



**Report of the Auditor General on the Financial
Statements of the Turks & Caicos Islands
Government as at, and for the year ended, 31st
March, 2014.**

Date of Audit Report: 17 February, 2015.

Anand Heeraman - Auditor General

Contents

Contents.....	2
Tables listing	3
Abbreviations Listing.....	4
1. Auditor General's Message	6
2. Brief High level Risk & Controls Review.....	8
3. EXECUTIVE SUMMARY.....	10
4. REVENUE.....	19
4.1 Potential revenue loss of \$5 - \$10 million annually - HR	19
4.2 Millions in revenue arrears to be validated, corrected, collected or recommended for write off - HR	19
4.3 Revenue arrears not accounted for on the statement of financial position - HR	20
4.4 Inadequate management of concessions granted (\$78.7M for the 3 years to March 31, 2014) - HR.....	21
4.5 Non-recording or non-recognition of \$2.915 million of stamp duty foregone - HR	22
4.6 Lease commitments and incentives not disclosed – HR	23
4.7 \$934K net repatriation deposits treated as revenue upon receipt instead of a liability – HR.....	23
4.8 Unregistered private lodgings possibly not paying Hotel and Restaurant Tax – HR	23
4.9 Revenue Control Unit did not subject tourism lodgings and restaurants to annual audit – HR	24
4.10 No systematic compliance checks for compliance with business licensing requirements – HR.....	24
4.11 No annual compliance checks for compliance with the Immigration Ordinance - MR.....	25
4.12 Significant number of custom tariffs can lead to possible tariff shopping by importers – MR.....	25
5. EXPENDITURE	26
5.1 Significant increase in IT costs from \$1.7M to \$3.5M and a \$6M contingent liability - HR	26
5.2 Netting of hospital revenues with hospital expenditures - HR	27
5.3 Consolidated healthcare related costs approximate \$64M (split between TCIG and NHIB) - HR.....	28
5.4 Several repeat audit findings impacting approximately \$21.2M in expenditure – LR to HR	29
5.5 Several control exceptions and repeat audit findings in Development Fund expenditure – HR	30
5.6 Lack of supporting documentation for \$6.6M in journals – HR	30
5.7 Bulk Ticket higher by \$154K compared to on-demand prices - HR.....	30
5.8 Poor vendor master file management – HR.....	30
5.9 IT Control Issues – HR.....	32
5.10 Excess Expenditure – MR	32
5.11 Expenditure arrears management – MR.....	34
6. ASSETS.....	36
6.1 Assets reported at higher than their likely recoverable amount - HR	36
6.2 Significant assets with an estimated value of \$50M not recorded in financials - HR	37
6.3 \$2.5M Belize Bank / British Caribbean Bank (BCB) account not clarified – HR.....	38
6.4 Prior Year Adjustments of \$5.8M between 2011-2014 not properly accounted for – HR.....	39
6.5 TC Invest loans not properly reflected in TCIG's Financial Statements - HR	40
6.6 No proper due diligence or tendering procedures followed in relation to non-performing loans – HR ...	41
6.7 Inconsistency in inventory values by \$1.1M – HR.....	43
6.8 Losses not managed in compliance with regulations – HR	44
6.9 \$1.2M outstanding checks not cleared by Nov 2014 – HR	44
6.10 Stamp duty receivables not recorded – HR.....	45

6.11	Staff loans not managed in compliance with the PFMR – MR	45
6.12	Travel advances not managed in compliance with the PFMR – MR	46
7.	LIABILITIES.....	49
7.1	Consolidated financial statements are mandatory under IPSAS 6 or IPSAS cash basis - HR.....	49
7.2	Proper accounting treatment required for the \$116M Hospital PPP - HR.....	50
7.3	Inadequate contract management of health costs – HR	52
7.4	Inadequate Treasury management – HR	52
7.5	Unfunded Actuarial Valuation of \$84.8M – HR.....	53
7.6	Determination of creditors and timing of payments - HR.....	53
7.7	Insufficient audit evidence – HR	54
7.8	Unrecognised accrued interest payable – MR	54
8.	DISCLOSURES.....	56
8.1	Non-compliance with Generally Accepted Accounting Practice – HR	56
8.2	Inadequate Basis of Accounting – HR	57
8.3	Risk of bad debts increases and non-approval of write-offs - HR	58
8.4	Large number of issues presented in TCIG’s financial statements – LR-HR	58
8.5	Inconsistency in the application of the basis of accounting – HR	59
8.6	Non-transparent economic value transactions not recorded – HR	60
8.7	Lack of disclosure of related party transactions – HR.....	61
8.8	Inadequate system to deal with third party payments and in-kind services – HR.....	62
8.9	Treatment of shareholding in Provo Water Company Limited – HR.....	63
8.10	Material changes made between both drafts of the financial statements submitted – HR.....	64
9.	Sensitivity Analysis on Key Risk Areas.....	66
10.	NAO MANDATE & OBJECTIVES.....	67
11.	NAO ACTIVITIES AND CHALLENGES.....	68
12.	LIMITATIONS	74
13.	Key Definitions	75
14.	DETAILED AUDIT ISSUES AND EXPLANATIONS.....	78

Tables listing

Table 1 - High Level Risk & Controls Review	8
Table 2 - Scholarship contributions reported by the ministry	19
Table 3 - Business Licence Arrears within the last 5 years	20
Table 4 – Number of Entities receiving concessions in the three years to March 31, 2014.....	21
Table 5 – Co-payments and 50% Third Party Revenues deducted from amounts due to ClinCo.....	27
Table 6 – TCIG and NHIB health related costs for the years ended March 31, 2014 and 2013.....	28
Table 7 – Excess expenditure per line item	32
Table 8 - Excess expenditure per department.....	33
Table 9 - Expenditure Arrears	34
Table 10 – Total expenditure and expenditure arrears summary	34
Table 11 – Extract of some transactions from the Belize Bank Account	38
Table 12 - Prior year adjustments.....	39

