SUBMISSION FROM THE
AUDIT REPORT ON ANNUAL FINANCIAL STATEMENTS
OF THE PHARMACY INSTITUTION OF MONTENEGRO FOR 2010

Type of review: General review
Auditee: Pharmacy Institution of Montenegro, Podgorica
Subject to audit: Annual financial report for 2010. year
Audit duration: 90 days of audit
Members of Collegium: Mr Dragiša Pešić (a member of the Senate - the head of the Collegium) and Mr Miroslav Ivanišević (President of the Senate - a member of the Collegium)
1. General information on the subject of audit

Pharmacy Institution of Montenegro was established by the Decision on the organization of public institutions in the field of health care in the Socialist Republic of Montenegro, which the Assembly of SRM adopted at its session of 15/05/1991. ("Official Journal of Montenegro", No. 21/91), as the Pharmacy Institution of Montenegro - Titograd, with the organizational units in all municipalities. The Assembly at its session of 02/08/1991 adopted the Decision on Amendments to the Decision on the organization of public institutions in the field of health care in the Republic of Montenegro ("Official Journal of Montenegro", No. 34/91), which made certain amendments of the activities of the Pharmacy Institution and defined the status of legal person of the Institution.

Activity of Pharmacy Institution is of public interest. The main activity of Pharmacy Institution was specified by the above mentioned Decision and the Statute of the Institution. Pharmacy institution does:
- Supply the population, health care institutions and companies with medicines, dietary supplements and other medicinal products and other means for prevention and treatment as well as other means for improving and maintaining health;
- Create a magistral formula and galenic preparations;
- Deal with the wholesale trade of medicines, medical supplies, medical and healthcare devices, instruments and equipment for health care;
- Provide foreign trade, including mediation and representation in trade of goods;
- Perform other tasks related to basic activity.

Director of Pharmacy Institution is Budimir Stanišić.

According to the Law on Companies PI MNE is registered on 13/08/2002 in the Central Register of the Commercial Court in Podgorica under number 8-0006764/001 as Pharmacy Institution of Montenegro.

Company headquarters is in Podgorica, Ljubljanska bb.

Persons authorized to manage funds of Pharmacy Institution, according to the specimen signature card in commercial banks with which the institution has the cooperation, the director Budimir Stanišić, Snežana Stanković and Radoman Dragaš.

Pharmacy Institution has concluded cooperation agreements with:
- Montenegrin Commercial Bank, account number 55105-603-09433414;
- Podgoricka Bank AD Podgorica, account 55105-603-0-2208;
- NLB Montenegrobank, account number 907-53001-03;
- Mortgage Bank, account number 520-8218-59.

Pharmacy Institution Statute was adopted by the Board of directors of the Institution, according to the Law on Social Services ("Official Journal of Montenegro", No.19/90) and the Decision on the organization of public institutions in the field of health care in the Socialist Republic of Montenegro of 10/02/1992. The Government of Montenegro gave its approval to this Statute of Pharmacy Institute , No. 02-4093 of 23/01/1992. Amendments to the Statute was adopted by the Board of directors of this Institution of 29/07/1999. The Government of Montenegro gave its approval on amendments of the Statute, the number 02-3097 of 29/09/1999. Since then, the Statute of Pharmacy Institute has not been altered and adjusted to the Law.
2. The accounting policies of the Company

The financial statements of Pharmacy Institute of Montenegro are in accordance with international accounting standards (IAS) and the Law on Accounting and Auditing ("Official Journal of Montenegro" No. 69/05 and "Official Journal of Montenegro", No. 80/08).

The basic principles of evaluating the balance sheet figures are the purchase price and cost price.

The revenues are related to the implementation of medicines, goods and services during the reporting period. Operating expenses comprise all expenses related to the execution of basic activity of Pharmacy Institute.

Fixed assets are shown at acquisition value less provision. If there is a significant divergence of the book value from the market value the reduction is performed to fair value through the assessment in accordance with IAS.

Stock of materials are shown at acquisition value which are comprised of net invoice value and the dependent acquisition costs.

The financial statements have been prepared on accrual basis.

