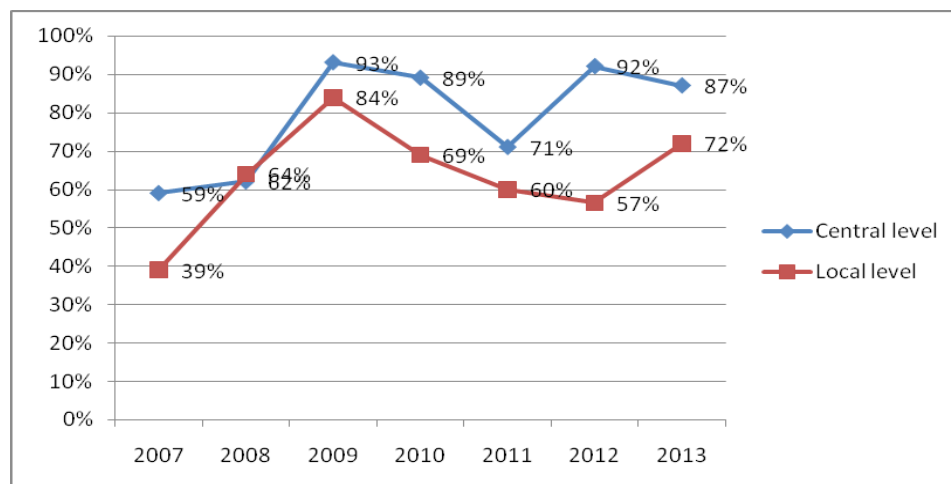


## **REPORT ON FINANCIAL MANAGEMENT AND CONTROL SYSTEM QUALITY AND STATUS**

### **2.1 Submitted Annual Reports on the Functioning of Financial Management And Control**

In 2013, 123 entities, or 79%, submitted Annual Reports on Financial Management and Control, 87% of which were public sector entities at central level and 72% were public sector entities at local level, which compared to 2012, it accounted for 4 percentage points decrease at central level and 15 percentage points increase at local level.

Observed by years, from 2007 to 2013, percentage of submitted annual reports at central and local level is presented below:



## **2.2 Progress achieved in financial management and control in 2013**

Data provided in the submitted annual reports on financial management and control functioning show the following progress achieved in 2013:

- new Financial Affairs Units were established in 22% of the entities (17) at central level,
- Heads of Financial Affairs Units were appointed in 6.6% of the entities (5) at central level,
- Implementation of decentralized public funds management system in terms of adopted decisions on internal distribution of total approved budget and conferred general mandates improved by 26 percentage points at central level and by 29 percentage points at local level.

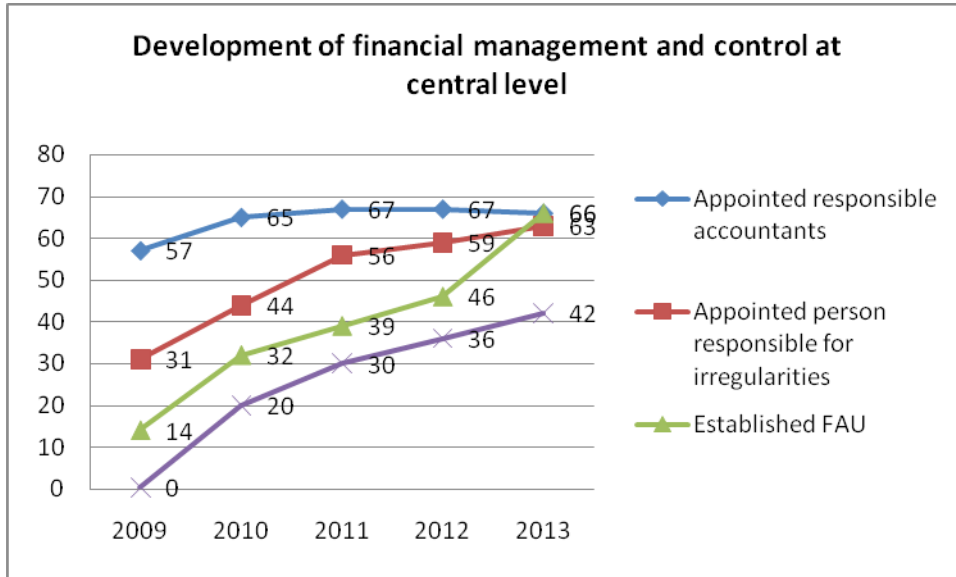
## **2.3 Current state of play as regards financial management and control system as of end-2013 inclusive**

Current state of play as regards financial management and control within 76 first-line budget users at central level and 81 local government units by end-2013 inclusive is as follows:

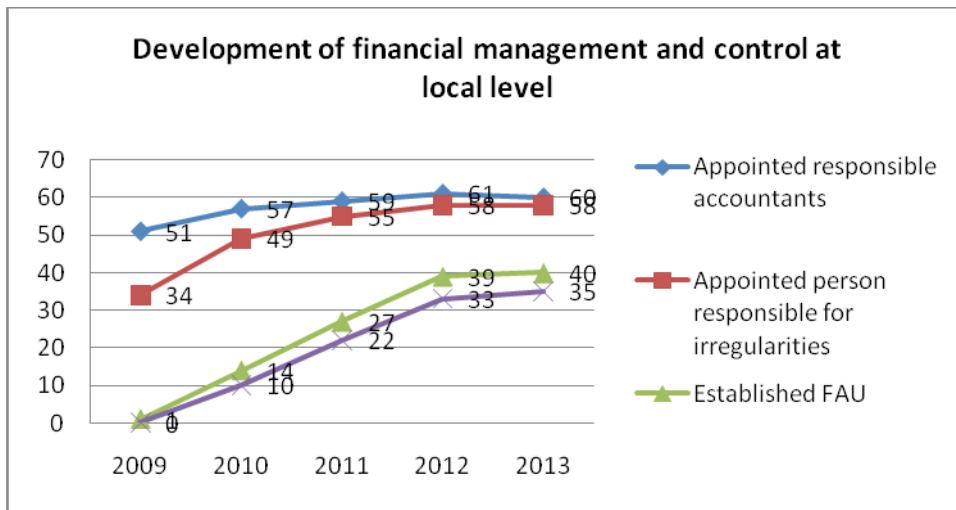
- FAU (departments / unit) were established in 66 (87%) entities at central level and 40 (49%) local self government units, fully implementing the financial management and control;
- Heads of Financial Management and Control Units were appointed in 42 (55%) entities at central level and 35 (43%) local government units;
- Accountants were appointed in 66 (87%) entities at central level and 60 (74%) local government units, pursuant to the Law on Accounting on Budgets and Budget Users and

- Irregularities Officers were appointed in 63 (83%) entities at central level and 58 (72%) local government units, pursuant to Article 50 of the Law on Public Internal Financial Control.