Table 13 – TC Invest Mar 2010 Audited Fin. Stats. vs. Sept. 2012 TC Invest unaudited Fin. Stats.	40
Table 14 - Non performing loans sold	42
Table 15 – Difference between Statement of Unallocated Stores and Board of Survey information.....	44
Table 16 - Travel claims retired compared to not retired	46
Table 17 – Comparison of reported hospital project costs between 2012/13 and 2013/14	51
Table 18 - Number of related party transactions between TCIG and Statutory Bodies	61
Table 19 - Sensitivity Analysis on key risks areas.....	66

Abbreviations Listing

Accruals Basis of Accounting	ABoA
Automated System for Customs Data	ASYCUDA
Association of Chartered Certified Accountants	ACCA
Caribbean Development Bank	CDB
Cash Basis of Accounting	CBoA
Certified General Accountant	CGA
Daily Subsistence Allowance	DSA
Department for Business Information & Skills	BIS
Department for International Development	DFID
European Union	EU
Fiscal and Strategy Policy Statement	FSPS
Foreign Commonwealth Office	FCO
Generally Accepted Accounting Practice	GAAP
Information Technology	IT
InterHealth Canada	IHC
Interactive Data Extraction Analysis	IDEA
International Education Standards	IES
International Federation of Accountants	IFAC
International Financial Reporting Standards	IFRS
International Public Sector Accounting Standards	IPSAS
International Standards on Auditing	ISA
International Standards of Supreme Audit Institutions	ISSAI
Modified Cash Basis of Accounting	MCBoA
Ministry of Defence	MOD
National Audit Office	NAO
National Health Insurance Board	NHIB
National Insurance Board	NIB
Other Comprehensive Basis of Accounting	OCBoA
Payment Voucher	PV
Public Accounts Committee	PAC
Public Finance Initiative	PFI
Public Financial Management	PFM
Public Finance Management Ordinance	PFMO
Public Finance Management Regulations	PFMR
Public Private Partnership	PPP
Public Procurement Ordinance	PPO
Public Works Department	PWD

SmartStream
 Southern Health Network
 Standard Integrated Government Tax Administration System
 Strategic Policy & Planning Department
 The Outstanding Loan Company Limited
 Turks and Caicos Islands Government
 Turks and Caicos Islands
 United Kingdom (UK) Border Agency
 Value for Money

SS
 SHN
 SIGTAS
 SPPD
 TOLCO
 TCIG
 TCI
 UKBA
 VFM

M - Million

K - Thousand

\$ - United States Dollar

Risk Rank

Entity Overall Risk			
10-25	High (HR)	Manage risk utilizing prevention and/or mitigation with highest priority. Promote issue to those charged with governance with commensurate risk assessment detail. Intolerable/Unacceptable.	1
4-9.99	Moderate(MR)	Manage risk utilizing prevention and/or mitigation with priority. Promote issue to those charged with governance with commensurate risk assessment detail. Incorporate risk reduction measures.	2
1-3.99	Low (LR)	No mitigation required where controls can be verified as functional. Manage for continuous improvement.	3

1. Auditor General's Message

This has been another challenging year for the NAO to complete a comprehensive audit of the public accounts of TCIG, as originally submitted on 31 July, 2014, then subsequently revised on 15 January, 2015 and further revised on 30 January, 2015 (not yet received as at 15 February, 2014). The majority of findings in this report reference the accounts submitted on 31 July, 2014. While there were some references to the later revisions they could not be fully validated and audited in the timeframe leading to a limitation in scope. The findings in this audit report are many and are derived from the detailed emerging issues, responses, evidence and other information either provided by the auditee or discovered during the course of this audit. ***Findings were provided to TCIG throughout the audit process via informed meetings, communication up to and including 15 February, 2015, some of which were acted upon resulting in revisions to the financial statements.*** For others management responses were not received in time or could not be collated given the revised timelines. Please see Section 3 for the Executive Summary which would give a high level overview of this audit.

I would like to extend my sincerest appreciation to all those who participated in this audit.

There is no question that TCIG is on a sound financial footing and the general economic outlook is positive. The sovereign credit rating of BBB+, from Standard and Poors, is certainly positive indicating that TCIG has adequate capacity to meet financial commitments, but is vulnerable to adverse conditions. The fundamentals are in place. Compared to many of its Caribbean neighbours, TCI should be proud to have passed into legislation, what are viewed by many, as precedent-setting financial laws and regulations. However, the public financial management laws and regulations by themselves are meaningless if they are not complied with and/or not properly supported by strong underlying systems and controls. Credit rating outlooks can change in an instant. While one cannot control what the next external shock to impact TCI's economy will be, or when, there are certain areas that TCIG can control and which it should therefore concentrate on.

In trying to build a transparent and publicly accountable architecture, there has been a genuine effort by many accounting officers to strengthen management of public finances despite very limited human and financial resources for many years. There are challenges in finding an optimum balance between expert resources, staff development and achieving department objectives. Legislation has increased extensively which dramatically increases the demands on officers while staff complement has been very limited for some departments and almost crippling for others. Accordingly, there is a large gap between the intention of the financial laws and their implementation. The financial laws and regulations are not being fully implemented or adhered to.