3. Opinion with the review of determined statements and given recommendations

On the basis of established facts and making statements of Pharmacy Institute of Montenegro (No. 5070 of 07/09/2011.) to the Report on Audit of the State Audit Institution (no. 40113-05-38/28 of 25/07/2011.), and in accordance with Article 50 of the Rules of Procedure of the State Audit Institution, within the competent Collegium: Dragiša Pešić (a member of the Senate and the head of the Collegium) and Miroslav Ivanišević (a member of the Collegium), at the meeting held on 03/10/2011. adopted a final Report on the Audit of the annual financial statement of Pharmacy Institution of Montenegro for 2010.

The audit has established that it is not defined the legal status of Pharmacy Institution of Montenegro in accordance with the Law on health care ("Official Journal of Montenegro" 39/04 and "Official Journal of Montenegro" 14/10) and that there are a certain number of irregularities in financial accounting records and conducting of business procedures. Therefore, the competent Collegium of Audit on the subject expressed conditional positive OPINION.

1. The audit has determined that Pharmacy Institution of Montenegro in the Law on health care ("Official Journal of Montenegro" 39/04 and "Official Journal of Montenegro" 14/10), as the basic Law regulating the area of health care in Montenegro, has no defined the legal status as a public health institution.

Law on health care ("Official Journal of Montenegro" 39/04 and "Official Journal of Montenegro" 14/10) does not define the Pharmaceutical Institution of Montenegro as a form of organizing pharmaceutical
activities. According to Article 42, paragraph 1 of the Law: "Pharmacy is a health institution at the primary level of health care that performs the pharmaceutical health activity."


Decision on the network of health institutions was established that the pharmaceutical activity at the primary level of health care in Montenegro are 44 pharmacies PPI "Montefarm". With this Decision has not been defined the Pharmaceutical Institution of Montenegro as a public health institution. Public health institution called "Montefarm" is not registered in the Central Registry of the Commercial Court, although the Pharmacy Institution uses the name "Montefarm" in business activities.

- The State Audit Institution recommends the Ministry of Health of Montenegro to initiate the amendments to the Law on Health Care ("Official Journal of Montenegro" 39/04 and "Official Journal of Montenegro" 14/10) in terms of defining the status of Pharmacy Institution of Montenegro as a public health institution or to initiate the transformation procedure of Pharmacy institution so as the legal status of that Institution shall comply with the provisions of the Law on Health Care.

- The State Audit Institution recommends the Pharmaceutical Institution of Montenegro that in business shall use the registered name the Pharmaceutical Institution of Montenegro whereas the name of "Montefarm" is not recognized in the court registration of the Institution.

2. Statute of Pharmacy Institution of Montenegro was adopted in 1992 and the amendments to the Statute in 1999. Regulation on job classification of Pharmacy Institution was adopted in 1992 and the amendment to the Regulation on the job classification in 1999. Since then, the Statute and the Regulation of the job classification have not been altered and adjusted to the Law.

The bodies of Pharmacy Institution of Montenegro have been constituted in accordance with the Law on Health Care ("Official Journal of Montenegro" 39/04 and "Official Journal of Montenegro" 14/10), although that Law does not recognize the Pharmaceutical Institution as a public health institution.

Government of Montenegro applies the Law on health care in the part concerning the election of Directors and the Board of Directors, although it has not met the previous procedure provided by the Law on Health Care, Article 60, paragraph 1, which states that the number of members of the Board of Directors of health institution is determined by the Statute, depending on the type and scope of activities that the institution performs.

The provisions of the Statute of Pharmacy Institution does not reflect the actual state in the Institution concerning on defining of institution’s bodies, its names and composition of management bodies - the Board of Directors.
By the Regulation on job classification of Pharmacy Institution is envisaged the existence of 39 pharmacies and the Institution has 44 pharmacies or 5 pharmacies more than as prescribed in the Regulation.

The total amount of systematized workplaces on the level of Pharmacy Institution is 360. According to the report of the Institution, 31/12/2010 there were 317 employees on permanent and 75 temporary employees to a total of 392 employees or 32 employees more than is prescribed in the Regulation on job classification.