Observed by years, from 2009 to December 2013, financial management at central level is shown below:

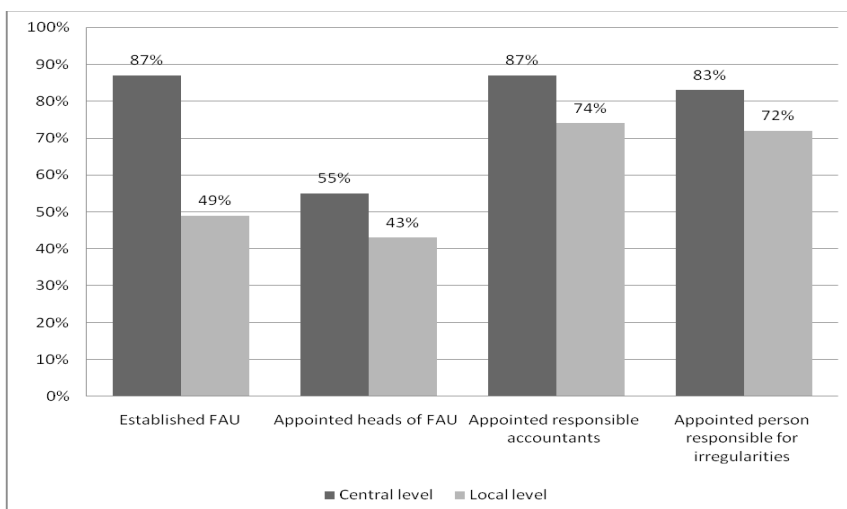


Observed by years, from 2009 to December 2013, financial management at local level is presented in the chart below:



Status of financial management and control at both central and local level as of December 2013 inclusive is shown in the chart below:



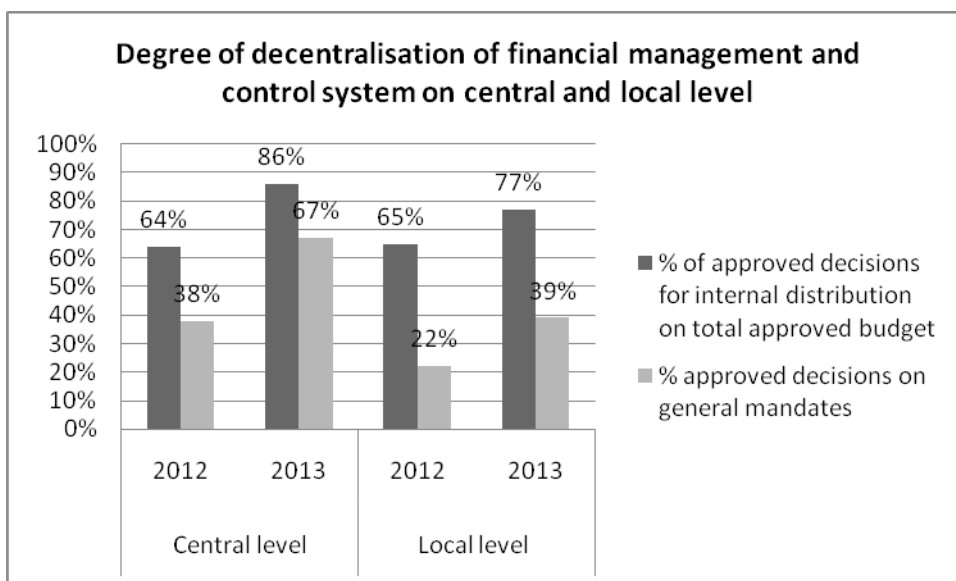


**2.4 State of play as regards establishment of decentralised system of financial management and control as of December 2013 inclusive**

State of play as regards establishment of decentralised system of financial management and control as of December 2013 inclusive is as follows:

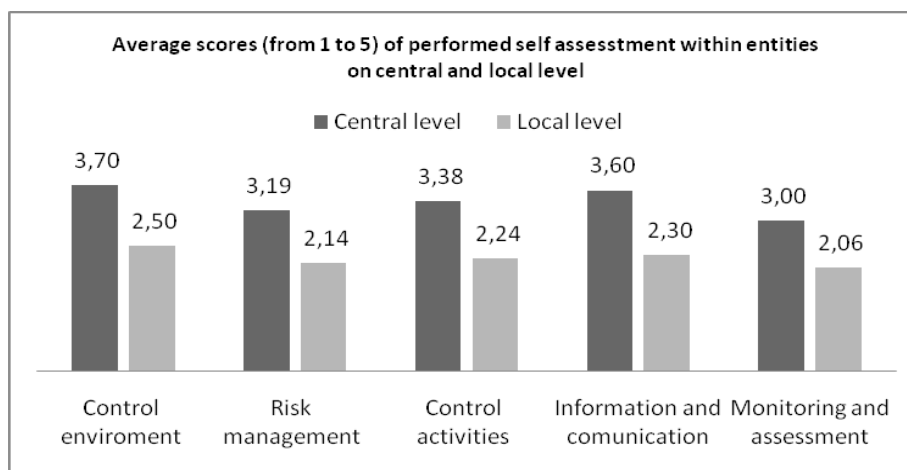
- 65 (85.5%) entities at central level and 63 (77%) municipalities adopted decisions on internal distribution of the total approved budget.
- 51 (67%) entities at central level and 32 (39%) municipalities adopted decisions on general authorizations.