Cash revenue recording appears to be adequate but all revenues legally due are not being collected. The risk of loss of revenues is therefore high. Expenditure control and compliance is improving in the smaller departments but remains weak in some of the larger ones. Accounting Officers should be commended for the significant reduction in excess expenditure over the last reporting period and the risk has

moderated in this respect. Accounting for, and reporting of, economic value transactions and events are not in compliance with generally accepted accounting practice (GAAP), the required basis of preparation per the PFMO. Economic value foregone is not monitored which can result in economic loss to TCI. Procurement risk is moderate but contract management risk is high. The cash basis of accounting used is inadequate as it does not capture many highly material non-cash economic events. High value fixed assets are not recorded in the financial statements while some of the assets that are recorded are overstated and need to be written off. Liabilities are seemingly recorded on a discretionary basis, while others are only partially recorded. Contingent liabilities are not accurately reflected in the financial statements. Treasury management requires some attention. Adjustments to prior years reported balances are incorrectly accounted for. Revenue arrears reporting appear to be deficient. Financial statement disclosures are improving but there is still much work to be done to ensure that they are accurate and reliable. Consolidation of all government entities, including the statutory bodies, is not done making it very difficult to obtain an overall economic and financial picture. Accounting treatment is arbitrary and discretionary, limiting transparency and increasing financial risk exposure. Value for money risk remains high. Compliance risk is high and controls are weak. Consequently the risk of economic and financial loss is high and fraud risk remains in the high range. With the strengthening of processes, high risks should be mitigated. Overall, financial governance risk is high and significant improvement is required. *The task ahead should therefore be to bridge the gap between the intention of the public financial management laws and regulations and their implementation. This demands an enhanced public service, compliance with financial laws and regulations, implementing effective processes and adopting, in compliance with, recognised rules-based accounting. This will reduce the risk of errors, omissions, fraud, abuse, wastage, undue influence and consequently improve value for money.*

A fundamental requirement is to ensure that the financial position and performance of TCIG is fully disclosed to the House of Assembly with the crucial objective being protection of the public purse. The intention of this Audit Report is to highlight vital issues to the House of Assembly in order that they may adopt many of the recommendations or take decisive action intended to improve processes and ensure public funds are prudently managed ultimately resulting in benefits to TCIG.

The financial statements as at, and for the year ended, March 31, 2014 are disclaimed. Further, I provide no assurance on the revisions made to the financial statements that were not able to be audited. However, with improvements in specific areas, I anticipate that TCIG should be able to strengthen its financial governance and improve transparency of its reporting processes in order to achieve an improved audit report in the next cycle (2015/16 or earlier), provided that recommendations are accepted and dealt with expeditiously.



Anand Heeraman FCCA, CFE Auditor General – 17 February 2015

2. Brief High level Risk & Controls Review

Table 1 is a high level assessment of identified risk areas examined over the last two audits, together with general comments on the issues and suggested actions on how to address them.

Table 1 - High Level Risk & Controls Review

	Risk Areas	2012/13	2013/14	Comments	Moving forward
1	Financial Laws & Regulations (FL&Rs) Compliance	FL&Rs are strong but not fully implemented or complied with	FL&Rs are strong but not fully implemented or complied with	Gap between law and its intention and implementation. FL&Rs are useless if not enforced, adhered to or implemented	Close gap between intention of laws and their implementation
2	Controls, Process, Systems	Weak	Weak but improving in specific areas	Activity level controls need to be built around the FL&Rs	Continue to strengthen processes
3	GAAP	Not compliant	Not compliant, but improving, however major issues still present	Arbitrary and discretionary accounting leaves room for abuse, undue influence, fraud and performance risks	Need to comply with GAAP. Required per the PFMO
4	Cash Revenue Transactions	Adequate recording, but based on entities opting to pay, NOT enforcement. Under reporting is a risk	Adequate recording, but based on persons opting to pay, NOT enforcement. Under reporting is a risk	Improve enforcement and compliance measure	Adequate but needs improvement. Proper validation is needed for cash revenue receipts
5	Basis of Accounting	Cash or Modified Cash - Inadequate	Cash or Modified Cash - Inadequate	Need to report in accordance with GAAP and TCI FL&Rs	The fundamental principle of true and fair view should guide the accounting decisions
6	Economic Events, obligations, major contracts, concessions, subsidies etc.	Not properly monitored, assessed, or recorded	Not properly monitored, assessed, or recorded	Need to significantly improve	Establish effective processes around economic events etc.
7	Tendering Process	Strong	Reduced to adequate. Some weaknesses exist	Watch for working around the controls, poor scoping, fast executions of contracts prior to major events, influence, abuse, poor contract management and over-expenditure	Monitor
8	Contracts Management	Inadequate	Inadequate	More expertise needed	Institute proper contracts management system to ensure transparency
9	Transparency	Limited	Improved. Greater independence encouraged in activities of TCIG and Governance Institutions	There is some level of resistance to change but this is reducing due to improved high level oversight	Allocate sufficient resources in areas that need it so that they can carry out their mandate including the governance bodies