- **The State Audit Institution recommends Pharmaceutical Institution of Montenegro that, after resolving the legal status as a public health institutions in Montenegro in the Law on Health Care, to initiate the procedure for adoption of the new Statute of the Institution and the new Regulation on job classification of the Institutions that should in a way based on the Law resolve legal, organizational and other internal issues in the Institution.**

3. **It is determined inconsistent application of legal regulations in the Pharmaceutical Institution of Montenegro**

The Board of Directors of Pharmacy Institution of Montenegro, which the Government of Montenegro has elected in accordance with Article 61 of the Law on Health Care ("Official Journal of Montenegro" 39/04 and "Official Journal of Montenegro" 14/10) has not made a plan and program of work and development of Pharmacy Institution or the annual financial plan of Pharmacy Institution for 20100, although it has the obligation according to Article 62 of the Law on Health Care.

- **The Board of Directors of Pharmacy Institution of Montenegro should ensure full implementation of Article 62 of the Law on Health Care ("Official Journal of Montenegro" 39/04 and "Official Journal of Montenegro" 14/10) and to adopt the plan and program of work of Pharmacy Institution and annual financial plan of Institution.**

4. **The share capital of Pharmacy Institution of Montenegro, which is 2.560 million euros has decreased by 1.194 million euros or 47% due to continuing negative business results of the Institution.**

Business revenues of Pharmacy Institution in 2010 were 41.504 million euros and are comprised of:
- Revenues of the Health Insurance Fund of Montenegro, which realizes on the basis of issued prescribed medicines to the insured persons in the amount of 13.665 million euros.
- Revenues from public health institutions in Montenegro, releasing of medicines from wholesalers, which also pays the Health Insurance Fund of Montenegro in the amount of 20.347 million euros.
- Revenues from sales of goods (pharmaceuticals and parapharmaceuticals) to citizens in the amount of 5.271 million euros.
- Other revenues and revenues from services rendered in the amount of 2.221 million euros.

Business expenses of Pharmacy Institution in 2010 were 41.957 million euros. Within business expenses, Health insurance fund was remitted to Pharmacy Institution the amount of 4.113 million euros for salaries and other personal income in 2010.

Business loss in 2010 was realized in the amount of 453 thousand euros.
The State Audit Institution recommends the Government of Montenegro, as the majority owner of Pharmacy Institution of Montenegro, to analyze the current status of the Institution and consider the need to cover the business loss through the capital increase or privatization due to the decrease of the part of share capital.

5. The audit has determined that the financial-accounting records in certain cases are not updated

The Board of Directors of Pharmacy Institution of Montenegro adopted the Decision No. 1085 of 28/02/2011 adopting the annual report of the Institution for 2010. Total revenues to above mentioned decision were presented in the amount of 41.340 million euros, and in the books are 41.603 million euros. Total expenses were presented in the amount of 40.949 million euros instead of 41.944 million euros.

In relation to the initial state of operating statement of Pharmacy Institution for 2010, the audit determined that is necessary to:

- Carry out the reclassification of the amount of 44 thousand euros from positions other business revenues to the item revenues from the performed services regarding that the position of discounts and returns related to income from the regular, primary business.

- In relation to the initial state of the positions the business expenses in the amount of 41.964 million euros carry out the reclassification in a way that 7 thousand euros transfer to item expenses of interest costs from the item other business expenses.

- In relation to the initial state of the position salaries and other personal income of 4.088 million euros carry out the reclassification in a way that 25 thousand euros related to representational expenses transfer from positions other business revenues because representational expenses belong to expenses for salaries and other personal income.

The position of salaries and other personal income is necessary to adjust in the operating statement of Pharmacy Institution for 2009. The amount of 615 thousand euros that make the cost of employer contributions was transfer to other business expenses, so that the position of salaries and other personal income decreased from 4.766 million euros to 4.151 million euros and other business expenses were increased from 669 thousand euros to 1.284 million euros.

For the amount of 4.9 thousand euros based on the invoices for spent electricity in 2009 were overestimated the costs for 2010 which reflected to an increase in negative financial result in 2010.