**Status of decentralisation of financial management and control at both central and local level** on the basis of adopted decisions on internal distribution of the total approved budget and adopted decisions on general authorizations as of December 2013 inclusive is presented in the following chart:



## **2.5 Results from carried out self-assessment of financial management and control components**

Average scores from the carried out self-assessment of financial management and control components (1 to 5) at entities at central and local level, presented in the second section of the Annual Report, are the following:



It can be concluded that weakest self-assessed component at central and local level is the monitoring and assessment component.

## **2.6 Weaknesses**

As of December 2013 inclusive, weaknesses detected in establishment and functioning of the financial management and control are the following:

- 13%<sup>1</sup> of central level entities and 51%<sup>2</sup> of local government units did not establish Financial Affairs Units (**Attachment No. 1:** Review of entities at central and local level not having established separate Financial Affairs Units);
- 45%<sup>3</sup> of central level entities and 57%<sup>4</sup> of local government units did not appoint Heads of Financial Affairs Units (**Attachment No. 2:** Review of entities at central and local level not having appointed Heads of Financial Affairs Units);

<sup>1</sup> 10 entities at central level

<sup>2</sup> 41 local self government units

<sup>3</sup> 34 entities at central level

<sup>4</sup> 46 local government units

- 13 entities (17%) at central level and 23 municipalities (28%) did not appoint Irregularities Officers pursuant to Article 50 of the Law on Public Internal Financial Control (**Attachment no. 3: Review of entities at central and local level not having appointed Irregularities Officers**) and
- 10 entities (13%) at central level and 20 municipalities (25%) did not appoint authorized accountants pursuant to requirements in the Law on Accounting on Budgets and Budget Users (**Attachment No. 4: Review of entities at central and local level not having appointed authorized accountant**).

## 2.7 Individual Reports

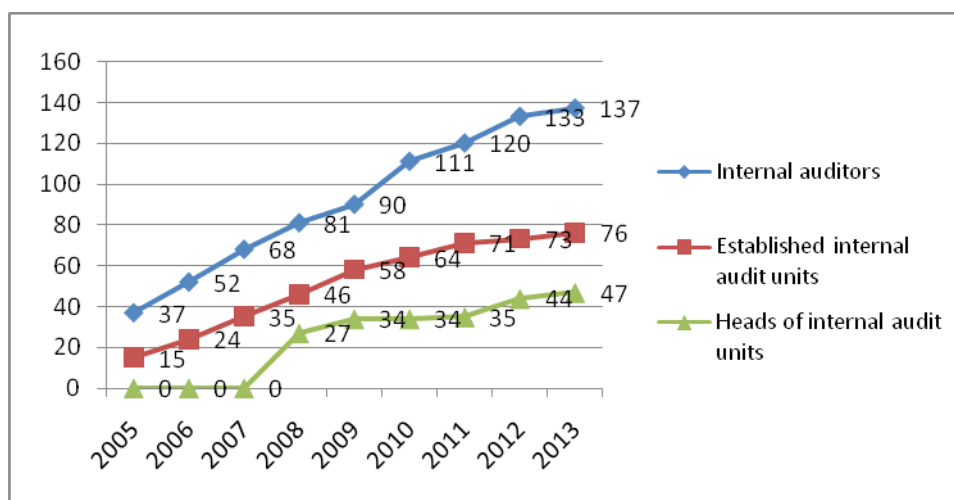
On the basis of the submitted 2013 Annual Reports on Financial Management and Control System Quality and Status, Ministry of Finance – Public Internal Financial Control Department, prepared individual reports for the entities at central and local level (**Attachment No. 5: Reports on financial management and control system quality and status at entities at central level and Attachment. No. 6: Reports on financial management and control system quality and status at entities at local level**).

## 3. 2013 REPORT ON AUDITS AND INTERNAL AUDIT ACTIVITIES

### 3.1 Internal Audit Report at Central Level

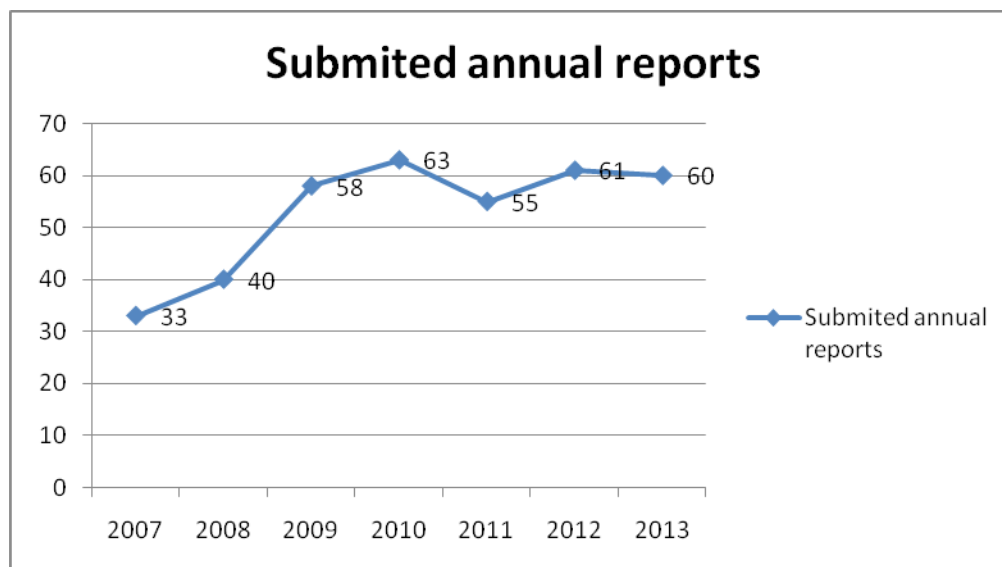
On the basis of the records of the Public Internal Financial Control Department (Central Harmonisation Unit) within the Ministry of Finance, as of 31<sup>st</sup> December 2013 inclusive, 76 internal audit units were established in 76 public sector entities at central level, employing 137 internal auditors, 47 out of which as Heads of Units. Twelve public sector entities had concluded contracts for internal audit to be performed by an internal audit unit of another entity. One out of these 12 public sector entities has its internal audit unit and had concluded a contract.<sup>5</sup>

As of December 2013 inclusive, number of established internal audit units, appointed internal auditors and Heads of Units by years is presented in the chart below:



<sup>5</sup> As of 10<sup>th</sup> July 2014, 77 internal audit units were established in 77 public sector entities at central level, 139 internal auditors were employed and 12 public sector entities had concluded contracts for internal audit to be performed by an internal audit unit of another entity.

