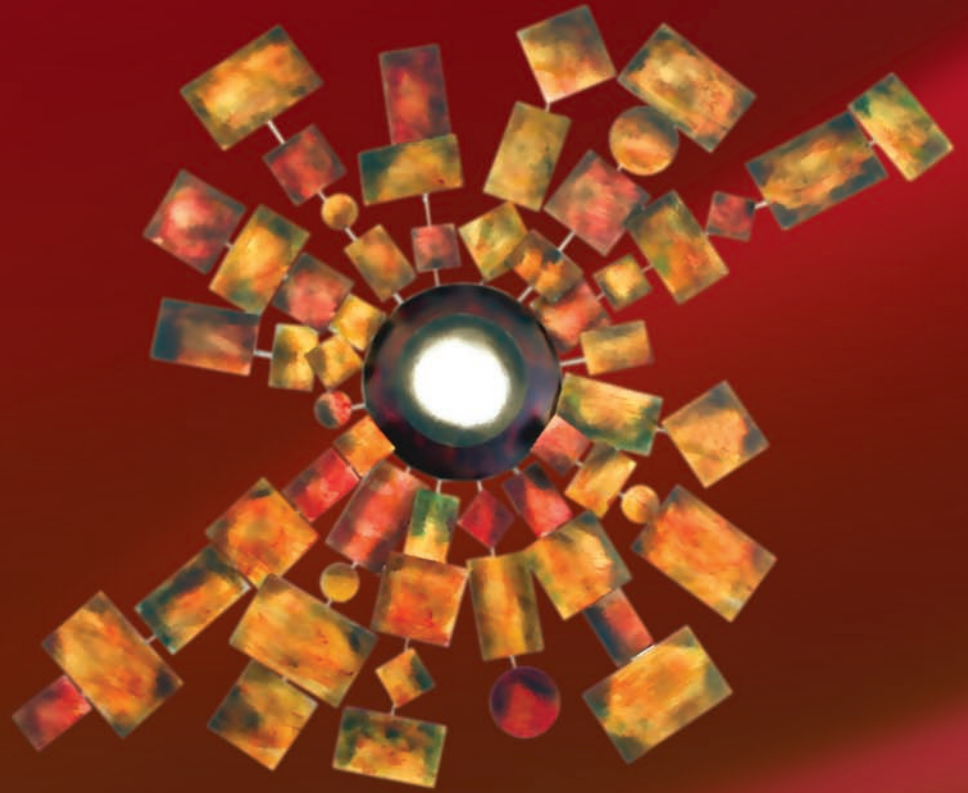




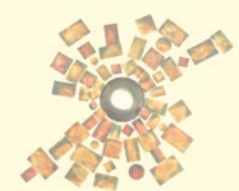
STATE AUDIT OFFICE



ANNUAL REPORT 2009

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Respected readers,

I hereby present the Annual Report of the State Audit Office for 2009, which illustrates the results of our work and the identified state of affairs of the auditees that were subjected to audit during 2009.

Last year the State Audit Office stepped into the second decade of its functioning as an autonomous and independent institution in the Republic of Macedonia, responsible for its work to the Assembly of the Republic of Macedonia.

Managing the State Audit Office is a great challenge, given its significant role in building a solid financial control system in the public sector of the Republic of Macedonia. In this respect, the State Audit Office significantly contributes to professional and efficient management of the taxpayers' money, and strengthening the financial discipline and accountability in the public sector.

In 2009 we devoted special attention to realization of the strategic goals, with emphasis on upgrading the quality of audits, strengthening audit skills, and introducing new types of audit as well as improving the information process.

With respect to follow-up of implementation of the recommendations in the audit reports, we intensified our cooperation with the Assembly of the Republic of Macedonia and other competent institutions in the Republic of Macedonia.

Regulating the status of the State Audit Office in the Constitution remains our priority for the next period. There is a strong need of introducing an amendment into the Constitution to define the role and the function of the State Audit Office, and to strengthen its independence. It is also a precondition for initiating negotiations with EU on the chapter of financial control.



Although chronologically it belongs to the current year, we have to mention the adoption of the new Law on State Audit in May 2010, for the purpose of harmonizing with the European practice.

The concept of the Annual Report enables understanding of the operation of entities subjected to audit through comprehensive analysis of the identified state of affairs, recommendations and the audit opinions included in the final audit reports. We also inform about the progress of the State Audit Office, the education and the methodological aspects as well as the cooperation with competent organs, transparency and the international cooperation.

All these activities have been completed by the enthusiastic engagement and commitment of all the employees of the State Audit Office for which I extend my sincere gratitude.

General State Auditor

A handwritten signature in black ink, appearing to be 'S. Stojanovska', written in a cursive style.

Mission

The State Audit Office is a supreme audit institution in the Republic of Macedonia the goal of which is to inform the Assembly, the Government and the other holders of public functions, and the public on the findings of the performed audits in a timely and objective manner.

The State Audit Office provides support to the Assembly of the Republic of Macedonia in pursuing its competences, by identifying and presenting irregularities, cases of illegal operation, and possible cases of corruption and abuse of office.

By the clear and effective recommendations, the State Audit Office supports the state institutions and beneficiaries of state funds in improving their financial management. In this way, the State Audit Office contributes to improving the quality of living of the citizens of the Republic of Macedonia.

Vision

In order to be successful in achieving our goal – watching over the public finance and promoting their management – our vision is to ensure permanent quality of operation and retain the epithet of independent and professional partner of high integrity, and at the same time, a holder of the progress of the state funds management, accountability and transparency of operation.

BACKGROUND OF THE STATE AUDIT IN THE REPUBLIC OF MACEDONIA

The beginnings of the state audit date from the time Macedonia was one of the six constitutive republics of the Yugoslav federation. The first state audit institutions were established in 1945.

During the period between 1945 and 1991 the state audit functioned as an organizational unit of the National Bank of the Federal People's Republic of Yugoslavia, and later within the Payment System Office after it was separated from the National Bank.

Since 1991, when the Republic of Macedonia became an independent and sovereign state, until 1998 the Directory for Economic and Financial Audit of the Social Accounting Office (later renamed into Payment Operations Office) performed state audit.

The State Audit Office started its operation in 1999 with nine employees, all from the Directory for Economic and Financial Audit of the Payment Operations Office. In 2009 it celebrated the 10th Anniversary with 93 employees.



In this period the State Audit Office had been managed by prominent experts in this area: Antonio Veljanov (1998-1999), Metodija Tosevski (2000-2005) and Dr. Dragoljub Arsovski (2005-2007). At the celebration on the occasion of the 10th Anniversary, the General State Auditor granted the former general state auditors recognitions, as well as the auditors who were the first employees of the State Audit Office when it started its operation in 1999.

During 2007, an audit authority was established by amending the Law on State Audit. It is an independent body responsible for auditing the EU pre-accession IPA funds. By the Law on Audit of the Instrument for Pre-accession Assistance (IPA), adopted in May 2010, the audit authority was established as an independent legal entity.



MANAGEMENT OF THE STATE AUDIT OFFICE



Tanja Tanevska
General State Auditor



Blagoja Ilievski
Deputy General State Auditor



Jadranka Boskoska
Advisor to the General State Auditor



Cveta Ristovska
Advisor to the General State Auditor



Tanja Janevska
Advisor to the General State Auditor



Mito Naumoski
Assistant General State Auditor



Vladimir Mилоjevic
Assistant General State Auditor



Tanka Blazevska
Assistant General State Auditor



Liljana Stojanova
Assistant General State Auditor



Branislav Gulev
Assistant General State Auditor



Tanja Tasevska
Assistant General State Auditor



Maksim Acevski
Assistant General State Auditor

STATUS

The legal framework for operation of the State Audit Office and the grounds for performing state audit were laid in 1997 by adoption of the Law on State Audit.

For the purpose of harmonizing with the basic principles of the Lima Declaration and the guidelines on the audit principles, the Law has been amended several times lately.

The Law on State Audit defines the organization and the function of the State Audit Office; the manner and the conditions for performing state audit; the audit process; the auditees as well as the rights and responsibilities of authorized state auditors and state auditors at performing the audit.

The State Audit Office adopts Annual Operation Program based on determined criteria. This Program determines the scope of operation of the state audit, i.e. the number of entities to audit, the audit teams and the timelines.

According to the Law on State Audit the State Audit Office prepares the Annual Report on Operation and Performed Audits, and submits the Report to the Assembly of the Republic of Macedonia within the deadline regulated by law.

For the purpose of enhancing the operational and the financial independence of the State Audit Office, and achieving higher effectiveness and efficiency in performing state audit, the new Law on State Audit was adopted in May 2010. The new Law provided harmonization of the operation of this supreme audit institution with the standards and the criteria of the European Union in this area.

STRUCTURE AND ORGANIZATION

Based on the nature, the scope, the complexity level and the other conditions necessary for efficient fulfillment of audit operations and tasks in the State Audit Office there are 7 /seven/ sectors, of which 5 /five/ financial audit sectors, 1 /one/ performance audit sector and 1 /one/ sector for development, strategic planning and international cooperation. Воедно, за независно извршување на работите поврзани со внатрешната ревизија, информатичката технологија и ревизија, правните работи и човечки ресурси и финансиските и сметководствени работи се формирани 4 (четири) самостојни одделенија.

In order to provide independent operations related to the internal audit, IT and IT audit, legal affairs and human resources, and finance and accounting, 4 /four/ independent departments were created as well.

GENERAL STATE AUDITOR

DEPUTY GENERAL STATE AUDITOR

CABINET OF GSA

ADVISORS TO THE GSA

DEPARTMENT FOR PERFORMANCE AUDIT

DEPARTMENT A – AUDIT OF THE BUDGET OF RM, ORGANS ESTABLISHED BY THE CONSTITUTION OF RM, MINISTRY OF FINANCE AND ITS AGENCIES, NATIONAL BANK OF RM, POLITICAL PARTIES FINANCED BY BUDGET FUNDS, OTHER BUDGET USERS, USERS OF EU FUNDS AND OTHER INTERNATIONAL INSTITUTIONS.

DEPARTMENT B – AUDIT OF STATE ORGANS, BUDGET BENEFICIARIES AND OTHER BUDGET FUNDS USERS (CENTRAL BUDGET OF RM)

DEPARTMENT C – AUDIT OF FUNDS AND FUND BENEFICIARIES (FUNDS BUDGET), COURT BUDGET AND USERS OF COURT BUDGET FUNDS

DEPARTMENT D – AUDIT OF PUBLIC ENTERPRISES, INSTITUTIONS ESTABLISHED BY LAW, JOINT STOCK COMPANIES IN WHICH THE STATE IS PREDOMINANT SHAREHOLDER AND OTHER INSTITUTIONS-USERS OF PUBLIC FUNDS

DEPARTMENT E – AUDIT OF STATE ORGANS RESPONSIBLE FOR MONITORING OF THE DEVELOPMENT OF LOCAL SELF-GOVERNMENT, BUDGETS OF LSU AND THEIR USERS

DEPARTMENT FOR DEVELOPMENT, STRATEGIC PLANNING AND INTERNATIONAL COOPERATION

UNIT FOR DEVELOPMENT, STRATEGIC PLANNING AND ADVANCED PROFESSIONAL EDUCATION

UNIT FOR PLANNING, ANALYSES AND REPORTS

UNIT FOR INTERNATIONAL COOPERATION AND COOPERATION WITH SAI

UNIT FOR INTERNAL AUDIT

UNIT FOR IT AND IT AUDIT

UNIT FOR LEGAL AND COMMON AFFAIRS AND HUMAN RESOURCES

UNIT FOR FINANCE AND ACCOUNTING

EMPLOYEES

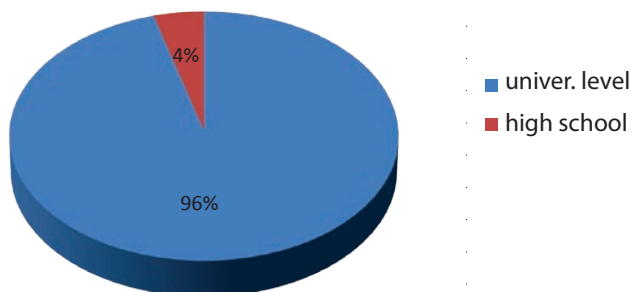
The State Audit Office is managed by the General State Auditor. The General State Auditor has a deputy. The General State Auditor and the Deputy General State Auditor are appointed by the Assembly of the Republic of Macedonia for a 10-year term.

In the past the number of employees was permanently increasing, thus strengthening the expert potential and the capabilities of the State Audit Office. The State Audit Office had 93 employees in 2009, 96% of which have university degree in economics, law and information technology. Eleven employees hold a certificate for authorized state auditor.