For the amount of 18 thousand euros were underestimated representational expenses and overestimated expenses of overhead costs of material. That amount refers to medicines that were given free of charge as a sponsorship.

On the position of abonnement on foreign and domestic suppliers was recorded the amount of 54 thousand euros to WHC "Buducnost", which refers to the earlier periods and which should be booked out as expenses in 2010.

On the position of responsibilities to suppliers it was determined the inconsistency in the business records of Pharmacy Institution and of two suppliers. At one supplier was registered that the responsibility of
Pharmacy Institution higher than in the business records of the Institution for 155 thousand euros and at the other supplier was registered that the responsibility of Pharmacy Institution higher than in business records of Pharmacy Institution for the amount of 86 thousand euros. For the amount of 241 thousand euros were underestimated responsibilities in 2010. Responsibilities were in the records of Pharmacy Institution were entered up in 2011.

On the position of accepted prepayments it was determined that the amount of 65 thousand euros emerged in the past. It consists of responsibilities of Pharmacy Institution to Military posts 6965 Podgorica. It should be credited to income in 2010.

On the position of accepted prepayments it was determined that the responsibility was not entered up well of Pharmacy Institution to the Ministry of Health of Montenegro on the basis of payment of 164 thousand euros for the procurement of Tamiflu capsules. With regard to non-repayable assets for the value of the part of spent capsules it should reduce inventories and increase costs and for the same amount it should decrease responsibilities to the Ministry of Health and increase the revenue.

➢ The State Audit Institution recommends Pharmacy Institution of Montenegro to carry out the proposed adjustments in their accounting records and that in future business due care dedicates to keep accounting records updated.

6. Pharmacy Institution of Montenegro has not registered a building structure, Administrative building and facility wholesale at Real estate administration of Montenegro, since the facility was built on land owned by the Health Insurance Fund of Montenegro, which now challenges the registration and defining of ownership on the land of the area of 6 800 m². The said land, the Fund has given on usage to Pharmacy Institution of the period of 10 years. Building permits of the facility is issued to Pharmacy Institution.

➢ The State Audit Institution recommends the Ministry of Health, Health Insurance Fund of Montenegro and the Pharmacy Institution of Montenegro to accelerate the actions and procedures necessary for resolving issues of land ownership in terms of providing registration of Administrative building and warehouse building-wholesalers in the real estate cadastre at Real estate administration of Montenegro.

7. In the procedure of implementation of public procurement during 2009 and 2010 there were some failures in implementing the procedures stipulated by the Law on Public Procurement ("Official Journal" No. 46/06).

- Pharmacy Institution of Montenegro was not adopted the annual financial plan for 2009 which should have served as the basis for the procurement plan for 2009.

- The annual plan of medicines procurement for 2009 was not submitted for inspection, which the Ministry of Health of Montenegro was obliged to adopt according to the provisions of the Law on health care and which should serve as the basis for the implementation of the open procedure of public procurement of medicines and medical supplies ("Official Journal of Montenegro" No .39/04 and " Official Journal of Montenegro "14/10).
The Pharmacy Institution was submitted to the Public Procurement Directorate the public procurement plan for 2009 which was filed on 30/12/2008 under number 6828, in the total amount of 26.695 million euros.

Public Procurement Plan for 2009 (in thousand euros)

<table>
<thead>
<tr>
<th>Position</th>
<th>Amount</th>
<th>Position</th>
<th>Amount</th>
</tr>
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<tbody>
<tr>
<td>Goods</td>
<td>26 370</td>
<td>Expenses for materials</td>
<td>26 675</td>
</tr>
<tr>
<td>Works</td>
<td>295</td>
<td>Expenses for Services</td>
<td>80</td>
</tr>
<tr>
<td>Services</td>
<td>30</td>
<td>Capital Expenses</td>
<td>70</td>
</tr>
<tr>
<td>TOTAL</td>
<td>26.695</td>
<td>TOTAL</td>
<td>26.825</td>
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The total value for goods, works and services was planned in the amount of 26.695 million euros, while expenses for materials, services and capital expenses were 26.825 million euros. There was a mistake in the classification of the planned values of the individual types and values of costs, so that there is a conflict of individual expenses and total amount.