2013 Report on Audits and Internal Audit was submitted by 60 public sector entities. Number of submitted reports by years is shown in the following chart:

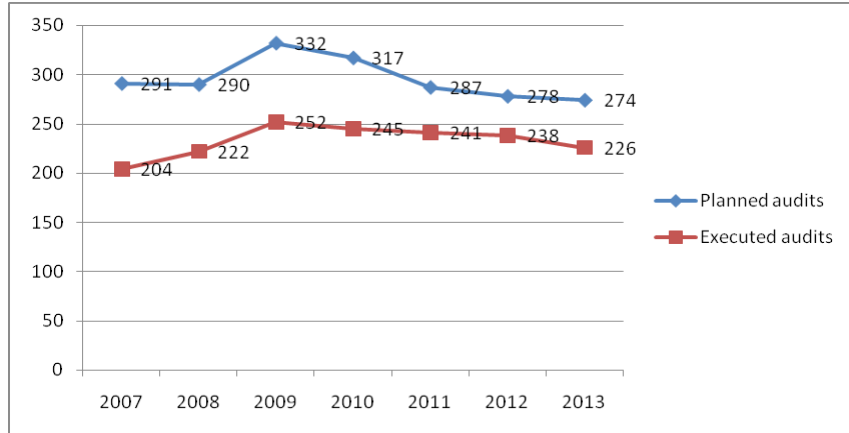


19 public sector entities did not submit Report on Audits and Internal Audit Activities. Three, out of these 19 entities, established Internal Audit Units and employed internal auditors, 10 entities established Internal Audit Units, but employed no auditors, and 6 entities did not establish Internal Audit Unit nor concluded contract for the internal audit to be performed by an internal audit unit of another public sector entity (**Attachment No. 7: Review of entities at central level not having submitted Report on Audits and Internal Audit Activities**).

In line with the 2013 Annual Plans, 244 audits were envisaged to be carried out in the public sector entities at central level. Upon request by the Heads of the entities, additional 30 (ad hoc) audits were planned, hence total number of planned audits was 274.

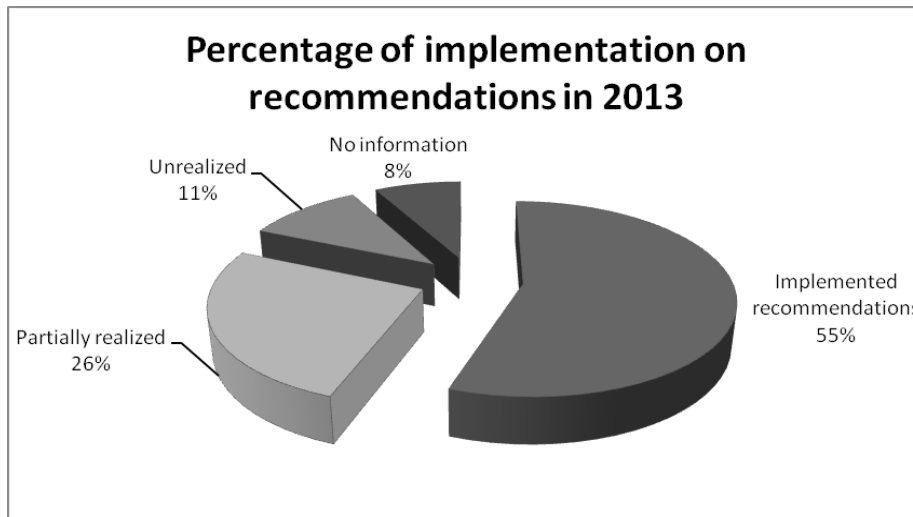
In 2013, 226 audits were carried out at central level and final audit reports were prepared for 42 entities. With respect to 18 entities which submitted annual financial report, but no audit was carried out, audits were planned at 8 entities out of them, while no audits were planned at 10 entities (**Attachment No.8: Review of entities at central level which submitted Report on Audits and Internal Audit Activities, but were not audited**).

Observed by years, planned and carried out audits are presented below:

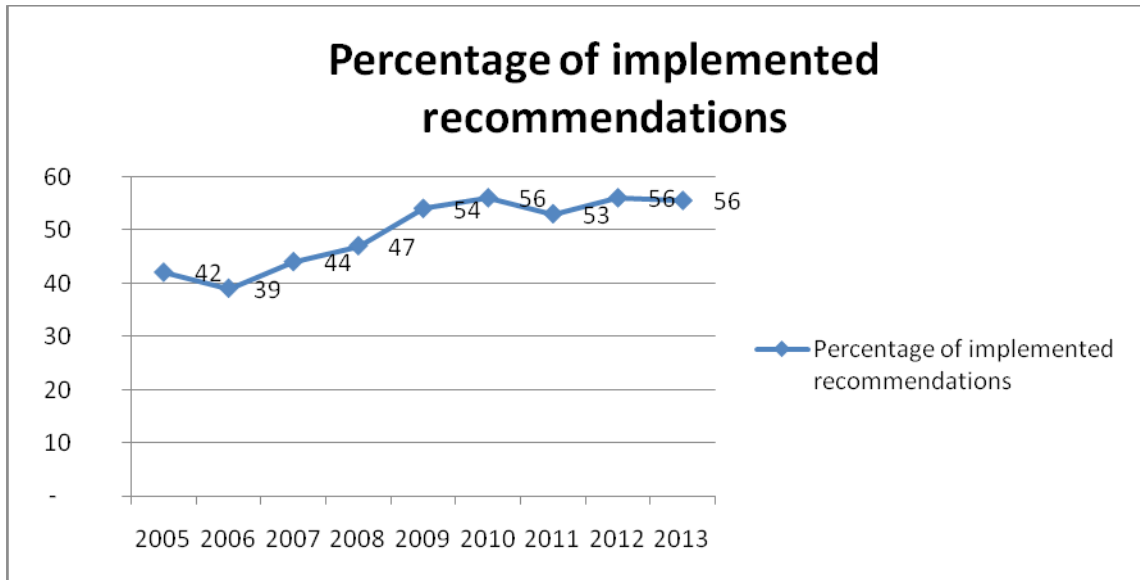


In 2013, carried out audits resulted in 964 findings. 1,031 recommendations were given therefore, 572 recommendations (55.5%) out of which were implemented, 268 recommendations (26%) were partially implemented, implementation of 110 (10.6%) recommendations did not commence, and no information was provided for the implementation of 81 recommendations (7.9%).

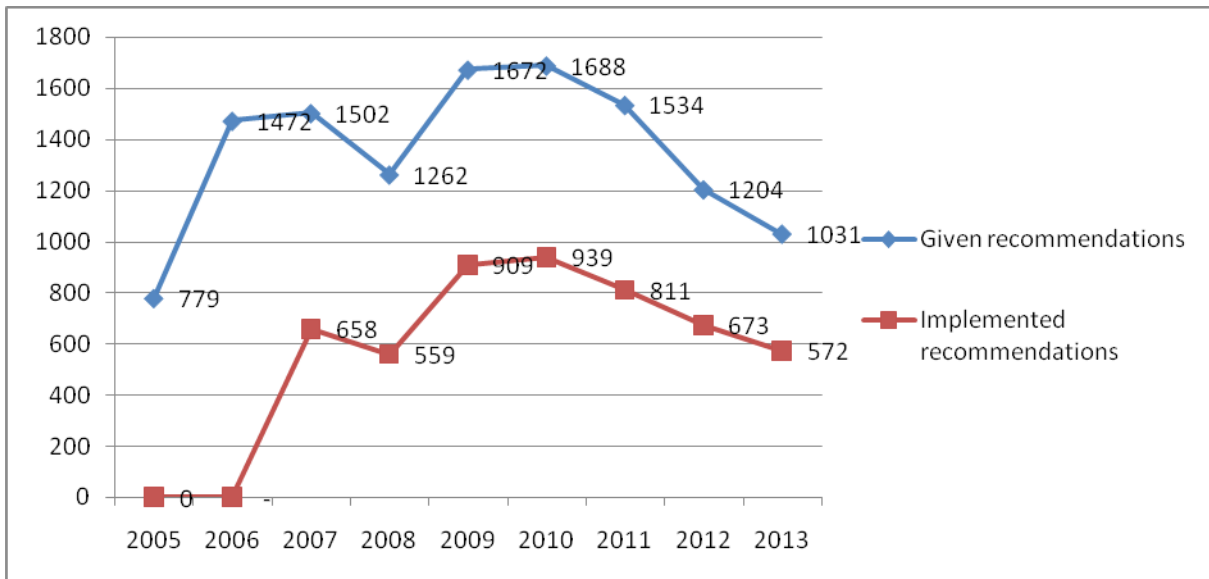
Percentage of implemented recommendations in 2013 is shown in the chart below:



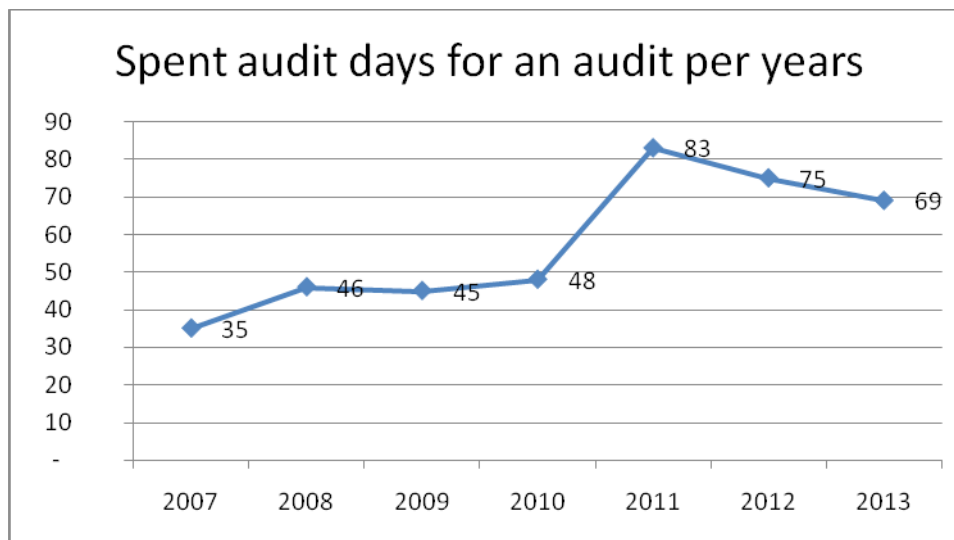
Percentage of recommendations implemented by year is shown in the following chart:



Recommendations given and implemented by year are shown in the chart below:



In 2013, Internal Audit Units at central level conducted 226 audits, final audit reports were prepared therefore, and 15,544 audit days were spent, or 69 audit days in average to perform an audit.



Data in the chart show that the number of audit days spent for an audit in 2013 was lower compared to the number of days spent for an audit in 2012, however, it is still higher than the previous years.

93% out of the total spent audit days was spent on carrying out the planned audits, and 7% of the audit days were spent for carrying out additional (ad hoc) audits.

Positive indicators in 2013, compared to 2012, are the following:

- number of established Internal Audit Units increased by 4% (from 73 to 76);
- number of internal auditors increased by 3% (from 133 to 137);
- number of Heads of Internal Audit Units increased by 7% (from 44 to 47);
- percentage of recommendations not being implemented dropped by 7.4 percentage points (from 18% to 10.6%);
- percentage of partially implemented recommendations increased by 8 percentage points (from 18% to 26%)
- number of audit days required to perform an audit dropped by 8% (from 75 of 69 audit days);
- number of ad-hoc audits decreased by 19% (from 37 to 30)
- number of detected findings dropped by 20% (from 1204 to 964) and accordingly number of given recommendations dropped by 14% (from 1204 to 1031).