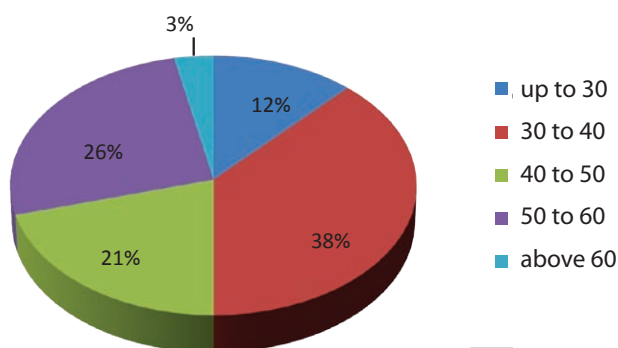
The exam for acquiring the title of an authorized state auditor is passed before a commission established by the General State Auditor, according to the Program adopted by the General State Auditor and approved by the Minister of Finance.

The procedure for conducting the exam for authorized state auditor started in 2009 and it was successfully completed in March 2010.

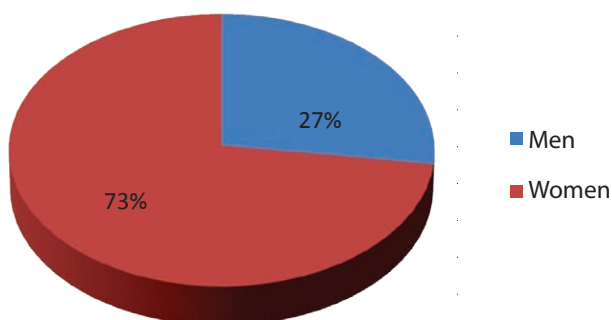
Structure by education level



Structure by age



Structure by gender



TRAINING OF STATE AUDITORS

Permanent professional development through training is a guarantee of the high standards of the auditors' work and the quality of the audits. The State Audit Office organizes permanent staff training to increase the efficiency of operation and to improve the professional knowledge of audit, IT and other audit –related areas. There are two main forms of training: basic training and permanent professional training of auditors.

The major trends for development of professional and expert capacities of state auditors are defined in the Strategy for Human Resources Management of the State Audit Office 2008 - 2012 and the Action Plan for Implementation of Planned Activities of the State Audit Office 2008 – 2012.

For the purpose of improving the expertise and the knowledge of the auditors in various audit areas the State Audit Office organized three workshops in 2009:

- Writing audit reports and providing quality of audits. More than 40 auditors attended the workshop organized and implemented by trainers of the State Audit Office and experts from the Netherlands Court of Audit.
- Basic CAAT's and IDEA software training. These workshops were organized and implemented by trainers of the State Audit Office and experts from the Netherlands Court of Audit (MATRA Project).
- Performance audit training attended by five auditors from the financial audit sectors. The head of the performance audit sector in the State Audit Office and experts from the Netherlands Court of Audit presented the performance audit experience.

During 2009 training in communication skills and team work was organized for all employees of the State Audit Office.

The State Audit Office pays strong attention to in-service training of auditors. Cooperation with the Netherlands Court of Audit continued in 2009 within the MATRA Program and two pilot financial audits were performed. These activities gave the opportunity to the auditors to exchange practical experience with their colleagues from the Netherlands Court of Audit on various aspects of the audit process.

Representatives of the State Audit Office attend regular basis workshops organized by national and foreign professional organizations and institutions. In 2009, 26 representatives of the State Audit Office took part in 12 workshops, seminars and working group meetings on various topics. The events were organized by EUROSAI, CIPFA¹, and EIPA², European Commission (DG Budget), and PSC³. We distinguish the following: Coordinated Climate



1 Chartered Institute of Public Finance and Accountancy
2 European Institute for Public Administration
3 Professional Standards Committee

Changes Parallel Audit (EUROSAI WGEA⁴); IT Working Group Meeting; INTOSAI/IDI Trans-regional Program for Public Debt Management Audit (TP PDMA⁵); PIFC Conference in Brussels; Increasing Awareness of ISSAI⁶ Standards in Warsaw; Performance Audit Development in Changing Circumstances in Prague; Workshop on IPSAS⁷ Standards in Ljubljana; Seminar on Successful Budgeting in Warsaw; Seminar on „Developing a COBIT standard-based IT program “ in Antwerp. The representatives of the State Audit Office had their presentations at a number of the events.

In 2009, within the bilateral cooperation between the State Audit Office of Macedonia and SAI of Bulgaria, 15 auditors of each audit institution took part in a seminar in Berovo, Republic of Macedonia. The auditors of both institutions exchanged their experience in various topics of the audit practice.

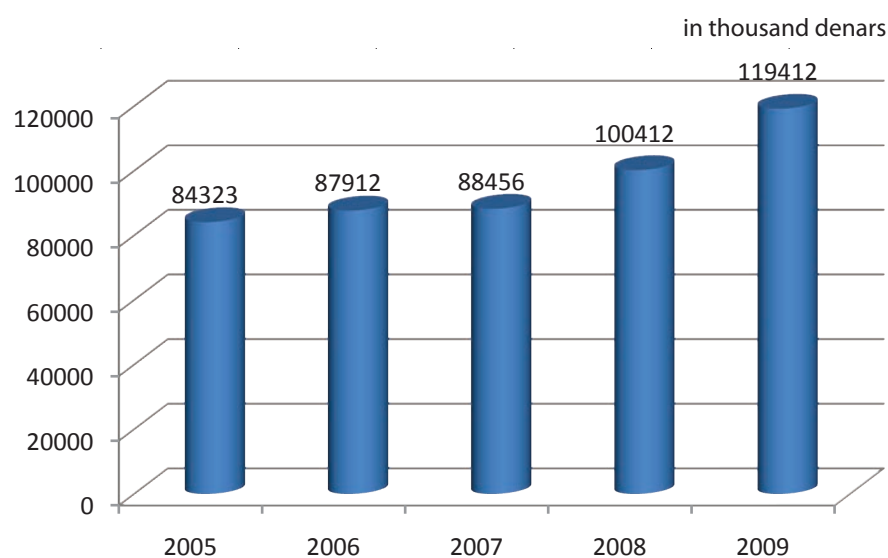
FINANCING

The State Audit Office is financed by the Central Budget and by own income from collection of state audit fees according to the tariff approved by the Assembly of the Republic of Macedonia.

The Law on State Audit, adopted in 2010, canceled the audit fee tariff; the Assembly of the Republic of Macedonia will determine the funds from the Central Budget upon proposal of the State Audit Office.

There has been an increasing trend of the Budget funds as a result of the development and the capacity building in the State Audit Office.

Reaized budget funds per year

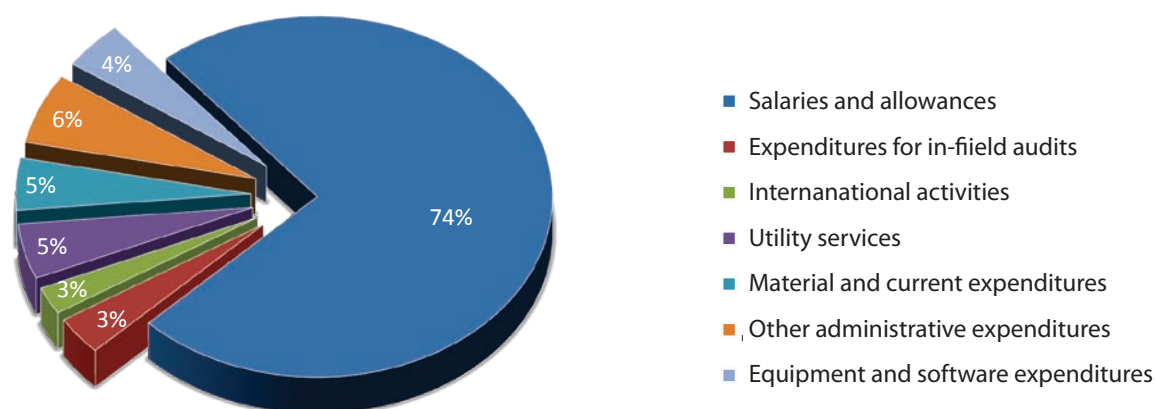


4 Working Group on Environmental Auditing
 5 Public Debt Management Audit
 6 International Standards for Supreme Audit Institutions
 7 International Public Sector Accounting Standards

The total budget for 2009 amounts to denar 119.412 thousand, 78.355 thousand or 66% of which received from the Central Budget and 41.057 thousand or 34% from own income.

The State Audit Office signed an agreement for donation in amount of denar 221 thousand, with the Netherlands Court of Audit in 2009. This is to finance activities of the MATRA Project for developing and strengthening the capacities of the State Audit Office in the period 2009 - 2010.

Expenditures in 2009



AUDIT STANDARDS AND METHODOLOGY

Unavoidable activity of an audit institution is development of methodology for performing audit as a support to the audit work in accordance with the changing environment, international trends and the best practice.

Standardization of professional requirements on international level and the need of compliance with the international standards add value to the professional regulatory activity of the SAI.

The State Audit Office permanently follows the new developments in the methodology and audit practice in the world through participation in workshops, seminars and other forms of presenting methodology documents and practice, organized by the committees and the working/regional groups of INTOSAI, and other professional bodies that develop and establish professional standards.

Based on the International Audit Standards (of INTOSAI⁸ /ISSAI⁹ , that is, IFAC¹⁰) accepted in the Republic of Macedonia, the experience of previous work of the State Audit Office and the experience of the cooperation with other SAIs, the Financial Audit Guidelines has been updated in the part of reporting. Update has been done in a form of “Manual on Reporting from Performed Audits” for financial audit. The Manual includes all relevant developments of the methodology practice in accordance with the latest international audit standards. The part about materiality of the Manual for Financial Audit has been upgraded as well, by a separate “Guidelines on Determining Materiality for Evaluation of Findings in Audit Reports”.

8 International Organization of Supreme Audit Institutions

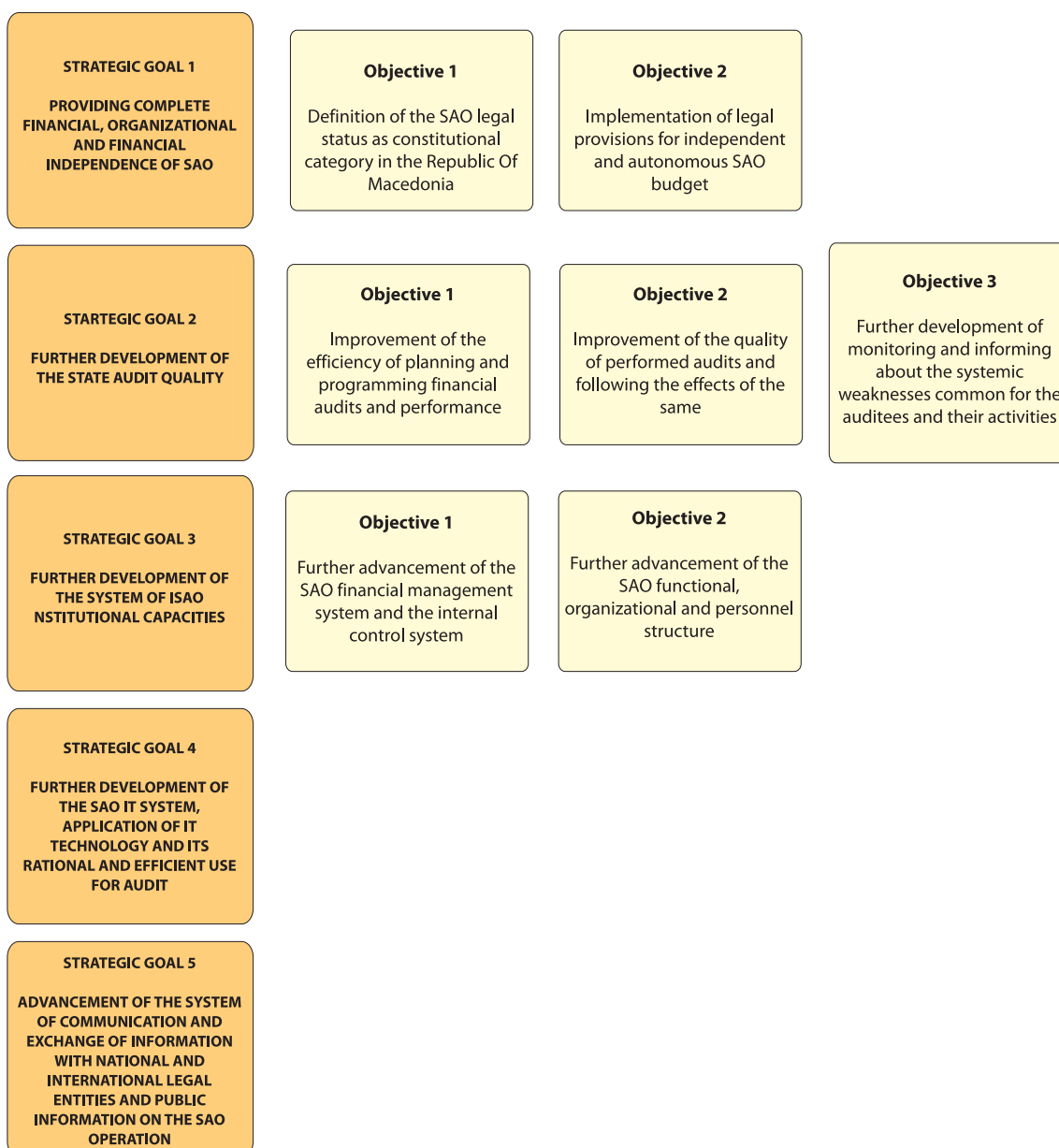
9 International Standards of Supreme Audit Institutions

10 International Federation of Accountants

SAO DEVELOPMENT STRATEGY

The State Audit Office development in the previous period inflicted defining new strategic goals. For this purpose, in 2009 the State Audit Office adopted the new Development Strategy for the period 2010 – 2014. The Strategy defines these five strategic goals: substantiating complete independence of the State Audit Office; permanent development of the state audit quality; permanent development of the system of institutional capacities management; permanent development of the IT system in the State Audit Office, and improvement of the communication system. The State Audit Office has developed Human Resources Management Strategy, and Communication and IT Strategy, as a part of the Development Strategy.