After the conclusion that there is disagreement of the public procurement plan, submitted to the Public Procurement Directorate, it was submitted the other plan of public procurement filed on 29/12/2008 under number 6879, which was not filed by the Public Procurement Directorate.

Public Procurement Plan for 2009

<table>
<thead>
<tr>
<th>Position</th>
<th>Amount</th>
<th>Position</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goods</td>
<td>26 405</td>
<td>Expenses for materials</td>
<td>26 405</td>
</tr>
<tr>
<td>Works</td>
<td>315</td>
<td>Expenses for Services</td>
<td>30</td>
</tr>
<tr>
<td>Services</td>
<td>30</td>
<td>Capital Expenses</td>
<td>315</td>
</tr>
<tr>
<td>TOTAL</td>
<td>26 750</td>
<td>TOTAL</td>
<td>26 750</td>
</tr>
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</table>

According to that plan it was envisaged the procurement in the total amount of 26.750 million euros.

- The Pharmacy Institution has not submitted to the Public Procurement Directorate of Montenegro proper report on awarded public procurement for 2009, No. 1515 of 24/03/2010, because the contracted values for the public invitation 03/09 were given based on the Decision on award of contract No. 4689 of 07/08/2009 in the amount of 23.171 million euros and were not adjusted based on the Decision on amending of decision on award of contract number 5165 of 03/09/2009, in the amount of 22.483 million euros, which is contrary to the Law on Public Procurement, Article 84.

- The Pharmacy Institution has submitted incorrect public procurement plan for 2010, to the Public Procurement Directorate, the sum of the first column is 34.130 million euros and the other is 34.216 million euros.
Public Procurement Plan for 2010 (in thousands of euros)

<table>
<thead>
<tr>
<th>Position</th>
<th>Amount</th>
<th>Position</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goods</td>
<td>34 000</td>
<td>Expenses for materials</td>
<td>34 086</td>
</tr>
<tr>
<td>Works</td>
<td>70</td>
<td>Expenses for Services</td>
<td>60</td>
</tr>
<tr>
<td>Services</td>
<td>60</td>
<td>Capital Expenses</td>
<td>715</td>
</tr>
<tr>
<td>TOTAL</td>
<td>34 130</td>
<td>TOTAL</td>
<td>34 216</td>
</tr>
</tbody>
</table>

- Public Procurement Plan for 2010 was determined without financial plan of Pharmacy Institution for 2010. The Ministry of Health has adopted an annual plan for medicine procurement for 2010 in July of 2010.

- The total planned amount for the goods procurement through open competitive procurement in 2010 was 23.086 million euros, while the contracted amount was 18.628 million euros and for services the planned amount was 24 thousand euros and the contracted amount was 14.24 thousand euros. The estimation of public procurement value of was planned in significantly larger amounts in relation to the contracted value which is not in accordance with the Law on Public Procurement, Article 32.

- The Pharmacy Institution was conducted in 2009 the procurement of commercial goods worth 4.006 million euros and in 2010 the procurement of commercial goods worth 4.323 million euros without the implementation of the procedure of public procurement, by concluding commercial (purchase) and commissioning contracts.

- The Ministry of Health of Montenegro, in accordance with Article 9 of the Law on Health Care ("Official Journal of Montenegro" 39/04 and " Official Journal of Montenegro" 14/10), is obliged to determine the annual plan for the needs of medicines, medical devices and equipment, in terms that will enable Pharmacy Institution of Montenegro that, according to the Law on Public Procurement ("Official Journal of Montenegro " No. 46/06 or " Official Journal of Montenegro ", No. 42/11) to adopt the plan for public procurement for current year.

- The Pharmacy Institution of Montenegro is obliged to adopt an annual financial plan which should serve as a base for adopting the annual procurement plan.

- The Pharmacy Institution of Montenegro is obliged to keep the record updated related to the process of planning, implementation and reporting of the procedure of public procurement.