Negative indicators in 2013, compared to 2012, are the following:

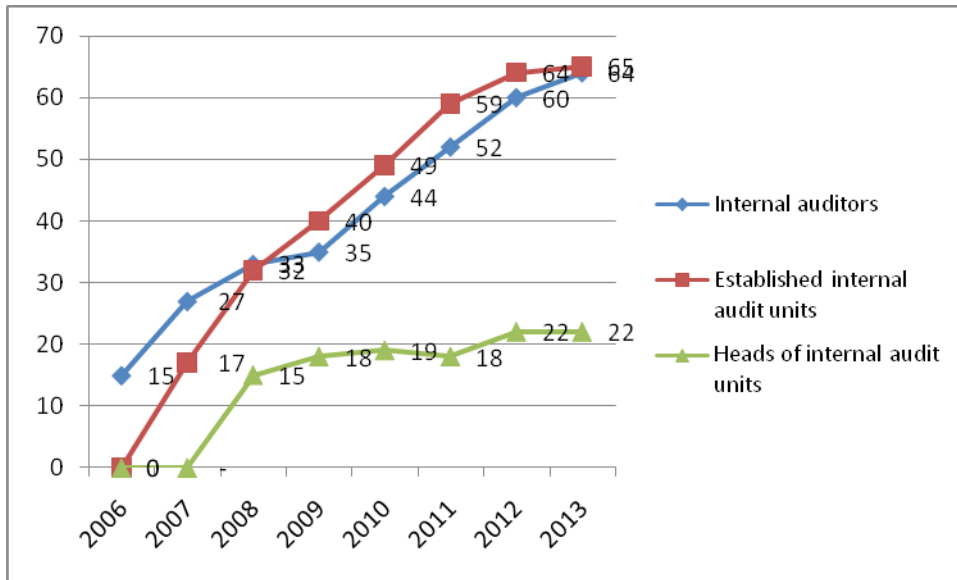
- number of reports submitted by public sector entities at central level decreased by 3% (from 62 to 60);
- number of carried out audits declined by 5% (from 238 to 226);
- percentage of plans performance dropped by 2.5 percentage points.

Percent of implementation of recommendations in 2013 is almost at the same level as in 2012 (56% in 2012 and 55.5% in 2013), and percent of recommendations for which there is no information about their implementation is at the same level as in 2012 (8%).

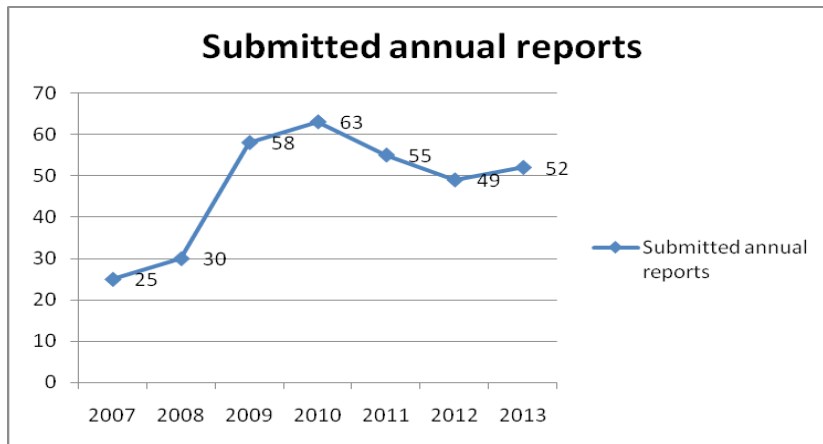
### 3.2. Internal Audit Report at Local Level

As of 31<sup>st</sup> December 2013 inclusive, 65 Internal Audit Units were established at local level and 64 internal auditors were employed, 22 out of which as Heads of Internal Audit Units. Twenty-four municipalities had concluded contracts for internal audit to be performed by internal audit unit of another municipality<sup>6</sup>.

The chart below shows number of established internal audit units, internal auditors and appointed Heads of Unit by years as of 31<sup>st</sup> December 2013 inclusive:



52 municipalities submitted 2013 Report on Audits and Internal Audit Activities. Number of reports submitted by years is shown in the chart below:



29 municipalities did not submit Report on Audits and Internal Audit Activities. 16 out of these municipalities established Internal Audit Units and employed internal auditors, two municipalities

<sup>6</sup> As of 7<sup>th</sup> August 2013, 67 internal audit units were established, 63 internal auditors were employed, 19 out of which as Heads. Twenty four municipalities concluded contracts for internal audit to be performed by internal audit unit of another municipality.



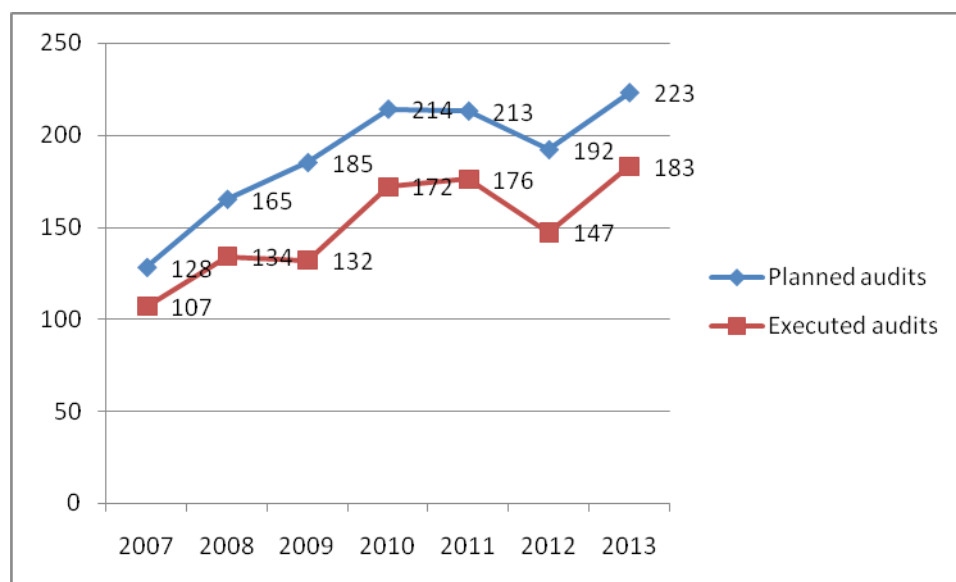
established Internal Audit Units and employed auditors, 6 municipalities had concluded contracts for internal audit to be performed by internal audit unit of another municipality, and 5 municipalities neither established Internal Audit Units nor employed internal auditors (**Attachment No.9**: Review of entities at local level not having Report on Audits and Internal Audit Activities).