STRATEGIC GOALS OF THE STATE AUDIT OFFICE



INFORMATION TECHNOLOGY AND AUDIT

Development and application of information technology, and its rational and efficient use for audit is a strategic goal of the State Audit Office. In this respect, the State Audit Office performed the following activities in 2009:

- Implementation of a centralized system for storage and exchange of data;
- Implementation of an integrated financial information system;
- Providing internet access for auditors at field work;
- Use of computer-assisted audit techniques (CAAT's), such as IDEA software, for data analysis and sampling .

IT systems have been evaluated at a number of auditees, which revealed absence of security systems for protection and integrity of data. This situation creates opportunities to modify the data without a recording of the original contents, which devalues the credibility and the relevance of the data.

After the audit institution indicated the necessity of introducing and developing security policies and procedures, the Government of the Republic of Macedonia tasked the Ministry of Information Technology with developing IT systems development strategy, comprehensive security policies, and policies for access to/ data back up. The Ministry of Information Technology has prepared Information on Defining Security Measures and Recommendations for Protection and Development of IT Systems that state institutions should utilize.



AUDIT ACTIVITIES IN 2009 THROUGH FIGURES

| | |
|---------|--|
| 157 | AUDIT REPORTS ON FINANCIAL STATEMENTS OF 2008 |
| 10 | AUDIT REPORTS ON THEMATIC FINANCIAL AUDITS |
| 1 | AUDIT REPORTS ON FOLLOW - UP AUDITS |
| 55 | PERFORMED FOLLOW - UP REVIEWS |
| 3 | AUDIT REPORTS ON AUDIT |
| 190 | AUDITEES COVERED BY AUDIT |
| 1.048 | FINDINGS IN AUDIT REPORTS |
| 996 | RECOMMENDATIONS INCLUDED IN AUDIT REPORTS |
| 630 | IMPLEMENTED RECOMMENDATIONS |
| 178.172 | MILLION DENARS OF AUDITED PUBLIC REVENUES |
| 121.509 | MILLION DENARS OF AUDITED PUBLIC EXPENDITURES |
| 64 | AUDIT REPORTS SUBMITTED TO THE ASSEMBLY OF RM |
| 12 | AUDIT REPORTS SUBMITTED TO THE PUBLIC PROSECUTION OFFICE OF RM |
| 15 | AUDIT REPORTS SUBMITTED TO THE STATE COMMISSION FOR PREVENTION OF CORRUPTION |

PERFORMED AUDITS AND ISSUED REPORTS

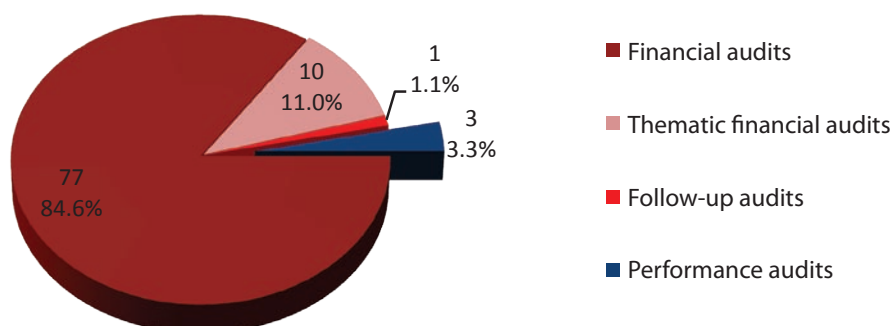
In 2009, 91 audits were performed (2008 – 84 audits) 77 of which were financial audits (51 obligatory audits and 26 audits of other entities according to the AP), 10 thematic financial audits, 1 follow-up audit and 3 performance audits. 55 follow-up reviews were performed upon recommendations included in the audit reports of 37 audits of 2009.

Total number of 171 audit reports were issued upon completed audits, 157 of which were financial audits, 10 thematic financial audits, 1 follow-up audit and 3 performance audits.

The table below presents information on the number of performed audits with structure of data for two years:

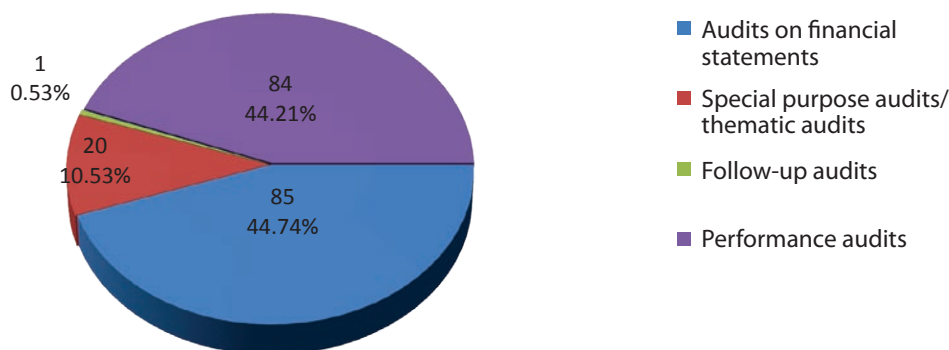
| Review of performed audits and structure | 2009 | | 2008 | |
|--|-------------------------|-----------|-------------------------|-----------|
| | No. of performed audits | Structure | No. of performed audits | Structure |
| 1 | 2 | 3 | 4 | 5 |
| Financial audits | 77 | 84,6% | 66 | 78,6% |
| Thematic financial audits | 10 | 11,0% | 9 | 10,7% |
| Follow-up audits | 1 | 1,1% | 6 | 7,1% |
| Total financial audits | 88 | 96,7% | 81 | 96,4% |
| Performance audits | 3 | 3,3% | 3 | 3,6% |
| Total audits | 91 | 100,0% | 84 | 100,0% |

Review of performed audits and structure for 2009



Total of 190 entities were covered by various forms of audit of accounting records, documents, analyses as well as economy of administrative activities, efficiency in use of resources and effectiveness of operation versus the achieved goals .

Entities covered by audit by types of audits 2009

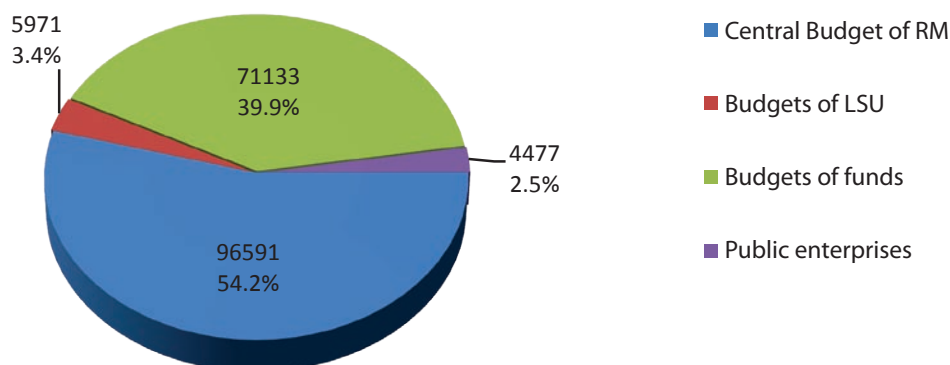


In the total of the audited public income in 2009, Central Budget income participates with 54,2%, income of the local self-government units with 3,4%, funds at the level of the Republic 39,9%, and public enterprises with 2,5%.

(in million denars)

| Audited public revenues | 2009 | | 2008 | |
|--|----------|-----------|----------|-----------|
| | Revenues | Structure | Revenues | Structure |
| 1 | 2 | 3 | 4 | 5 |
| Central Budget of RM | 96.591 | 54,2% | 99.099 | 74,2% |
| Budgets of local self-government units | 5.971 | 3,4% | 4.526 | 3,4% |
| Budgets of funds | 71.133 | 39,9% | 26.791 | 20,1% |
| Public enterprises | 4.477 | 2,5% | 3.073 | 2,3% |
| Total | 178.172 | 100,00% | 133.489 | 100,00% |

Audited public income for 2009 (in million denars)

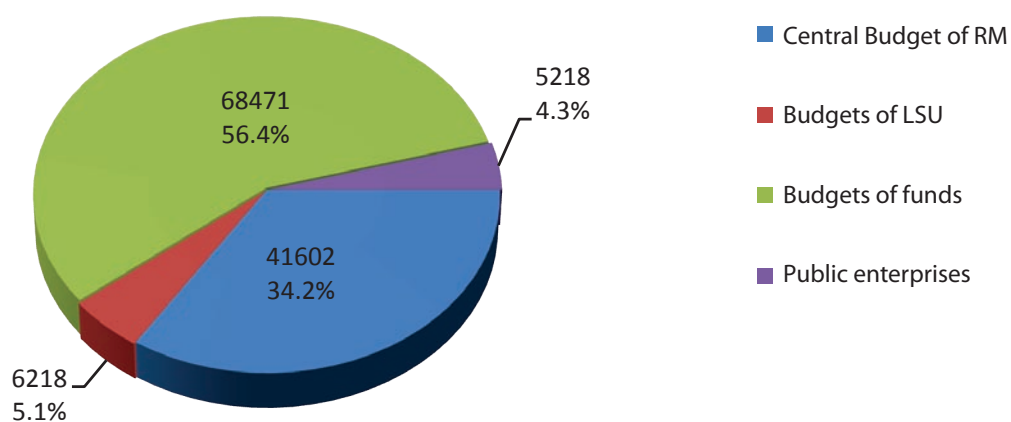


In the total of the audited public expenditures in 2009, Central Budget users expenditures participate with 54,2%, local self-government units with 5,1%, funds at the level of the Republic 56,4%, and public enterprises with 4,3%.