- The Pharmacy Institution of Montenegro should ensure full implementation of Article 2 of the Law on Public Procurement ("Official Journal of Montenegro " No. 46/06 or " Official Journal of Montenegro ", No. 42/11) in the part of medicines procurement and other pharmaceutical and para pharmaceutical and goods in a way that these procurements are done through an open competitive procurement, except in the part of the business through commission contract.
The Pharmacy Institution is obliged to take care of adequate assessment of the value of public procurement, and in this regard to undertake the research of market suppliers, in order to avoid significant differences between the estimated and realized value of public procurement.

8. In the process of implementation of public procurement during 2009 and 2010 there were some failures during the implementation of the procedure stipulated by the Law on Public Procurement ("Official Journal of Montenegro" No. 46/06) for individual public procurement procedures.

- The procurement of stationary, No. 02/09. The contract for delivery of stationary No. 2769/09, does not contain the price which is contrary to the Law on Obligations, Article 470. Price is defined in the annex of the contract in the amount of 23.53 thousand euros.

- The procurement of medicines, medical devices and pharmaceutical chemicals for the needs of public health institutions in Montenegro, whose founder is the Republic, No. 03/09.

- After conducted procedure of public procurement the decision was adopted on the award of the contract No. 4689 of 07/08/2009 which the highest bidder is awarded the contract for underlying public procurement in the total amount of 67 639 euros. The contract was submitted to the bidder for signature, but until the day of audit it was not signed with that bidder, which is contrary to Article 74 of the Law on Public Procurement.

- The Record of the re-examination, evaluation and comparison of bids and Report on the re-procurement process, were not submitted to inspection, after the Commission for the control on public procurement procedure adopted the Decision No. 5903 of 12/10/2009 by which was adopted the appeal of an stakeholder and annulled the Decision of awarding the contract number 4689 of 07/08/2009 to the highest bidder, which is contrary to Article 101 of the Law on Public Procurement. There were submitted two decisions of amending the decision to award the contract no. 4689 of 07/08/2009. By the first Decision, number 5165 of 03/09/2009 the highest bidder was awarded the contract for the underlying public procurement worth 421.84 thousand euros. The second Decision, number 5218 of 04/09/2009 contains the list of bidders who offered the highest bids. With that supplier was signed the Contract on the amount of 421.84 thousand euros, number 5184 of 04/09/2009 by the Pharmacy Institution.

- The procurement of stationary No. 02/10. The Contract for delivery of the stationary number 2262/10 which was concluded with the highest bidder does not include the price. The price is defined in the Annex of the contract in the amount of 28.38 thousand euros.

The Pharmacy Institution of Montenegro is obliged to consistently appreciate the process of planning, implementation of the procedure of open public procurement and making of the Contract with the highest bidders according to the Law on Public Procurement ("Official Journal of Montenegro" No. 46/06 or "Official Journal of Montenegro", No. 42/11) and Article 470 of the Law on Obligations ("Official Journal of Montenegro" No. 47/08 and 04/11).
9. The procedure of public procurement for the selection of the highest bid for procurement of medicines, medical devices and pharmaceutical chemicals for the needs of Public health institutions in Montenegro, founded by the Republic for 2010 number 05/10 is not completed in 2010 but the Decision on the award of Contract was adopted and registered under number 324 of 24/01/2011.

- The State Audit Institution recommends the Ministry of Health, Health Insurance Fund of Montenegro, the Public Procurement Directorate and the Pharmacy Institution of Montenegro to review the current decisions of the Law on Public Procurement ("Official Journal of Montenegro" No. 46/06 or "Official Journal of Montenegro", No. 42/11) related to the process of the procurement of medicines from the positive list and to give recommendations for specific legal definition for the procurement of medicines and other medical supplies, if such specificity shall be determined.

- The State Audit Institution recommends Pharmacy Institution of Montenegro that during planning of the process of public procurements takes into consideration the total time necessary for the implementation of an open public procurement process (preparation of documents, advertising, collecting and evaluating bids, procurement contracting and appeals process for each of these procedural actions) and the risk factor that occurs due to the announcement of a single public procurement procedure for the total amount of medicines, medical devices and pharmaceutical chemicals for the needs of Public health institutions in Montenegro, founded by the Republic, so as the open public procurement procedure could be implemented in the same year.