	Risk Areas	2012/13	2013/14	Comments	Moving forward
10	Fraud (corruption, financial misstatement, misappropriation of assets)	Risk of fraud high	Risk of fraud high	As laws are not enforced, controls are not adhered to. As GAAP is not complied with, the risk of fraud increases	Focus on improving processes, systems and providing resources to key institutions, including governance institutions, to reduce this risk. Budgetary resources have been increased for 2015/16 for the NAO
11	Revenue Arrears	Revenue collection and arrears cannot be assured	Revenue collection and arrears cannot be assured	Caused by weak controls, non-compliance with GAAP. Needs to be improved significantly. Millions outstanding not policed. Write-offs should be presented to House of Assembly	Include arrears in the balance sheet for better control. Coordination needed between Revenue and Treasury. All write offs to be presented to House of Assembly
12	Expenditure	High risk, weak controls, high excess expenditure	Moderate risk, improving controls, excess expenditure greatly reduced	Many repeat audit findings at moderate level, but high risk due to repeat findings	Have internal audit do quarterly checks on controls. Capture and correct early
13	Assets	High risk, weak controls	High risk, weak controls	Need to comply with GAAP. Cannot be fully relied upon	Need to value assets and include in balance sheet. Provide for, then write off, unrecoverable assets
14	Liabilities	High risk, weak controls	High risk, weak controls	Need to comply with GAAP. Cannot be fully relied upon	All liabilities should be included on statement of financial position. Some discretionary amounts included as liabilities while others omitted
15	Contingent Liabilities	High risk, weak controls	High risk, weak controls	Need to comply with GAAP. Seemingly arbitrary basis as to what is and isn't included. Certain amounts may not be contingent. No year on year comparisons	Proper classification needed between what are liabilities, commitments and contingent liabilities
16	Disclosures	High risk, weak controls	High risk, slowly improving controls	Level of data provided is improving but weaknesses remain due to non-compliance with GAAP, weak controls, arbitrary & discretionary accounting treatments	Comply with GAAP
17	Implementation of Audit Recommendations	Weak	Improving in some small departments, remains weak in some large departments	Some recommendations were incorporated into the revised financial statements but still not adequate	Engage Internal Audit to assist in implementation
18	Value for Money	High Risk	High Risk	Enhancements needed to see improved results on the VFM side	NAO to increase attention in this area provided appropriate staff are recruited or audit firms are retained

3. EXECUTIVE SUMMARY

The financial statements as at, and for the year ended, March 31, 2014 have been disclaimed due to a substantial number of material and pervasive issues identified during the audit as further detailed in the body of this report. When considering the cumulative effect of these findings on the TCIG financial statements, as presented, is very significant. There were over 200 individual findings and recommendations which were collapsed into specific areas, included in this audit report and the supplemental detailed report, which it is hoped would be acted upon within the upcoming period.

Below are the highlights:

Revenue

The controls over cash revenue recording appear to be adequate, however, there is a high risk that TCIG may not be collecting all revenues to which it is legally due. Compliance and enforcement is weak. Resources must be increased in the area of collection of revenues to ensure appropriate compliance and enforcement activities, while at the same time maintaining successful growth and investment initiatives. There is difficulty in adequately estimating the revenue shortfall because of a lack of information, however, this could range between \$5M - \$10M annually.

There are millions reported as revenue arrears, for example scholarship fund contributions (\$19M) and business licence arrears (\$38M), which need to be validated for errors and omissions in a timely manner, the legitimate amounts collected and the remainder recommended to the House of Assembly for write off where sufficiently justified.

Over the last 3 years concessions granted by TCIG were \$79M, most of which were not properly monitored and quite possibly led to a loss in economic value. It was also discovered that \$4M in stamp duty arrears, relating to a single property sale, was not recorded as a receivable at March 31, 2013, of which \$3M was then forgiven via a Stamp Duty Remission Order which was also not recorded until identified by the NAO.

Leases granted, by way of licence or other means, should be disclosed and recorded in the financial statements in accordance with GAAP. TCIG needs to ensure that economic values given, in the form of concessions, subsidies and preferential leasing rates on land, meet minimum transparency requirements and are properly tracked as these are high risk areas.

There were \$934K of net deposits received for work permits recorded as cash revenues received when these should have been recorded as a liability (deposit advances for work permits).

Expenditures

While there was a noted and commendable significant reduction in excess expenditure, there still remained several expenditure control exceptions and repeat audit findings. There have also been control improvements in some of the smaller departments, however, weaknesses still exist in the larger departments and ministries where the repeated audit exceptions were present. Approximately \$21.2M of expenditure was impacted by these exceptions. Risks still remain in some other related areas such as probable under-statement of expenditure, expenditure management, and proper virement procedures.

Healthcare expenditures are currently split between TCIG and NHIB and, as a result of non-consolidation, the total costs are not properly presented to the public. NHIB paid to IHC, on behalf of TCIG, an additional \$4M over the amount granted by TCIG to NHIB which increases the reported total healthcare costs. It has also been established that hospital revenues have been netted against hospital expenditures (approximate average of \$500K - \$680K annually) and that NHIB has other healthcare costs, such as overseas treatments, totalling \$14M in the year ended March 31, 2014. The consolidated healthcare costs for 2013/14 are approximately \$64M which includes infrastructure payments. The management of the contract has been very weak but, it appears that efforts are being made to improve contract management generally.

There were other issues, including journals recorded of \$6.6M which did not have proper supporting documentation to assure the NAO that these were appropriately reported, either poor contract management or poor scoping of contracts identified in relation to an information technology services contract which increased from \$1.7M to approximately \$9.5M and bulk domestic airline ticket prices were approximately 75% higher compared to on-demand prices, potentially costing TCIG an additional \$154K.

Assets

The assets presented on the statement of financial position are, in many cases, reported at carrying values significantly above their likely recoverable amounts. While there are certain protocols for writing off amounts due to TCIG no protocols were identified preventing such assets being provided for in the financial statements, prior to write-off. Furthermore, there are very significant assets not presented on the statement of financial position due to the accounting basis adopted. The assets presented are not, therefore, considered to be an accurate representation of TCIG's asset position. In addition, by not presenting all assets on the statement of financial position the legal requirements for write-offs to be presented to the House of Assembly may be inadvertently by-passed.