According to 2013 Annual Plans, 172 audits were planned to be performed. Upon request by the Mayors, additional 51 (ad hoc) audits were planned, hence the total number of planned audits was 223.

In 2013, 183 internal audits were conducted at local level, and final audit reports for 39 municipalities were prepared. With respect to 13 municipalities which submitted annual financial report, but no audit was carried out, audit was initially planned at 1 municipality out of them, while no audits were planned at 12 municipalities (**Attachment No.10**: Review of entities at local level which submitted Report on Audits and Internal Audit Activities, but were not audited).

Observed by years, planned and carried out audits are presented below

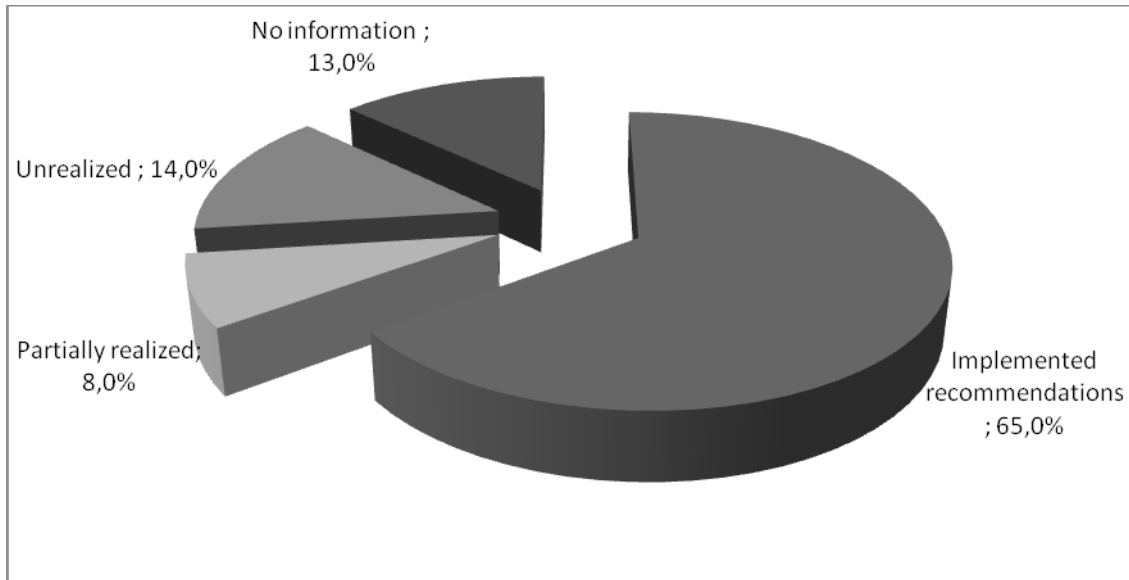
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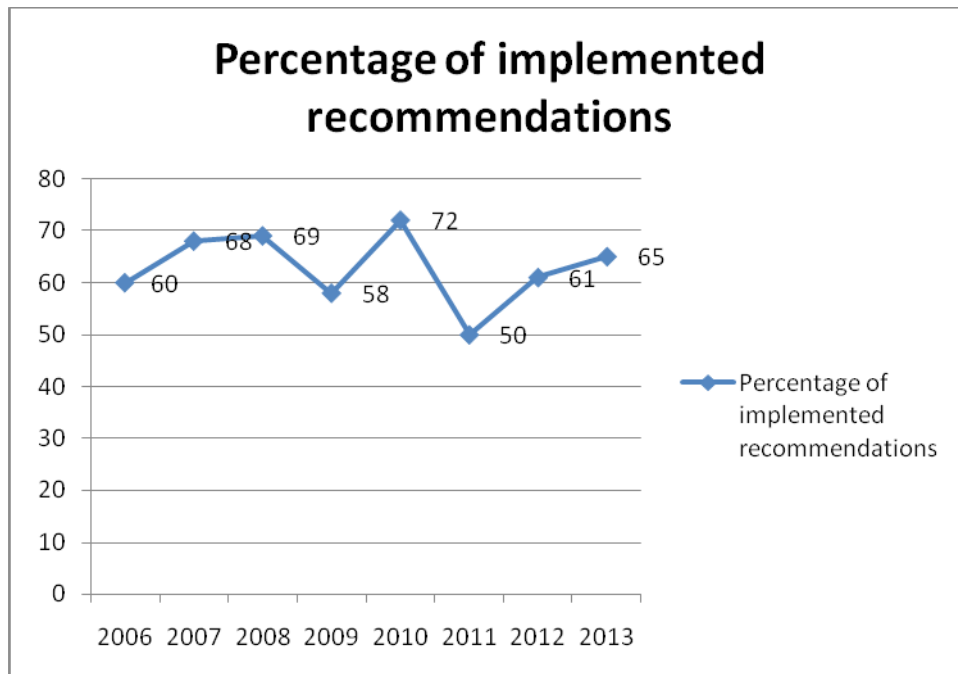
Internal audit, for conducted audits of local level ascertained total 1.391 finding. For the established findings of the audits have been given 1.382 recommendations, of which 902 are implemented (65%), 104 were partially implemented (8%), 193 have not been implemented (14%), and for 183 there is no information about their implementation (13%).