(in million denars)

| Audited expenditures | 2009 | | 2008 | |
|--|--------------|-----------|--------------|-----------|
| | Expenditures | Structure | Expenditures | Structure |
| 1 | 2 | 3 | 4 | 5 |
| Central Budget of RM | 41.602 | 34,2% | 36.597 | 42,6% |
| Budgets of local self-government units | 6.218 | 5,1% | 4.236 | 4,9% |
| Budgets of funds | 68.471 | 56,4% | 41.607 | 48,5% |
| Public enterprises | 5.218 | 4,3% | 3.388 | 4,0% |
| Total | 121.509 | 100,00% | 85.828 | 100,00% |

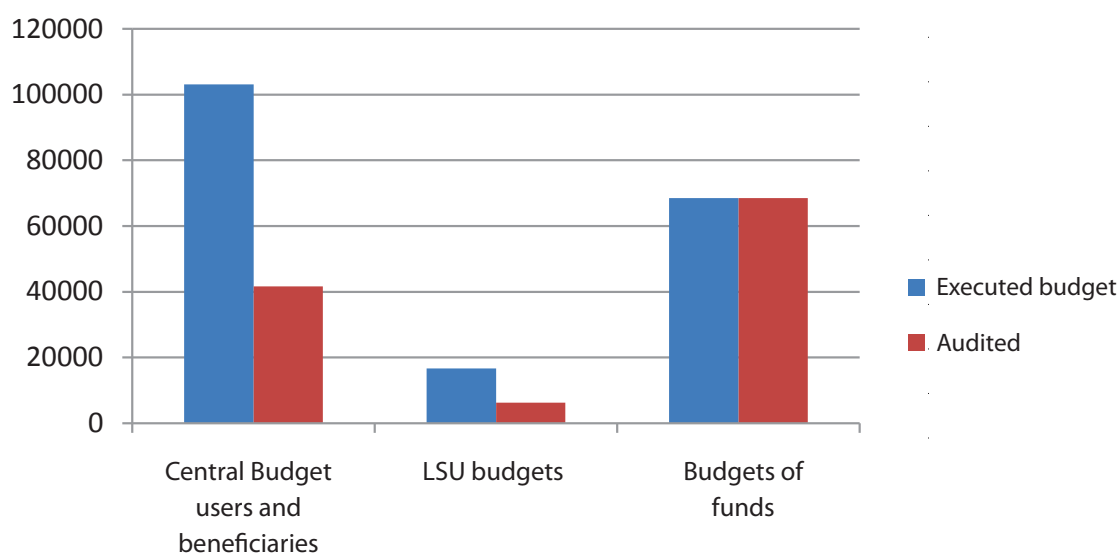
Audited public expenditures for 2009 (in million denars)



Audited expenditures per types of budgets in relation to total budgets of users and beneficiaries of the Central Budget, budgets of LSU and budgets of funds in 2009

(in million denars)

| Central Budget users and beneficiaries budgets of LSU and budgets of funds | 2009 | | | 2008 | | |
|--|-----------------|---------|---------|-----------------|---------|--------|
| | Executed budget | Audited | Share | Executed budget | Audited | Share |
| 1 | 2 | 3 | 4 (3/2) | 5 | 6 | 7(6/5) |
| Central Budget users and beneficiaries | 103,147 | 41,602 | 40.33% | 103,092 | 36,597 | 35.50% |
| Budgets of local self-government units | 16,650 | 6,218 | 37.35% | 9,842 | 4,236 | 43.04% |
| Budgets of funds | 68,471 | 68,471 | 100.00% | 58,329 | 41,607 | 71.33% |
| Total | 188,268 | 116,290 | 61.77% | 171,263 | 82,440 | 48.14% |



AUDIT OPINIONS

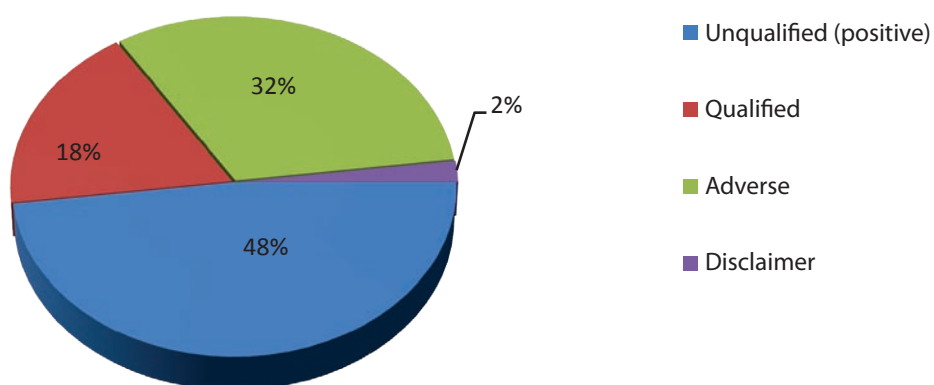
Primary objective of the audit of financial statements is to allow the auditor to express an opinion as to whether:

- Financial reports accurately and objectively present the financial situation and the result of the financial activities, and
- Intended and legal use of funds has been accomplished

In accordance with the goals defined in the audit reports, auditors express opinions on both the financial statements, and compliance with the legislation/intended and legal use of funds.

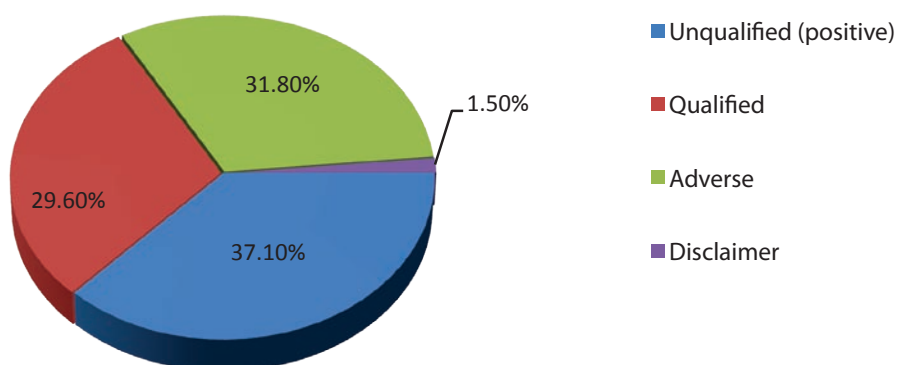
On the accuracy and objectivity of financial statements for 2008 there were 48,0% unqualified opinions; 18,0% qualified opinions; 32,0% adverse opinions, and 2,0% disclaimers.

Correctness and objectivity of financial statements



There were 37,1% unqualified opinions on the compliance with the legislation as well as 29,6% qualified opinions; 31,8% adverse opinions, and 1,5% disclaimers.

Intended and legal use of funds



Beside the audit opinions on the set of financial statements, there were diverse opinions about the income statement/balance sheet in six audit reports.

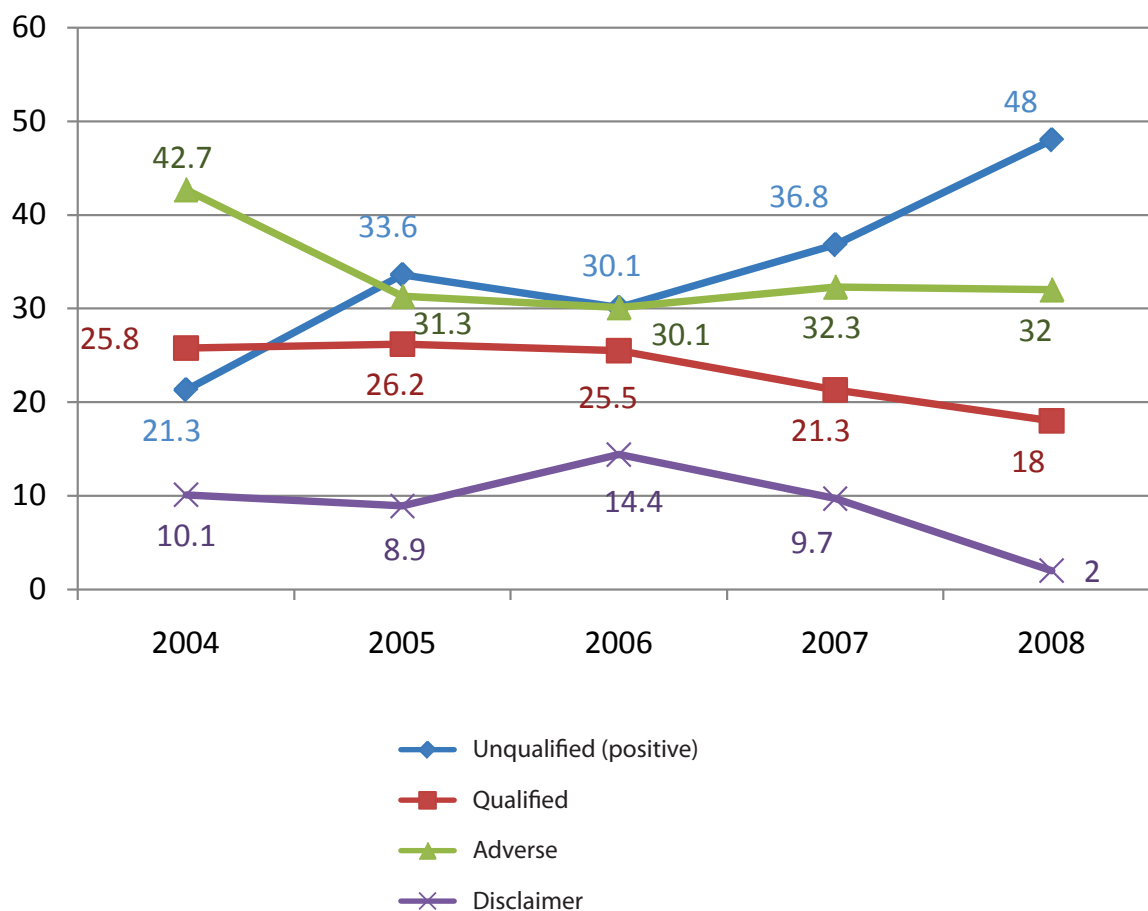
Ten thematic financial audits for special purposes were performed in 2009 (for one/more financial statement components or certain aspects concerning several auditees/areas). The following segments were audited: fixed assets and inventory; leases; subsidies and transfers; capital expenditures; public procurement; public debt management; receivables from unpaid privatization fees; collection of fees for arrangement of construction land, and intended use of funds.

Upon specifically defined objectives for each of these audits, 16 opinions were expressed as follows: 6 unqualified opinions; 5 qualified opinions; 4 adverse opinions; 1 disclaimer and 2 audit conclusions.

The following is the structure of expressed opinions per years (for 5 years):

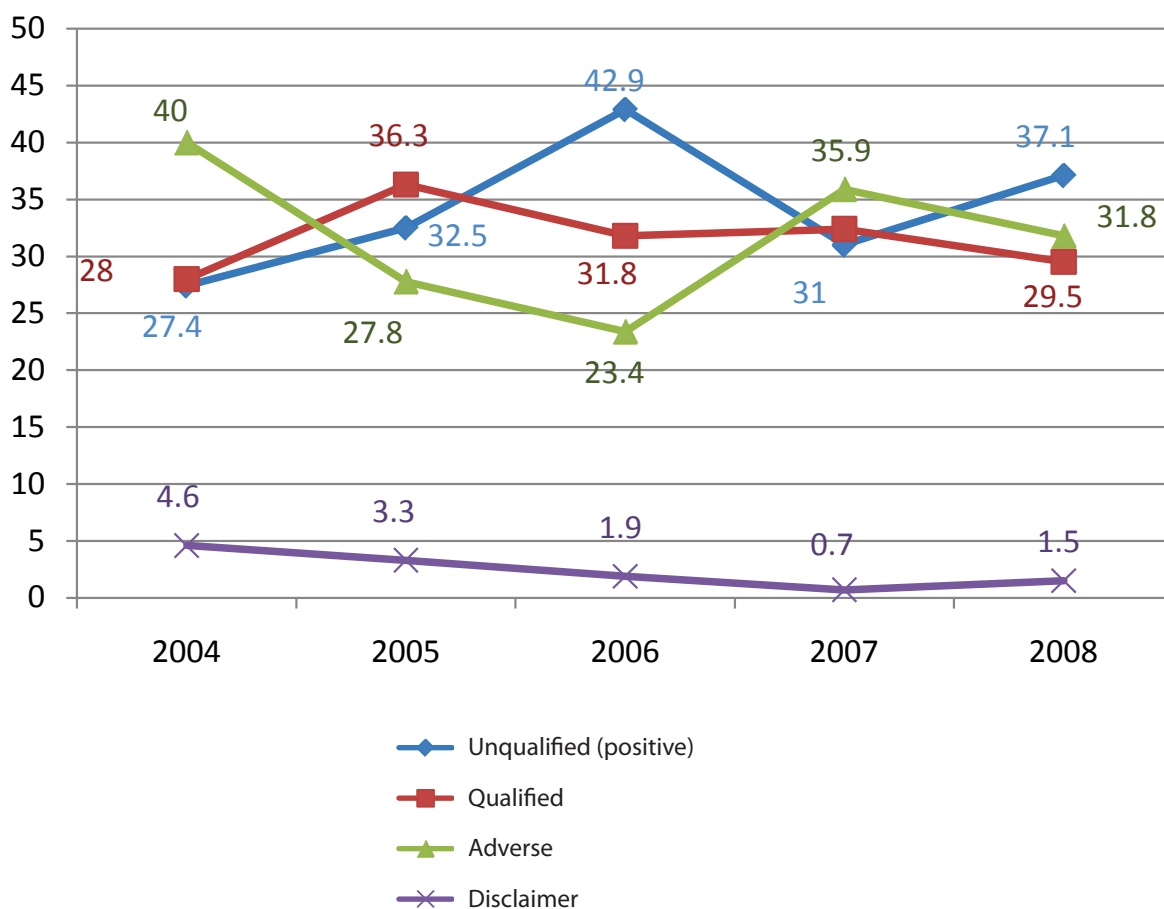
Audit Opinions on Financial Statements

The number of unqualified opinions in a period of 5/five/ years shows upward trend, i.e. from 21,3% in 2004 to 48,0% in 2008. This indicates decrease of the number of found irregularities in the operation and the use of public funds. Upward trend is also seen at qualified opinions: from 25,8% in 2004 to 18,0% in 2008; disclaimers from 10,1% in 2004 to 2,0% in 2008 година; and adverse opinions from 42,7% in 2004 to 32,0% in 2008. This structure of expressed opinions for the analyzed years indicates that, basically, upward trend is obvious for all types of opinions. This further indicates positive feedback from the auditees upon audits and recommendations made in the audit reports.