A rough estimate of \$50M, possibly more, in fixed assets, investment property, intangible assets and infrastructure improvements, is not currently recorded in the statement of financial position. This could have a positive lift to the asset side of the balance sheet. There are approximately 169 TCIG owned buildings which have not been valued, of which a few have possibly been sold off at below market value however, due to the current lack of reporting, no one can ascertain what they were bought for, if they were sold at a profit, or at a preferential price, and whether there was a suitable procedure to support this type of transaction. There are also major infrastructure improvement costs and the purchase from NIB of the NJS Francis Building for \$5.9M together with the associated furniture and fixtures for \$385K, which have all been expensed as incurred as opposed to recorded as assets.

The balances brought in to TCIG's accounting records relating to loan receivables transferred from TC Invest did not include the associated accrued interest. A detailed review is required concerning the accounting treatment and valuation of these loans. An additional examination is also required into the treatment of the non-performing loans sold to TOLCO together with an assessment of their recoverability. A special audit was conducted by the Auditor General into the circumstances surrounding the sale to TOLCO of certain non-performing loans of \$7.7M in exchange for 40% of the loan principal recoveries TOLCO realizes. The audit identified there was insufficient due diligence performed on the principals behind TOLCO along with an inadequate tender process. Greater attention should have been paid given the material amounts being sold off at a significant discount. This matter warrants a further examination.

The \$2.5M write-off of the Belize Bank/British Caribbean Bank deposit balance is still not clear. Approximately \$86M in journals were entered in order to remove this bank balance. However, I am not yet satisfied that this amount should have been written off as not enough information has been provided to date to support the write-off. All journals should be reversed and the \$2.5M reinstated until such time as it is determined what the \$2.5M was used for or until such time that the House of Assembly gives approval for write-off.

The remaining amounts reported as held at TCI Bank Limited Account of approximately \$965K should be provided against, and subsequently recommended for write-off, to reflect a more likely recoverable amount as the bank is in liquidation. This will need House of Assembly approval.

There were also prior year adjustments made of \$5.8M in 2011 and 2012 which are unclear and need to be investigated and properly accounted for.

Compliance with GAAP would have provided the guidance to determine how to account for these assets. The limited recording of assets on the statement of financial position, such as arrears, leases, scholarship commitments etc., increases the risk that amounts may be written off without

sufficient transparency including the requisite House of Assembly approvals. In addition, given that there were weak controls over the assets, this increases the risk of misappropriation of assets.

Liabilities

There is inconsistency in the presentation of liabilities on the statement of financial position. There are very significant liabilities not presented, including creditors, accruals, public private partnerships, alternative financing, pensions and accrued interest. In addition, some significant liabilities were included on the statement of financial position, together with the associated expense in the statement of financial performance, which did not meet the purported cash basis of accounting adopted by TCIG. The liabilities presented were not, therefore, considered to be an accurate representation of TCIG's liability position.

The accounting treatment of the \$116M PPP loan arrangement needs to be properly assessed and, if found to be a public debt, to be included as such. This amount is made up of costs to construct the hospitals, provide ring-fenced medical equipment, capitalized interest, project management fees, professional fees and accommodations which, together with the future contractual obligations, were all not fully disclosed in the July 31, 2014 financial statements. The difference noted was \$37M, a significant amount. In the absence of such important information to policy makers and other stakeholders, decision making can be impaired. The information being disseminated to the public and users of the financial statements, including other stakeholders, regarding this PPP was previously incorrectly stated in the notes to the financial statements which showed approximately \$80M as the infrastructure and ring-fenced medical equipment costs paid under the hospital services contract.

During the audit there has been a common theme of poor contract management strategies employed with respect to the management of the health contracts. The financial audit of the IHC contract has taken an inordinate amount of time to complete and this should be placed in the House of Assembly for debate when it is completed. Further engagements of audits of this nature must involve the Auditor General as required in the Constitution and the NAO Ordinance.

Effective treasury management needs to be addressed as there are high interest loans being serviced while very large amounts of surplus cash are invested at low interest rates. Examination of some of these loans or bonds should be undertaken and, where possible, be repaid earlier and potentially save millions in future interest costs. This is an important consideration. Against the backdrop of retiring a Scotiabank loan of \$9M at around 0.98% interest, it is recommended that certain higher interest loans and bonds could have been repaid in priority. By focusing on the higher interest debt repayments, this can further improve the reported surplus. It is concerning that NIB is having to write-down amounts held at TCI Bank Limited by approximately \$9M to \$11M while TCIG, on the other hand, continues to pay high interest on \$11.5M, 8 to 8.5%, bonds held with, or

partially with, TCI Bank Limited. This should be examined closely with a view to repaying higher interest debt first and foremost to save the public purse unnecessary expenditure.

Contingent liabilities are not accurate. Amounts are included and removed on a seemingly arbitrary basis. A contingent liability for \$6M, for example, likely includes certain amounts that have already been committed to and received, and should therefore be expensed in the statement of financial performance and included as a liability in the statement of financial position. An actuarial valuation for TCIG had not been performed since 2006, despite the significant unmeasured liability it represents for TCIG. In a review of an actuarial valuation of the Public Service Pension Plan submitted to me on 30 January, 2015, it was confirmed that the unfunded actuarial liability was \$84.8M. Given the late timing this liability could not be audited and I provide no assurance on the figure.