Total of 1,391 findings were detected in the course of the audits carried out at local level. 1,382 recommendations were given therefore, 902 recommendations (65%) out of which were implemented, 104 recommendations (8%) were partially implemented, implementation of 193 recommendations (14%) did not commence and no information was provided for the implementation of 183 recommendations (13%).

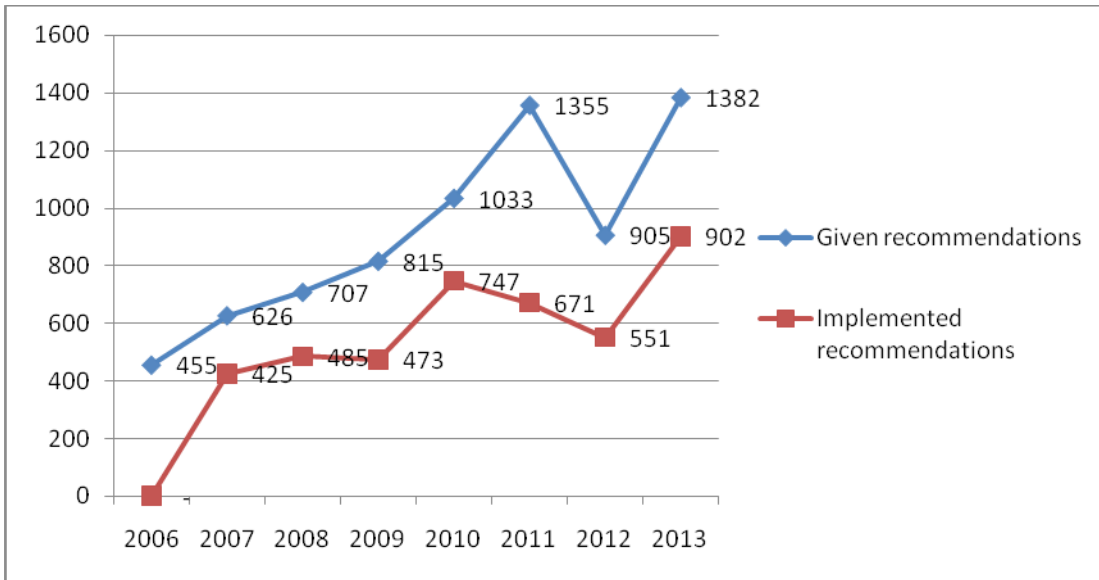
Percentage of implemented recommendations in 2013 is shown in the chart below:



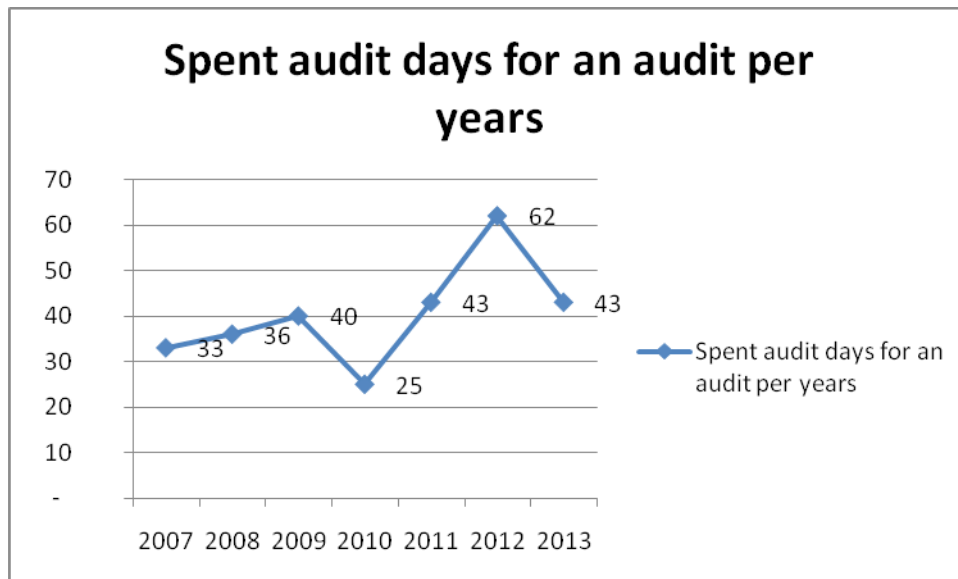
Percentage of recommendations implemented by year is shown in the following chart:



Recommendations given and implemented by year are shown in the chart below:



Internal auditors spent total of 7,860 audit days for the 183 audits carried out in 2013, or 43 audit days in average to perform an audit.



Data in the chart show that the number of audit days spent for an audit in 2013 was significantly lower.

87% out of the total spent audit days was spent on carrying out the planned audits, and 13% of the audit days were spent for carrying out additional (ad hoc) audits.

Positive indicators in 2013, compared to 2012, are the following:

- number of Internal Audit Units increased by 1.5% (from 64 to 65 units);
- number of internal auditors increased by 6.7% (from 60 to 64 auditors);
- number of municipalities having submitted 2013 Report on Audits increased by 6% (from 49 to 52);
- number of carried out audits surged by 24% (from 147 to 183).
- number of implemented recommendations increased by 4% (from 61% to 65%);
- number of partially implemented recommendations increased by 3% (from 5% to 8%);
- number of recommendations for which no data on their implementation is provided dropped by 15% (from 28% to 13%) and
- number of audit days spent to perform an audit dropped from 69 days in 2012 to 43 days in 2013.

Negative trend observed is as follows:

- number of recommendations not being implemented increased by 7% (from 7% to 14%) and
- number of ad hoc audits increased from 22 to 51 audits.

### **3.3 Individual Reports**

On the basis of the submitted Annual Reports on Audits and Internal Audit Activities, Ministry of Finance - Public Internal Financial Control Department prepared individual reports for public sector entities at central and local level (**Attachment No.11**: Individual 2013 Annual Reports on Audits and Internal Audit Activities at Central Level and **Attachment No.12**: Individual 2013 Annual Reports on Audits and Internal Audit Activities at local level).