Audit Opinions on Compliance with the Legislation/Intended and Legal Use of Funds

The audit opinions on compliance with the legislation generally follow the same upward trend: unqualified opinions from 27,4% in 2004 to 37,1% in 2008; adverse opinions from 40,0% in 2004 to 31,8% in 2008; disclaimers from 4,6% in 2004 to 1,5% in 2008. Insignificant increase has been noticed only with qualified opinions: from 28,0% for 2004 to 29,5% in 2008. Generally, the aforementioned structure of expressed opinions on compliance with the legislation indicates upward trend in the analyzed period.



COOPERATION WITH COMPETENT ORGANS

In 2009, the State Audit Office intensified its cooperation with the competent organs through identification and presentation of irregularities, cases of illegal operation, and possible cases of corruption and abuse of office.

At the 64th session the Assembly of the Republic of Macedonia reviewed the Annual Operation Report of the State Audit Office and adopted conclusions regarding the measures to be taken by the Government of the Republic of Macedonia and the competent organs for the purpose of improving the supervision, and spending the public funds.

According to the Law on State Audit, the audit reports on the Central Budget of RM; the budgets of ministries, funds and public enterprises established by law as well as audit reports including disclaimers and adverse opinions on the accuracy and the objectivity of the presented situation, and the results of the operation, are obligatorily submitted to the Assembly of the Republic of Macedonia. 64 audit reports upon audits performed according to the Annual Program for 2009 have been submitted to the Assembly of the Republic of Macedonia.



In order to improve the cooperation between the State Audit Office and the Assembly of the Republic of Macedonia a seminar for members and employees of the Assembly was organized by the Westminster Foundation for Democracy. On the seminar, the topic of which was “Financial Supervision, Budgeting and Audit”, representatives of the State Audit Office also had their presentations.

Another activity to improve the cooperation with the Assembly was a study tour to the Netherlands. Representatives of the Assembly of the Republic of Macedonia –members of the Commission for Financing and Budget, accompanied by members of Component 4, External Communication, of the MATRA Project, visited the Netherlands Court of Audit in the period between 28 September and 1 October 2010.

Within the reporting period 31 audit reports have been submitted to the Government of the Republic of Macedonia. The reports included irregularities in the operation of entities under the competence of the Government.

There is permanent cooperation with the Public Prosecution Office of the Republic of Macedonia. In 2009, the State Audit Office received quarterly and individual reports from the Prosecution Office on acting upon submitted audit reports. During the reporting period 12 audit reports were submitted to the Public Prosecution Office, which included findings on possible misdemeanor or crime.

Final audit reports have been submitted to the State Commission for Prevention of Corruption (15), Ministry of Finance, Ministry of Interior, Financial Police and the responsible organs of the auditees.

TRANSPARENCY OF SAO

Providing access of the public to the results of the operation of the State Audit Office has been defined as one of the five goals of the State Audit Office Development Strategy 2010-2014. In this respect, the final audit reports published on the web site of the State Audit Office, have a high priority in the system of the public information.

In order to be as transparent as possible, beside publishing the results of the completed audits, other information are published as well, related to activities planned by the Annual Program, international activities, bilateral meetings, educational workshops etc.

The official web site remains the most exploited tool for public information. During 2009 the web site was visited 126.501 times, which is 10.541 monthly or 350 daily. The analysis of visits in 2009 showed increase of 12.013 compared with the previous year.

The State Audit Office introduced Intranet as a system of internal information. Exchange of information through this system is performed by publishing all information and documents stemming from the operation of the State Audit Office.

The State Audit Office received 6 (six) requests for access to public information in 2009 and granted them all in compliance with the Law on Free Access to Public Information.





AUDIT ACTIVITIES

BUDGET AND BUDGET USERS

Starting from the definition according to which budgeting is allocation of limited funds for meeting the needs of the citizens of the Republic of Macedonia, it is necessary to base planning and approving **the Budget of the Republic of Macedonia** on observation and application of budget principles, such as completeness, timelines and comprehensiveness. In this respect, it is necessary to:

- Provide timeliness of the budget process, that is, all participants in the process to fulfill their obligations within the deadlines stipulated in the Law on Budgets
- The Government of the Republic of Macedonia to define and adopt strategic priorities and fiscal strategy being the basic documents for preparation of the Budget within the deadlines stipulated in the Law on Budgets
- Budget user to submit their requirements within the legal deadline that is not later than 1 September of the current year.

If the deadlines are not met, as stated in the audit reports, the process of handing down the Budget of the Republic of Macedonia may be slowed down.

In order to have budget requirements that present the real needs, and planned budget funds that comply with the strategic priorities, it is necessary to strengthen the capability of the person responsible for developing the strategic plans and planning the funds at the budget users..

With respect to the collection of the revenues in the budget of the Republic of Macedonia, the risk of incomplete and untimely collection of non-tax **revenues from concessions** has been identified irrespective of the fact that the Ministry of Finance is able to monitor the collection of this fee through the Treasury Department. This may be achieved by creating database to monitor the regularity of payments, through matching the data on signed contacts with the data on collection of concession fee. Irrespective of the fact that, by adopting the Law on Concessions and Other Types of Public Private Partnership, the recommendation of the auditors has been accepted, the legal provisions are not operated in practice.

There is, also, a risk of untimely realization of revenues from **sale of state-owned residences** due to incomplete accounting records in the Ministry of Transportation and Communications, which does not keep data on residences managed in the past. In order to eliminate this situation a recommendation has been made to accelerate the procedure of adoption of the Law on Housing and the Draft Law on Amendments to the Law on Sale of State-owned Residences, to define the methodology of recording the same and assigning the entity to be responsible for recording the mentioned residences.

According to the provisions of the Law on Execution of the Budget of the Republic of Macedonia for 2008, the budget users are obligated to realize at least 30% of the planned **capital expenditures** for a period of six months; the Minister of Finance should transfer the remaining unused amount to the Section "Functions of the State", as reserves for capital expenditures. The audit found that the reasons for the low participation of the capital expenditures in the Budget structure and the slow realization of the same are weaknesses of the funds management, unsuccessful tender procedures and problems with providing construction documentation.

In 2008 and during the previous years the auditors pointed out that, according to the Law on Budgets, the funds from the **current budget reserve** should be spent to cover the expenditures caused by natural disasters or other emergencies. Portions of the current reserve were spent for purposes, which could have been planned during the preparation of the Budget and appropriate items at budget users. Spending the funds for purposes, which could have been planned, creates the risk of insufficiency of funds necessary to resolve situations stipulated in the Law.

Budget funds in amount of denar 596,400 thousand were paid in 2008 for **final court findings to budget users of the executive power**. In the past years the auditors recommended to the Government of the Republic of Macedonia to define the material liability of persons who, in the course of duty, cause impairment to the state organ and spending funds otherwise planned for main activity operations, by making legally unsound decisions and lost lawsuits.

The Annual Program for 2008 of the **Bureau for Commodities** should include information on the type, quantity and the value of the commodities as well as the expiry dates and the manner of renewing the commodities stocks. The Bureau for Drugs should also prepare a list of necessary drugs and medical consumables to provide effective protection of the population in peace and wartime. The auditors found that the Annual Program did not include necessary data on the quantity and the value of the commodities or a list of drugs of special importance, as stipulated in the Law on Commodities.

Within the Sub-program K5 – Appropriate and Just Representation of Ethnic Communities – the Secretariat for Implementation of the Framework Agreement carried out a procedure for employment of 240 persons in 2008. The audit found that the employment procedure was not carried out in compliance with the regulations, that is, there was not prior approval of the Coordination Body for Appropriate and Just Representation. This body was established by the Government of the Republic of Macedonia for identifying the needs of new employments in the administrative organs.

Given the aforementioned, the auditors recommend that, beside the percentage of representation of the ethnic communities, the following should be taken into consideration as well:

- Vacant positions according to the systematization documents,
- Adequate education (type and level of education)
- Available space for settling new employees.

This way will prevent irrational use of budget funds, and inappropriate and untimely use of the human resource.

The auditors recommend that the Ministry of Finance approve new employments within the Sub-program K5 – Appropriate and Just Representation of Ethnic Communities upon completion of the procedures stipulated in the regulations.

The Rule of Procedures of the **Assembly of the Republic of Macedonia** does not include criteria for evaluation of the explanation of absences of members of the Assembly, which is contrary to the Law on Members of Assembly.

Due to the exclusivity of the activities, distance (dispersal) and harmonization with the payment systems of the other countries, the **diplomatic and consular posts abroad**, present unspent funds on

31 December on their accounts and daily operation treasuries, which is contrary to the Law on Budgets, and allows unintended use of funds. In 2009 the competent ministry took measures for elimination of this problem and presented the intention to initiate amendments to the Law on Budgets to prolong the deadline until 15 January the following year, in order to enable diplomatic and consular posts enforce the right to use of funds.

Audit of the public procurement procedures at diplomatic and consular posts, which they mainly carry out by way of gathering bids without public announcement, found irregularities with respect to the Law on Public Procedures. In this respect, the Ministry of Foreign Affairs offered an initiative to the Public Procurement Bureau for amending the Law from the aspect of releasing the diplomatic and consular posts from the obligation to carry out procedures for signing a contract up to a certain amount, whereas the obligation to report to the Public Procurement Bureau remains. The reason for such exclusion is objective, that is, the distance of the diplomatic and consular posts from central administration of the Ministry.

With respect to the sale contracts and adaptation of facilities of embassies and missions of the Republic of Macedonia, the audit found that the competent ministry acted upon the recommendations of the state auditor. Namely, in 2009 the activities for purchasing facilities for embassies and missions abroad were interrupted due to insufficiency of budget funds; adaptation works in Vienna and Ljubljana were completed and the facilities became operative; the funds for the embassy in Moscow were returned due to the failure to regulate the ownership of the Republic of Macedonia.

There is not a system in place for control over the criteria for fulfilling the **veteran and disability protection rights** and the process of their payment in compliance with the regulations. The Office for Veterans and War Invalids, as an agency of the **Ministry of Labor and Social policy**, is responsible for these matters. The Office independently keeps a register of beneficiaries and identifies the legal grounds for granting allowances. The Minister of Labor and Social Policy has tasked its Internal Audit Department with dealing with this matter.

The audit found unrecorded construction facilities at the Ministry of Labor and Social Policy due to uncalculated value and unconfirmed ownership status by a competent organ (Real Estate Cadastre Agency). Measures have been taken for elimination of this problem by way of submitting appropriate requests to the competent institutions, and by determining the ownership status, the facilities are progressively recorded in the accounting records of the Ministry.

In the Ministry of Defense the auditors identified the risk of untimely and incomplete calculation and collection of incomes from leases the reason being absence of database on capital assets, and incomplete and partially arranged organization and operational procedures that to are to provide functioning, monitoring and developing a stable financial management and control.

During 2008 и 2009 measures and activities had been taken for evaluation of the real estate value, and obtaining proof (title deed) of the utilization right from the Real Estate Cadastre Agency. For this purpose, a 3-year contract was signed in 2008 for real estate exposure – facilities, business offices, apartments and land.

In 2008 and in the previous period the Ministry has collected income from long-term real estate lease, in compliance with the Law on Use and Operation of State-owned Property. According to this Law, this type of income is an income of the Budget of the Republic of Macedonia, and it has to be paid on a separate account in the Treasury Department. Following the audit recommendations and the proposals from the



СВЕТИ КИРИЛ
И МЕТОДИЈ

commission for reviewing the leasing contracts, established by the Minister, the Ministry has performed activities for identifying the situation with the real estate and handover of the same, as well as updating, and keeping records on the real estate utilized by the Ministry. The Logistics and real Estate Sector delivered warning letters, and initiated collection of unpaid debts from a large number of lessees. This resulted in a number of lawsuits filed to the competent court through the Procurator General of the Republic of Macedonia.