Limitation of Scope

A significant amount of information requested was not provided in the time allowed, thus limiting the scope of the audit procedures.

Accounting Basis

The PFMO requires the financial statements to be prepared in accordance with GAAP. The accounting basis used by TCIG, the modified cash basis of accounting / cash basis as modified (modified cash basis), is not a recognised GAAP. The modified cash basis has significant limitations, not least the ability of accelerating/delaying payments or receipts to impact financial performance, the ability to discretionally modify the basis as the preparer sees fit, lack of comparability to other entities, exclusion of significant TCIG assets and liabilities, and the inability to make decisions based on accurate and reliable financial information.

The cash basis of accounting is not adequate to meet the accounting requirements in the PFMO and PFMR. In reviewing the PFMO and PFMR, it appears the intention is not to report on a cash basis.

Disclosures

Many of the financial statement disclosures are incomplete, inadequate and not in compliance with GAAP. They do not allow the user to fully understand TCIG's financial performance and position as presented as well as other important issues. The accounting policies presented, in both the July 2014 and January 2015 versions of the financial statements, are incomplete and unclear. There are inadequate systems to record and manage related party transactions, non-compliance in relation to disclosures of related party transactions, elements of significant influence are not adequately monitored as the controls are weak, inadequate disclosure in relation to close members of the family of key management personnel and an inadequate system to deal with third party payments

and in-kind services. There has been some limited improvement to the disclosures but, given the late timing of revisions and lack of information requested in the timeframe required, I cannot provide any assurance at this late stage.

TCIG's financial statements are a critically important document for TCIG and TCI. They are a publically available document used by many stakeholders. They act as the basis for credit ratings, budgeting, financing and good governance. Without accurate, reliable, comparable and consistent financial reporting their credibility is undermined and the stakeholders' needs are not being met. It is therefore of critical importance that the issues identified are examined and a critical path analysis immediately prepared by TCIG to address the points raised.

The purpose of GAAP, accounting policies, accounting bases etc. is to ensure financial statements are meaningful and comparable, that they represent a true and fair position, are fit for purpose and that policies are consistently applied. Financial reporting has to follow a framework. It is not intended that the framework be used and/or changed to facilitate the desired reporting.

Internal Controls and Internal Audit

The NAO received from the Audit Committee Chairman a high level assessment on TCIG's internal controls which gave general indications of improved high level controls but weak activity level controls. It is hoped that future internal audit deliverables can be improved to provide a full report on the effectiveness of internal controls as required under the PFMO and PFMR. This would assist the NAO in being able to establish more meaningful recommendations across the public service. While the NAO used the controls in order to develop programs, we cannot provide an opinion on the effectiveness of the controls at this stage.

Value for Money

In terms of value for money within the procurement process, the risk appears to be low to moderate on the front end (e.g. at the assessment and justification stage) but high risk exposure exists during the implementation phase i.e. in the contracts management phase. Attention should be paid on scoping and properly assessing the need but even greater attention should be paid in ensuring TCIG gets what it pays for during the performance of the contract. Contract management is weak and needs to be improved as an immediate priority.

There are increasing purchase orders, contracts, transactions, services, revenues, expenditures, commitments, liabilities and business investments throughout the whole of government (including statutory bodies and other agencies) across the islands. This requires increased audit coverage to ensure that VFM audits are completed to give an overall indication of how well money is being spent. It is not cost effective to have both the NAO and Internal Audit Department, with

approximately 15 staff members in total, all based in Grand Turk when audit activities are demanded across all the islands, including high levels of audit and other risks in Providenciales.

Fraud/Abuse/Mismanagement

Legislation within the PFM Framework relating to combating fraud (asset misappropriation, corruption and material misstatements) is adequate, but because the activity level controls are not properly implemented, the risk remains high.

I am unable at this time to provide any assurance that the risk of fraud and abuse is managed to an acceptable level. There do appear to be situations in which the risk of fraud, abuse and mismanagement exist. The matters which came to my attention and/or occurred during the course of this audit are to be further investigated or transferred to the relevant authorities for action.

Conclusions & Recommendations

A combination of ineffective implementation or adherence to laws, weak operational procedures, non-compliance with GAAP, shortage of a mix of appropriate resources and minimal disclosures of related party transactions can increase other risks such as errors, omissions, material misstatement, misappropriation of assets, wastage, abuse and fraud. The root causes of the problem are primarily due to a resource limited public service, a tolerance for errors and omissions, a lack of transparency in monitoring and reporting related party interests and poor contracts management, all of which can have significant influence on operational decisions made.

The recommendations are to:

- Enhance the public service, including oversight bodies, with an optimum mix of expertise, training, knowledge transfer and getting the job done coupled with the use of technology;
- Adhere to GAAP as required under Section 45 of the PFMO and throughout the PFMO and related regulations;
- Implement, enforce and adhere to the financial laws by establishing operational level controls and systems;
- Reduce tolerance for errors and omissions;
- Strengthen the revenue collection process, in particular, ensuring the accurate capture and monitoring of arrears, including write-off procedures;
- Strengthen performance management of contracts; and
- Establish a strong system to record and disclose properly all related party transactions and move to ensure proper audit trail of ALL economic and financial transactions.

Specific Recommendations

- 1) Immediately prepare a detailed critical path analysis as to how TCIG continues the transition from cash accounting to accruals accounting, together with compliance with GAAP, as already achieved in the Cayman Islands. Rules-based accounting must be enforced as we risk moving back into the pre-2009 position with large scope for discretion to be applied.
- 2) Immediately put in place plans to consolidate the entire Government accounts including TCIG and the statutory bodies, as done in the Cayman Islands, to get a complete economic and financial picture of TCIG.
- 3) Immediately retain or appoint suitable expertise in bringing the accounts up to an acceptable standard in compliance with GAAP that is consistent with Section 45 of the PFMO and in accordance with Section 52 (5) of the PFMR to ensure the fundamental requirement of the financial position and performance of TCIG being FULLY disclosed to the House of Assembly.
- 4) Immediately ensure proper resourcing requirements are provided to critical areas of financial management and governance.
- 5) Immediately retain specialist expertise in implementing more of the complex PFM laws and regulations as these have the highest risk and impact.
- 6) Consider appointment of a team of financial controllers from the statutory bodies to make solid recommendations in improving TCIG's financial reporting including working with the Ministry of Finance to ensure that this is done by the 2015/16 cycle at the latest.
- 7) Ensure the development of an enhanced public service organization with the optimum balance of expertise, training, knowledge transfer and achieving objectives.
- 8) Ensure that the activity level controls in support of the new laws and regulations are sufficiently embedded in the system of financial accounting and reporting, in particular, ensuring ALL transactions that have an economic value (whether given or received, cash or non-cash) are captured.
- 9) Move towards measuring, recording and disclosing transactions such as assets with a service potential of more than one year such as TCIG's buildings and capital developments.
- 10) Ensure proper evaluation and management of contracts which place a long-term liability upon the public purse in accordance with the PFM laws and regulations.
- 11) Develop a strategy to implement all controls, laws and regulations in finance and other departments especially those related to contract requirements and other covenants that give rise to an event which creates an obligation on TCIG's finances or results in a benefit to TCIG.
- 12) Improve collection and enforcement efforts to ensure that TCIG receives what it is legally due, while at the same time encouraging growth and investment initiatives.

- 13) Engage internal audit to assist the ministries and departments with improvement of the controls as required under Part VI of the PFMR and other relevant sections of the PFMO.
- 14) Evaluate the possibility of repaying some of the loans and or redeeming bonds early to reduce net interest expense and improve treasury management.
- 15) Ensure that appropriate due diligence is performed on entities prior to their transacting with TCIG.
- 16) Ensure that the NAO is properly resourced, removed completely from entities which it audits and a separate central server is established to mitigate against any confidentiality risks.

The fundamental requirement is to ensure that the financial performance and position of the Government is fully disclosed to the House of Assembly with the ultimate objective being protection of the public purse and in the interest of the long term financial stability of TCI.

Whichever way it is achieved it must be grounded in sound compliance with laws and regulations AND a recognised GAAP which limits arbitrary and discretionary accounting practices.

4. REVENUE

4.1 Potential revenue loss of \$5 - \$10 million annually - HR

While controls around revenue actually recorded appear to be adequate and working, compliance with laws and regulations around collection of amounts due are inadequate. Due to the absence of sufficient resources to marshal a robust compliance and enforcement program it appears likely that substantial revenues are foregone. The weaknesses identified in revenue collection, and by extension the likelihood of tax revenue legally due not being collected, appears high. Due to a lack of information **estimating the revenue shortfall is difficult however it could range between \$5M and \$10M.**

Consideration should be given to setting up a properly resourced central revenue department, under the leadership of a Commissioner of Revenue, with the power to examine compliance in all revenue streams and to levy civil penalties for tax being evaded.

4.2 Millions in revenue arrears to be validated, corrected, collected or recommended for write off - HR

The revenue arrears statement was received from the Ministry of Finance, however, when it was compared to the supporting documentation provided by the accounting officers, some of the figures did not correspond, no supporting documentation was provided and/or no arrears were recorded on the revenue arrears statement.

Scholarship fund contribution arrears \$19.9M

There was a significant difference in the scholarship fund contributions arrears of \$3.2M, as reported in the financial statements resubmitted on 15 January, 2015, and the \$19.3M comparative. Another table provided by the ministry showed the arrears as \$19.9M.

Table 2 - Scholarship contributions reported by the ministry

Active Developments in arrears	\$1,676,400
SIPT Cases	\$8,567,000
Under Renegotiation - Investment Unit	\$8,078,174
Receivership	\$843,000
AG Chambers Case	\$91,000
Projects that were halted/ never started	\$601,250
Total	\$19,856,824

Differing reports showed scholarship contributions due as \$20.3M (a statement received when the 2012/13 audit was done), \$19.9M (as shown in Table 2), \$19.3M, as shown in the 2013/14 financial statements resubmitted on 15 January, 2015, and \$3.2M, as shown in same resubmitted financials.

\$38.2M business license arrears accumulated since 2001

Another major element of outstanding arrears, that was received from revenue control by the NAO on/about 13 Jan, 2015, showed business license arrears accumulated since 2001 as **\$38.2M**. This amount is extremely significant and material. Even simply taking the last 5 years ageing report, as shown in table (below), the amounts are significant.

Table 3 - Business Licence Arrears within the last 5 years

Ageing	Applicable Rates	Penalty	Total
Within the last 5 years	13,124,986	13,217,296	26,342,282
Within the last 3 years	8,870,080	8,536,899	17,406,979
Within the last 2 years	6,045,783	5,430,173	11,475,956

The ageing report must be validated, sanitized, enforcement action taken to collect amounts legally due to TCIG, and approval sought from the House of Assembly to write off those amounts that are not considered recoverable.

Overall

Given the importance of accurate arrears reporting and the material amounts presented as revenue arrears in the prior year, a misstatement in this area can significantly impact the accuracy of TCIG's financial statements. The Ministry of Finance needs to ensure that accurate and reliable figures are made available. The lack of proper documentation and information indicates that there is inadequate regular monitoring and ineffective management of the collection process.