Similar is the situation with the income from sale and lease of apartments of the former Yugoslav Army, which the Ministry acquired after the Republic of Macedonia became an independent state, under construction, acquired by way of yielding and exchanging real estate, as well as apartments acquired based on decisions of the Government of the Republic of Macedonia. There are not complete and updated records to reveal the number of apartments available to the Ministry, there is no inventory of the apartments or contracts signed by the beneficiaries, and the lease is not collected. This situation results in less income entering the Budget of the Republic of Macedonia

The auditors made precise recommendations for elimination of the identified irregularities and a general recommendation to the responsible persons in the Ministry and all other institutions that may contribute to improving the situation (Government of the Republic of Macedonia, Ministry of Finance, Real Estate Cadastre Agency, Procurator General of the Republic of Macedonia) to take appropriate measures and activities within their competence.

In the Ministry of Health procurements have been made as planned by the draft strategic plan for the period 2008-2010 within the Programs for modernization and promotion of the health sector, in order to improve the efficiency of the working conditions in public health institutions.

The results from the performed audit of the capital expenditures in health, point to the improper application of certain procedures for public procurement of medical equipment, video surveillance, services for preparation of project documentation for reconstruction, construction, and additional works for counters for the needs of the public health institutions. Weaknesses refer to the lack of competition of suppliers, invalid proof and amendments in the conditions of the tender documentation for the purpose of proving the technical and technological capacity of candidates, non-adherence to the approved bonuses of the selected supplier, non-observance of the final delivery term for the equipment, advance payments of the agreed amount prior to delivery and construction of the equipment etc. The audit has given recommendations to improve the procurement process and they were accepted by the responsible persons in the Ministry.

Upon audits performed in the public health institutions, the State Audit Office recommends that the activities for adoption and establishment of appropriate written procedures, control mechanisms and accounting policies for monitoring the stock and medical materials continue, whereby control of their use and management will be enabled.

Currently, the project for procurement of an integrated health IT system – IZIS is being realized, under which it is expected that inconsistencies in the inventory, recording and spending of stock will be resolved.

In the Ministry of Agriculture and Water Supply, subject of audit were the expenditures for subsidies and transfers whereby weaknesses were identified in the activities that refer to the application of documents regulating the criteria for indemnification of the animal breeders for the slaughtered animals

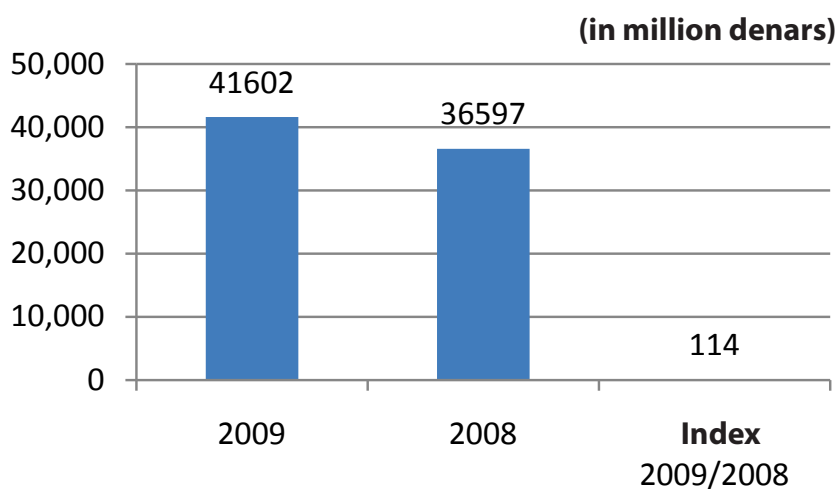
and the improper application of the Program for Animal Health Protection. Whilst realizing the program for financial support to agriculture and the program for encouraging the development of organic agricultural production in 2008, the specified criteria were not observed with respect to the allocation of financial support to applicants in view of determining the structure of points, inclusion of applicants that do not meet the requirements for subsidies, advance payments without confirmation of realized activities by beneficiaries and without submission of the financial report on the intended use of allocated funds.

The audit gave recommendations to eliminate such weaknesses, and they were accepted by the Minister and the responsible persons in the Ministry as further activities.

At the budget beneficiaries that were subject to audit under the Annual Program 2009 (Faculty of Architecture, DSL Zafir Sajto, - Kumanovo, Macedonian Theatre – Skopje, Institute for Earthquake Engineering and Engineering Seismology – Skopje, Institute for Sociological and Political and Legal Research – Skopje) there is no system for regular internal accounting control that will provide assurance that all transactions are performed in accordance with the regulations and appropriate accounting documentation. There is absence of controls and procedures in the organizational structure of auditees that need to provide functioning, monitoring and development of an efficient system of safe financial management and control. The reason for such conditions is absence of staff for the employment of which prior approval is needed from the Ministry of Finance.

At budget beneficiaries, weaknesses were identified in the application of certain public procurement procedures. Irregularities have been identified with respect to the evaluation of economic operators, criteria for assessing the most favorable offer in economic terms, proving the financial capacity and capacity to perform professional activities, the effect of which is the non-transparency of supplies, fair competition and non-economic spending of funds. It has been identified, upon the performed audits on the undertaken measures according to the audit recommendations, at the beginning of 2010, that recommendations are acted upon to rectify the irregularities.

Audited expenditures at Central Budget users and beneficiaries



HEALTH INSURANCE FUND OF MACEDONIA

The audit at the Health Insurance Fund of Macedonia revealed absence of adequate control mechanisms and written procedures for full control over:

- sick leave benefits,
- health services in the primary health protection level, laboratory and drugs issued on prescriptions ,
- issuance of confirmations of paid health insurance contribution.

Recommendation of the State Audit Office to the Health Insurance Fund of Macedonia is to develop written procedures, and to establish reliable and efficient control mechanism in various segments of its operation, in order to reduce or prevent the risk of incorrect payments.

The audit of the planning of budget limits and payment of health services to specialized health institutions and hospitals by the Health Insurance Fund of Macedonia revealed the following::

- disagreement of the deadline for signing contracts with health institutions with the time period , which is analyzed and is basis for determining the budget limits for the following year
- corrections of the budget requirements at some health institutions, without clearly defined criteria about the grounds and the amount of the correction made
- partially made analysis for satisfying the criteria for payment of the variable portion of the health service compensation to the health institutions

In order to eliminate some of this situation the Fund made amendments to its regulations applicable as of 01.01.2010.

The Fund should also make permanent and occasional analysis, and based on the results make payments of the variable part of the health service compensation.



During 2008 the Fund calculated the amount of the compensation for pharmacies without legally defined criteria and determined value points for each criterion.

In order to eliminate this situation the Fund adopted Regulation on the Procedure for Calculation of the Monthly Amount of Funds that the health institution may receive for drugs issued on prescription, from the list of drugs that the Fund compensates for as well as Guidelines on Control of Invoices in Pharmacies, applicable as of 01.01.2010.

A managerial contract has been signed with one of the two directors of the Fund. This is why the Fund required that the Government of the Republic of Macedonia regulate signing a second contract in order to provide equal rights and responsibilities for both directors.

The State Audit Office found not registered ownership right and use of property of the Fund; for this reason the Fund submitted a request to the Real Estate Cadastre Agency for providing a document to confirm the ownership right/right to use facilities and land.

The State Audit Office recommended finalization of the activities for obtaining the document to confirm the ownership right/right to use real estate, and reconciliation of the value of the facilities and the land in the Health Insurance Fund of Macedonia, the district offices and in the public health institutions.

The audit found payments to persons engaged through the Temporary Employments Agency for tasks and duties of a permanent employment and not temporary ones. The Fund submitted requests for permanent employment of these persons.

The State Audit Office recommends finalization of the activities for obtaining approval for permanent employments of persons to fill vacant positions according to the Fund's Systematization Document.

PENSION AND DISABILITY INSURANCE FUND

The construction of the new administrative facility of the Headquarters of the Pension and Disability Insurance Fund has been completed in 2008 for which the Fund has a title deed for a sub-facility and land. The procedure for obtaining a title deed for the administrative building is in progress.

With respect to the district offices, for which the Fund has no title deeds, requests have been submitted to the Real Estate Cadastre Agency, for obtaining a document for the registered right to ownership/use of construction facilities and land.

By auditing the number of engaged staff that performed the tasks and obligations, a document was prescribed and specified for the organization and systematization of job positions, the audit determined that at the level of the Fund the vacancies are filled completely whereas in regional units the distribution of employees is not in accordance with the stipulated number of employees according to the staffing regulation.

The audit points out the need that competent bodies for managing the Fund should harmonize the organization and systematization document in the appropriate department of the Pension and Disability Insurance Fund due to the equal distribution of the number of employees and the rational use of employees.

The Pension and Disability Insurance Fund undertakes a series of measures by which the opportunities for the insurees to exercise their right to pension are increased:

- For a part of the non-collected receivable for pension and disability contributions there is a court proceeding and a permanent collateral - shares, parts, movable and immovable property from bonds.

To ensure the legal framework for performing sale, cashing in of the property and recognizing the working experience of insurees, an initiative was undertaken to amend the Law on Pension and Disability Insurance, the Charter of the Fund and the Bankruptcy Law and

- For insurees, whose bonds are bankrupt or liquidated and have unpaid liability for pension and disability insurance contribution, it will remain unpaid due to the absence of ownership of the property related to the bonds whereby the insurees may not enforce their right to pension. To eliminate such situation, the Fund took measures to amend the Law on Pension and Disability Insurance by which insurees would be enabled to pay the contribution and enforce their right to pension.

The Fund is obligated to permanently record i.e. transfer documents and data on the work experience, salaries and compensation fees for insurees for each working year in an electronic medium based on which the pension and disability insurance rights are enforced.

Upon inspecting the pension files, the data in the electronic media and the database including data on the work experience, salaries and compensation fees for each working year, the audit determined that there is an absence of complete harmonization between databases.

From the aspect of the given recommendations – the adoption of solutions for recognizing the pension right – to be based on accurate, complete and reliable data whereby the payment of pensions

will be legal and intended, there are several project activities underway: Project for Calculation and Payment of Pensions, Project for Digitalization of Microfilms, and Project M-4, which will lead to higher efficiency and quality in all processes related to payment of pensions.

In accordance with the Law on Contributions and Obligatory Social Insurance, starting as of 01.01.2009 the control, specification, payment, enforced collection, out-datedness and writing off of contributions for obligatory social insurance (pension and disability insurance, compulsory capital funded pension insurance, work experience that is calculated with a lengthened duration, health insurance and unemployment insurance) are performed by the Public Revenue Office.



The contributions for obligatory social insurance, such as public expenditures, are **income** to institutions for compulsory social insurance – funds (Pension and Disability Insurance Fund of Macedonia, Health Insurance Fund and Employment Agency of Macedonia).

The Public Revenue Office and the Funds have an obligation to exchange data on bonds for payment of contributions, **calculation and paying in of contributions, amounts of calculated, collected and non-collected contributions**, as well as other official data related to contributions. However, funds receive data from the Public Revenue Office only for calculated and collected contributions, and not data on non-collected contributions.

Such situation causes funds not to dispose of accurate data on expected and non-collected contributions/income that will be the basis for planning of their budgets, and the Budget of the Republic of Macedonia, for statistical and other needs as well as for implementation of additional control when determining data on contributions.

Due to the aforesaid, the audit determined that the funds in coordination with the Public Revenue Office should take activities, the amount of expected and future income to be recorded in the accounting records and stated in the financial reports of these institutions.

EMPLOYMENT AGENCY OF THE REPUBLIC OF MACEDONIA

According to the Law on Employment and Unemployment Insurance, an unemployed person who was uninterruptedly employed for at least nine months or 12 months with interruptions during the last 18 months, is entitled to compensation.

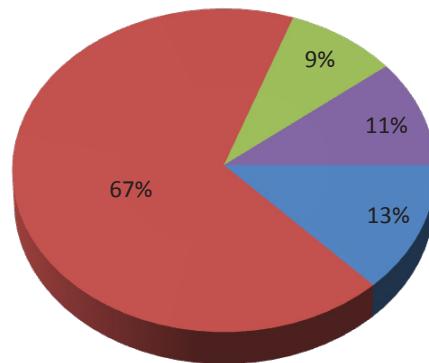
The State Audit Office reviewed the procedure for enforcing the right to compensation for:

- regular beneficiaries,
- receivership redundancy workers
- redundancies
- as well as the legality of enforcing the right to compensation, accuracy of calculation, its recording and payment.

The audit found legal use of funds for compensation to unemployed persons, and intended payment of the same during 2008.

The following graphic shows the paid funds for compensations in 2008, for which decisions were made during the year and previous years:

Graphic on paid funds for compensations in the Employment Agency of RM



- Allowance for bankruptcy redundancies
- Allowances for redundancies
- Allowances for regular beneficiaries
- Other allowances

The audit found that, for the decisions on recognition of the right to compensation until August 2008, there is no methodology or internal regulations, except the provisions of the Law, to regulate the process and prevent errors or frauds.

This situation resulted in incompleteness of a number of cases for which decisions had been issued during the previous years, and payments were made in 2008 as well.

List of necessary documents for enforcing this right was created in September 2006 and distributed to all employment centers throughout the Republic, for the purpose of unifying the procedure for enforcing the right to compensation.

During 2009 the Agency developed Guidelines on the Manner and the Procedure for Enforcing the Rights to Unemployment Insurance, which defines the course and the type of this process, and related the activities.

The audit recommends that the competent organs for managing the Agency provide adequate application of the Guidelines on the Manner and the Procedure for Enforcing the Rights to Unemployment Insurance. This will prevent the risk of making incorrect and incomplete decision on enforcing of the right to compensation during the period of unemployment, and the risk related to the correctness of the payments made upon this right.

LOCAL SELF - GOVERNMENT

The audit revealed insufficient coverage of the risks in processes by internal controls or absence of **internal control**, at most of the audited municipalities. It is necessary to establish full control of operation through written procedures, based on the principle of safe financial management. This will enable legal, intended, economical, efficient and effective use of the funds. In order to improve the operation the municipalities have to strengthen their internal control departments, thus contributing to achieving the goal.

Recommendation of the State Audit Office, in circumstances when during the fiscal year, the income and the expenditures are not realized as planned by the municipality budget, to perform **reprogramming of the municipality budget**. This will enable assuming liabilities based on realistic amounts of funds.

Complete and regularly updated **data base of taxpayers** will result in higher municipality income. Large number of audited municipalities initiated activities for completion of records by working in the field. With respect to collection of taxes, not all legal measures are taken to bring it to a satisfactory level.

Payments of funds have been found without previously developed programs and criteria for use and granting funds for social protection, payments to non-government organizations, and cultural and sport events. Absence of such documents is the reason for partiality in decision-making, lack of transparency, and illegal and unintended use of funds.

There is legal obligation for regular reconciliation of **movable properties and real estate registers** between the municipalities in the Republic and the Real Estate Cadastre Agency; however, this has not been done yet, because according to the Law on Property tax, the administration offices of the City of Skopje and the municipalities keep registers of real state based on the unique registration numbers of citizens, and the the Real Estate Cadastre Agency based on the cadastre municipality, number of a cadastre plot or number of a title deed.

Cooperation with public enterprises, for a number of audited municipalities is performed without agreements to regulate the rights and responsibilities with respect to defining the prices of services, and the manner of providing evidence on the performed activities.

At a number of audited municipalities in 2009 as well, the transferred equipment, facilities and other investments by the municipalities, owned by the public enterprises, did not have a treatment of **share of the municipalities and the City in the public enterprises**. This might have significant consequences in case of transformation of a public enterprise and determining the structure of the founding capital, and further losing the position as a shareholder or partner in their management. It is necessary to determine the share and registration of the same.

According to the Law on Local-self Government, the municipalities can sell and offer for use its properties only by way of public bidding. There is no special law, and the public bidding procedure is only regulated by the Law on Use of State-owned Property, which does not treat the municipalities. This legal inconsistency causes flaws and irregularities at sales to/yielding to other entities, of the municipality properties. It is necessary that law regulate management and use of property of municipalities.

The income from fees for arranging construction land is a significant source of income for financing the municipalities and the City of Skopje, and is strictly intended to realization of the program for Arrangement of Construction Land. We have performed municipality – wide audit at 10 municipalities and the City of Skopje, in order to review the collection of this fee and the intended use of the funds from the same. Based on the findings, the State Audit Office recommended the following:

- **Software application for calculation of the fee from arranging construction land** in the City of Skopje should be develop, with network connection between the municipalities and the City, in order to avoid the risk of incorrect calculation of the fee and collection of lower income for both the municipalities and the City of Skopje
- Municipalities and the City of Skopje, in cooperation with the utility enterprises, operating the infrastructure facilities, should create a **register of data on the status of infrastructure facilities** as grounds for quality planning of the activities of the program for Arranging Construction Land. Very often, lack of such data increases the value of the facilities under construction due to additional activities not foreseen by the Program (underground installations)) thus imposing additional costs. Having in mind that developing database is a long and expensive process, the municipalities and the City of Skopje have to initiate its implementation as soon as possible.
- Internal document and written procedures should be developed in order to enable adequate application of the Law on Construction, and the **necessary documents and procedures** should be determined to be included in each construction facility file, such as: construction project and construction license; observation of deadlines for implementation of projects and construction works; calculation and collection of penalties for delays; obligatory keeping construction logs by contractors to be made available to investors after finalization of construction works; supervision of construction to be assigned to authorized experts, who will write phase and final construction reports; after the final technical inspection is performed and license for use is issued by the municipality, composing minutes on handover of the finalized facility, to be signed by both the contractor and the investor.

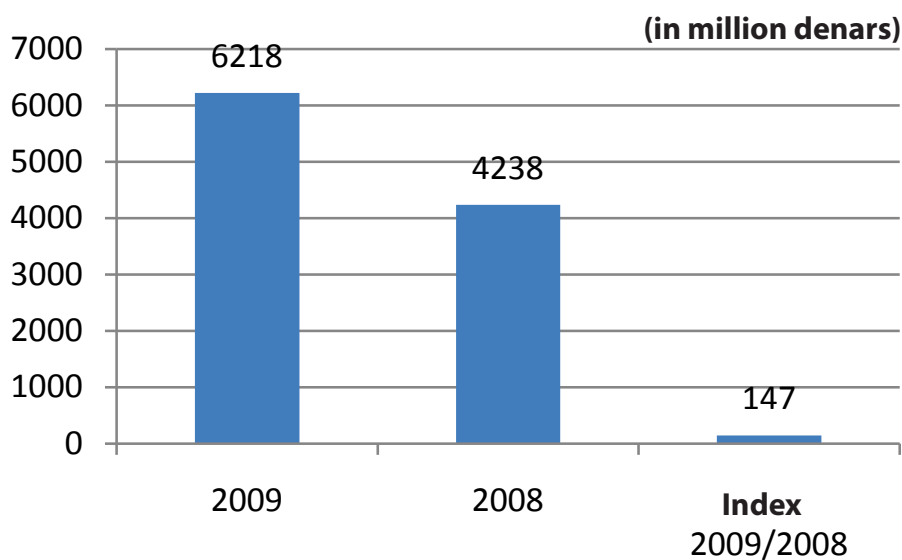
This manner of operation will contribute to: elimination of the found irregularities resulting from non-observation of the Law on Construction; keeping complete and well-arranged construction documentation, and high-quality construction works and reduction of costs. .

With respect to allocation of funds of intended subsidies to the municipality public institutions, recommendation of the State Audit Office to the municipality councils is to adopt written criteria on allocation of funds.

With respect to the public procurement the audit identified significant improvement of the procedures and their implementation, at many municipalities. There are, however, cases of absence of procedures for procurement of some goods and services as well as signing annexes to basic contracts without procedures, especially for construction works.

Audited Expenditures at LSU

Budgets of local self-government units



PUBLIC ENTERPRISES

The reduced economic activity in 2009 resulted in lower liquidity and solvency of the public enterprises that were subjected to audit. This is seen in reduction of the collection of the performed services, which further results in permanent negative financial effect at the entities, inadequate payment of taxes and contributions, and other obligations to the Budget of the Republic of Macedonia; avoiding bank account payments and performing cash payments instead, frozen accounts and irregular use of cash funds.

The results of the audit indicate presence of risks in performing the activities of public interest as follows:

Drinking water supply and elimination of urban waste waters

- Absence of control over the water inflow/outflow at the water supply system;
- Inadequate number of waterflow meters for calculation of the real quantity of drinking water used;
- Absence of agreements between the public enterprises and the user for arranging the rights and responsibilities;

Waste management

- Absence of license for collection and transport of waste;
- Absence of daily records on prescribed form on the quantity of waste;
- Absence of agreements with the entities producing commercial waste;
- Absence of careful selection of waste;
- Non-observance of rules for burning waste/uncontrolled burning of waste;
- Inappropriately arranged dumping grounds
- Monitoring of waste management and developing the information system on local level;

Public hygiene maintenance

- Absence of devices and authentic documents to confirm the performed services;
- Absence of internal regulation on calculation of the fee for maintaining public hygiene ;
- Absence of invoices to the founder of the public enterprise (municipality) for performed services;

Maintenance and protection of national roads, and road toll collection

- Uncertainty about the completeness of collected and paid funds for road toll, and the influence of the human factor in the collection system;
- Non-harmonized and incomplete process of registration of property right, that is, use of material assets (land and facilities);
- negative financial situation with aggravated liquidity¹¹ and solvency¹², that is, insufficient funds and untimely payment of maturing obligations;
- reduction of the scope of performed activities resulting in reduction of the total income of the enterprise ;



Public railroad transportation

- Imbalance has been created by division of the public enterprise, between the value of the assets and the liabilities in the balance Sheet;
- No credible and written criteria have been presented on the manner of compensating costs, that is, payment of the fee for use of the railroad infrastructure ;
- There have not been conditions for regular payment of obligations for loans and credits, for which the Ministry of Finance made payments on behalf of the Republic of Macedonia;
- There is no registration of the main capital in the Central Securities Depository JSC Skopje;

Beside the previously identified risks in the operation of the auditees, weaknesses have been identified of the internal control system of the procurement system, resulting in the possible unfair competition, absence of equal treatment of bidders, and absence of transparency and publicity of procurement of goods and services.

¹¹ Liquidity relates to availability of funds in near future, after the financial liabilities are taken into consideration, and

¹² Solvency relates to availability of funds during a long time period for fulfilling maturing financial liabilities.

Appropriate measures and activities for elimination of the identified situation should be taken by the competent organs for managing the auditees, especially public enterprises performing utility activities. It is necessary to regulate the relations with the founder, regular invoicing and presenting the VAT amounts, as well as realistic measuring and invoicing the drinking water quantities used.

Adoption of the National Waste Management Plan (2009-2015) of the Republic of Macedonia (Official gazette of RM No. 77/2009) as well as the decisions for initiating a procedure for granting concession for financing, projecting, constructing and managing the regional solid waste dumping ground in several regions, is a basis for development and implementation of an integrated waste management system, and elimination of the identified situation regarding the waste management by the auditee, environmental protection and protection of the health of the citizens.

Permanent organization and implementation of education by the competent organ in the area of the public procurement, appropriate treatment of the human resources and creation of appropriate organizational form of procedures for granting public procurement contracts as well as realization of public procurement contracts by the contracting organs (auditees) creates preconditions for elimination of irregularities in the public procurement procedures, observing the public procurement principles (competition between economic operators, equal treatment and non-discrimination of the same, transparency and integrity of the process of granting public procurement contracts, and rational and efficient use of funds in the procedures of granting public procurement contracts) as well as procurement of goods, services and works under best possible economic conditions.

Creating conditions for establishing appropriate financial management and control system, and risk management will be a challenge for the management teams of the public sector entities. This will contribute to the reasonable assurance that the goals of the entities will be achieved, that is, realization of activities of public interest in an accurate, ethical, economical, effective and efficient manner.

PERFORMANCE AUDIT

Performance audits in 2009 focused on evaluating a number of activities and functions in various areas as follows:

1. Records and coordination of data on foreign assistance in the Republic of Macedonia;
2. Activities related to reduction of climate changes in the Republic of Macedonia – International parallel performance audit in coordination of EUROSAI WGEA ROSAI WGEA;
3. Activities related to fire protection in the Republic of Macedonia;
4. Activities in the area of public services – emergency medical aid in the Republic of Macedonia (in phase of drafting a preliminary report));

The performance audit of the **records and coordination of data on foreign assistance in the Republic of Macedonia** focused on the functions of the competent institutions regarding the objective presentation of the situation with the records, coordination and the completeness of the data on projects financed by foreign assistance funds as well as other aspects of their operation.

The foreign assistance, from the aspect of application and preparation of draft projects, and the receipt, use, recording, monitoring and reporting on the effects has not been not regulated by laws or sub-laws. Foreign assistance is granted based on procedures determined by each donor individually; there are no coordinated procedures for granting foreign assistance or methodology for project cycle management to be implemented by the institutions - beneficiaries of the foreign assistance. A number of limitations obstructed the evaluation of the degree of utilization of the foreign assistance funds, mainly related to comparability of the data available to the competent ministries against the information available to the Central Database on Foreign Assistance of the Government of RM (CDAD). At several ministries there is insufficiency of personnel for the projected activities as well as differences in organization of the units coordinating the foreign assistance.

The performance audit for **reduction of the effect of climate changes in the Republic of Macedonia** found that the Republic of Macedonia has laws and sub laws, national strategies and plans, and measures and projections, which mainly cover and regulate the activities for reduction of the emission of greenhouse gasses thus affecting the activities for reduction and dealing with climate changes. This is a good basis for national and international implementation of provisions stemming from the international conventions. Measures and activities have been undertaken for reduction of emission of greenhouse gasses in all risk areas, and reduction of/dealing with climate changes. These measures could only be implemented if financial conditions were met, as well as the conditions for human capacities building and creation of coordination among all institutions that have competence over the process of reduction the climate changes in the Republic of Macedonia.

With respect to reduction of the effects and the **fire protection in the Republic of Macedonia** in 2008/2009 activities have been performed to improve the situation by preparing a feasibility study for implementation of the single European number for emergency calls E – 112 as well as purchase of new vehicles and aircrafts for fire extinguishment. Yet, inconsistencies and weaknesses were found related to absence of the key laws and regulations, strategies, plans and estimations as well as overlap of authorities of the entities responsible for fire protection, age of the equipment and facilities between 25 and 47 years, and the need of increasing the number of personnel and improving their capabilities.



The goal of the performance audit of the **public service – emergency medical aid** in the Republic of Macedonia, which has reached the phase of drafting a preliminary report, is to assess the risks and the possibilities for improvement the emergency medical aid system in the Republic of Macedonia.



PUBLIC PROCUREMENTS

In accordance with the planned audits, in 2009 the state audit office audited the public procurements that the auditees carried out during 2008, and identified the following irregularities:

About one fourth of the identified irregularities relate to procurement of goods, services and works **without public procurement procedure**.

There is significant inobservance of the regulations in the phase of **evaluation, proposal for selection of the best bidder, and making the actual selection**. Namely, inconsistencies were identified at performing evaluation, inappropriate application of the ranking methodology, irregularities at creation of ranking lists, proposing for selection certain bidders although they did not meet the set criteria.

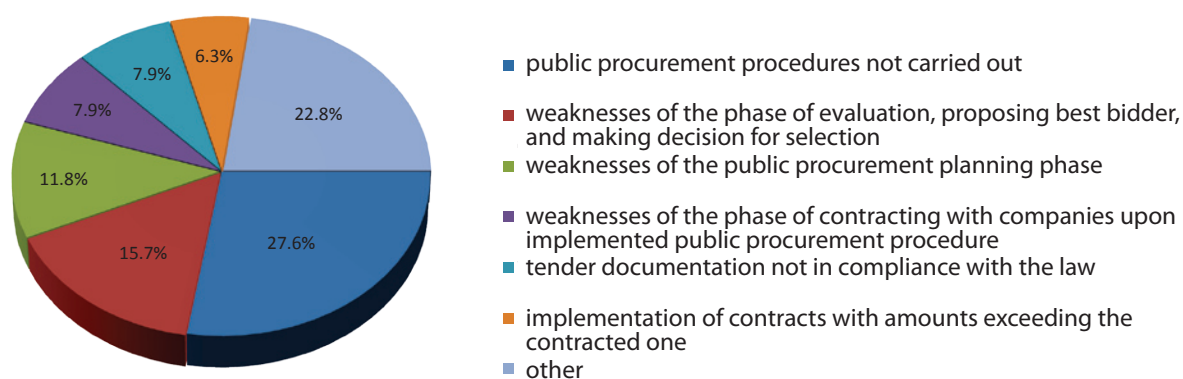
Absence of public procurement plan and other weaknesses in the planning phase make about 12% of the identified irregularities. The irregularities most often relate to absence of public procurement plan, elements prescribed by law and absence of/untimely amendments to the plan.

In the **contracting phase**, 7,9% of the total of irregularities were found. There are contracts concluded, which do not include the basic elements of the tender documentation or the bid: price, quantity or value. Other contracts include conditions different from those of the bids or the tender documentation, and value higher than the one included in the decision for public procurement or the plan.

There are contracts carried out **with higher amounts than the contracted** or the additional value surpasses the limit stipulated by law.

While carrying out the contracts, very often the deadlines and conditions are not met, the contracting organ does not apply the penalty provisions of the contract, or the submitted guarantees are not activated/used in cases specified in the contracts.

Public procurement 2009



In the **tender documentation**, the contracting organs do not always provide complete, accurate and precise information about the manner of performing the procedure, that is, it does not include the obligatory elements; deadlines are shorter than the planned; there are technical characteristics indicating the origin and the type of product; there is no criteria for eligibility, i.e. selection for procurement, or the technical documentation is modified after the bids are received..

The audit identified inconsistencies in application of the law at the process of **making decisions on public procurement**, which do not exist at all or the decision documents lack some obligatory elements: subject, quantity, amount and source of funds, manner and procedure for granting a public procurement contract.

MEASURES TAKEN UPON AUDIT REPORTS

The goal of the audit, as a necessary part of the control system, is to timely identify deviations from the accepted standards and the violations of the principles of legality, efficiency, effectiveness and economy of operation, in managing public funds, for the purpose of taking corrective measures in certain cases, and taking steps for elimination or prevention of such deviations and violations in future.

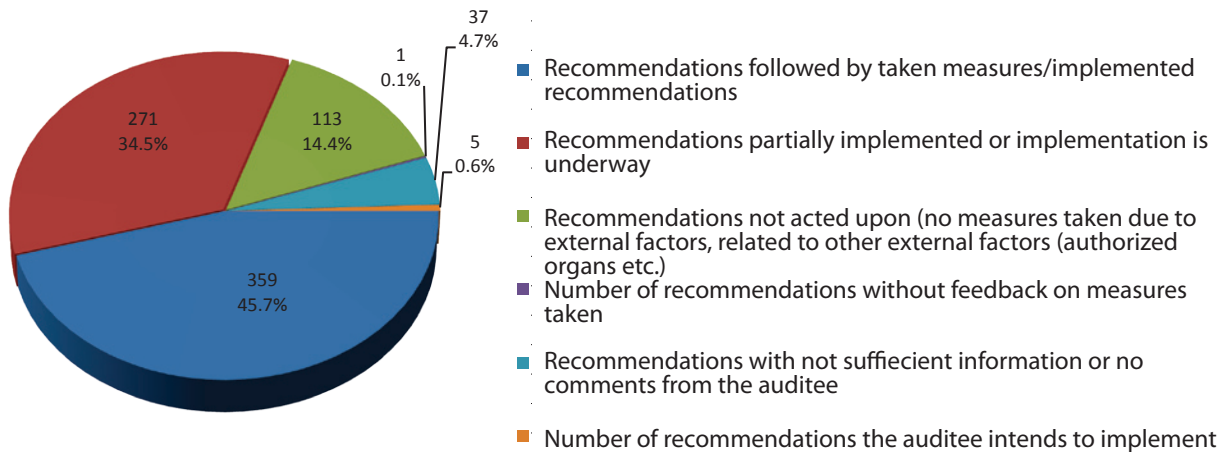
Within the regular audits, special audits and follow-up reviews, the process of implementation of recommendations is permanently monitored for the purpose of maintaining effective control procedures at auditees. The recommendations and feedback form the same create the basis for the follow-up.

According to the Law on State Audit, the competent organs for the operation of the auditee are obligated to notify the State Audit Office on the measures taken regarding the findings of the audit reports within 90 days of the day of the final report has been received.

The State Audit Office performed 55 follow-up reviews upon audits performed in 2009, for the purpose of identifying the extent of implementation of the recommendations included in the final audit reports.

Upon completion of the audits, the State Audit Office made 996 recommendations (920 upon financial audits and 76 thematic financial audits). Until the date of preparation of the Annual report for 2009, for 210 recommendations the deadline for feedback from auditees has not expired. Of the 786 recommendations, 359 have been completely implemented, 271 have been partially implemented or implementation is underway, 113 have not been implemented (related to other competent organs/external factors or discrepancies), and five recommendations are planned to be implemented. The auditee has not provided comments on 37 recommendations, and for one recommendation, the auditee has not provided any feedback.

Implementation of recommendations upon audit reports of 2009



General conclusion from the audits and the received feedback from the legal entities and the competent organs is that majority of the recommendations have been implemented by the auditees and the competent organs. The analyses show that of the total number of recommendations (786) upon which the auditees were obligated to take measures, 630 or 80% were implemented, completely or partially until the date of preparation of the Annual Report. In 2009, there was 51% increase of completely and partially implemented recommendations compared with 2008.

The audits confirmed that some recommendations require longer time for implementation due to their complexity (required approval from competent organs, proof of ownership, and transformation of the ownership status of some entities). The State Audit Office encourages the auditees to continue their activities until full implementation of these recommendations.

INTERNATIONAL COOPERATION

The State Audit Office continues its bilateral and multilateral cooperation with other SAIs, and the international institutions and organizations in order to acquire and exchange experience of the public sector audit. The State Audit Office is a member of the International Organization of Supreme Audit Institutions (INTOSAI) since 2001, and the European Organization of Supreme Audit Institutions (EUROSAI) since 2002. At the same time, since 2005 the State Audit Office is an active member of the network composed of SAIs of candidate countries and potential candidate countries for EU membership, and the European Court of Auditors in Luxemburg. Since 2006 the candidate status of the Republic of Macedonia has allowed the State Audit Office to attend the meetings of the Contact Committee of the heads of the EU SAIs and the European Court of Auditors, as an active observer.

European Organization of Supreme Audit Institutions (EUROSAI)

The State Audit Office is a member of the EUROSAI environment working group since 2002 and the IT working group since 2005. During 2009 representatives of the State Audit Office attended the meetings and the thematic seminars of these working groups in Warsaw, Bern and Antwerp. The State Audit Office participated in a coordinated parallel audit on climate changes and in drawing up the joint final report together with nine other SAIs –members of EUROSAI.

At the invitation of the INTOSAI Developing Initiative (IDI¹³) and the EUROSAI, the State Audit Office joined two new international projects in order to strengthen its capacities and to improve the professional skills of its employees. These two projects are 2-year programs: a) public debt audit, and b) parallel audit of programs for increasing employment in the public sector of persons with special needs.

A delegation headed by the General State Auditor attended the II EUROSAI - ARABOSAI¹⁴ Conference that took place in Paris in March 2009. The topic of this Conference was “The role of the supreme audit institutions in improving the operation of state institutions”.



¹³ INTOSAI Development Initiative

¹⁴ Arab Organization of Supreme Audit Institutions

Network of SAIs of Candidate Countries and Potential Candidate Countries for EU Accession and the European Court of Auditors

Representatives of the State Audit Office attended the meetings of the SAIs and were actively included in defining the priorities for strengthening the institutional capacities of the State Audit Office and the other SAIs walking on the road to EU accession. For this purpose a representative of the State Audit Office attended the meeting of liaison officers in Luxemburg in 2009. In December of the same year, the General State Auditor attended the meeting of the Contact Committee in Budapest, composed of heads of SAIs of the EU members and the European Court of Auditors.

The State Audit Office cooperates with the European Court of Auditors regarding the internship program at the European Court for junior auditors employed with the SAIs of the candidate countries Croatia, Macedonia and Turkey. By the end of 2009 five junior auditors of the State Audit Office had completed the 5-month program.



Bilateral and Regional Cooperation

Within the bilateral cooperation, working meetings have taken place with representatives of the supreme audit institutions of Albania, Croatia and Bulgaria, where experience has been exchanged on current topics in the area of the state audit. Within the cooperation between the State Audit Office of Macedonia and the SAI of Bulgaria, 15 auditors of each institutions attended a seminar organized in Berovo, Republic of Macedonia. Representatives of both institutions exchange experience on various topics of the audit practice.

MATRA¹⁵ Pre-accession Project Program

The successful cooperation between the State Audit Office and the Netherlands Court of Audit within the Twinning Project of 2005-2008 continued in 2009 in a form of a project to finish at the end of 2010. The Project is financed through the Ministry of Foreign Affairs of the Government of the Netherlands. The program aims at improving the organizational and the administrative capacities of the State Audit Office, and strengthening the audit skills, IT and IT audit, and the external communication.



Cooperation with SIGMA and the European Commission

Cooperation with SIGMA¹⁶ and the European Commission occurs within the annual evaluation missions of the functioning of the financial control in the Republic of Macedonia. Such cooperation has a positive effect over the process of advancement of the State Audit Office as a competent external audit institution in accordance with the EU requirements and the international state audit standards.

¹⁵ Program of the Ministry of Foreign Affairs of the Netherlands for social transformation aimed to support the reforms of the new EU member countries, candidate countries, potential candidate countries and the EU neighboring countries, and their institutions

¹⁶ Support to improving management and government (OECD and EU joint initiative)

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