It is also possible that not all debtors were considered when preparing the arrears report. This can impact future revenue receipts, if debtors are not followed up for payment, and also contribute to poor monitoring of future financial periods because the absence of receipts may be attributed to another reason/issue.

4.3 Revenue arrears not accounted for on the statement of financial position - HR

Revenue arrears represent amounts owed to TCIG. These should be accounted for as receivables due on the statement of financial position. Any write-offs of these receivables should be approved

by the House of Assembly. As these revenue arrears are not currently reported on the statement of financial position their write-offs may not be subject to the required approvals by the House of Assembly. This has a material impact on the accuracy of the financial statements and compliance with the PFMO and PFMR.

TCIG should consider including revenue arrears on the statement of financial position as this facilitates far greater control and accountability over the accuracy and reliability of what is reported to the House of Assembly.

4.4 Inadequate management of concessions granted (\$78.7M for the 3 years to March 31, 2014) - HR

Concessions granted by TCIG are preferential provisions (e.g. for import of goods) that provide certain taxpayers with subsidies, exemptions, discounts etc. that are not available to others. Although there are some benefits derived from granting these concessions, the economic values foregone are not being properly monitored to ensure that value for money is received. The value of concessions, or economic value foregone, in the year ended March 31, 2014, per the financial statements submitted on July 31, 2014, was \$28.1M (\$78.7M in the three (3) years to March 31, 2014). The value of concessions granted for the year ended March 31, 2014 was increased to \$30.5M in the financial statements resubmitted on January 15, 2015.

There are certain conditions which must be met in order to be approved for these concessions. If the value obtained in return for providing these concessions is not being monitored this can result in a loss of benefit to TCIG.

The total number of persons/companies granted concessions during the 3 years to March 31, 2014 was 1,650 as detailed in Table 4. The associated benefits derived were unable to be established because they have not been sufficiently monitored.

Based on limited records, it was discovered that there were 108 companies who received concessions during the year ended March 31, 2014 who also owed monies (\$344K (concessions granted), \$1.8 million (arrears)) to TCIG. This appears possible due to weak controls. This impacts the accuracy of disclosures in the financial statements. Appropriate measures should be taken to correct these control weaknesses.

Table 4 – Number of Entities receiving concessions in the three years to March 31, 2014

Range	No. of Entities	Amount received in 3 year period (million)	% entities	% concession granted
>5 M	2	38.1	0.1%	48%
>1 M	10	23.8	0.6%	30%
>500K <1 M	1	0.6	0.1%	1%
>100K <500K	39	8.5	2.4%	11%
>20K <100K	94	4.2	5.7%	5%
5K <20K	223	2.2	13.5%	3%
>5K	1281	1.3	77.6%	2%
1650		78.7	100%	100%

The table indicates that under 1% of the total entities are granted 79% (approx. \$62M) of the concessions in the last 3 years. These only relate to concessions that are recorded.

Concessions by sector/industry such as utilities, tourism, health etc. should be disclosed (this was included in the revised financial statements submitted on 15 January, 2015). TCIG should institute a proper controls management system for concessions and subsidies to measure their economic benefit.

A value for money audit needs to be conducted to determine the relative benefits (quantitative and qualitative) especially in the larger grants such as for power and fuel.

4.5 Non-recording or non-recognition of \$2.915 million of stamp duty foregone - HR

In December 2012, stamp duty calculated (per TCIG's records) on a \$53 million property sale was \$5.3 million payable over 4 equal annual installments under the installment payment option available at the time of the sale. One payment of \$1.325 million was received at the time of the sale. The balance of \$3.975 million was not recorded or disclosed in the 2012/13 Financial Statements as a receivable or arrears due to TCIG. In December 2013, a year later, a Stamp Duty Remission Order was passed, \$1.060 million was paid to TCIG, and the balance of stamp duty due to TCIG of \$2.915 million was foregone. It could not be ascertained whether the write off was, or was required to be, reported to the House of Assembly as this could be viewed as revenue due to TCIG instead of a concession granted. The Ministry of Finance needs to clarify this together with the rationale for the remission order.

TCIG needs to consider the level of accountability for these types of revenues foregone or concessions granted and ensure that they are monitored. It must also consider the quantum of

concessions granted to a few entities and ensure that the relative benefit derived is assured. There is a risk of loss of economic value to TCIG if these concessions are not monitored.

4.6 Lease commitments and incentives not disclosed – HR

Leases entered into by TCIG should be disclosed. Those containing concessions should be separately disclosed as part of the concessions disclosures. It is recommended that GAAP be adhered to determine the accounting treatment of lease incentives and how the leases themselves are treated. Leases at “peppercorn” rents, or below market value, are revenues foregone and should be accounted for in accordance with GAAP as provided for in Section 45 of the PFMO.

4.7 \$934K net repatriation deposits treated as revenue upon receipt instead of a liability – HR

As part of new work permit applications the employer is required to pay TCIG a deposit to be used by TCIG in the event that the employer fails to repatriate the employee at the end of their contract. These deposits are refundable, however, they are currently recorded as revenue upon receipt. When the work permit is surrendered at the end of the employee’s contract, and evidence provided that the employee has been repatriated, any deposit refunds made to the employer are currently charged as an expense against revenue at the time of repayment. These amounts should not be recognized as revenue at the time of receipt, but held on the statement of financial position as a liability until such time as they are either utilized to pay for repatriation, refunded to the employer or can be released. This may be caused by inappropriate coding to a revenue code. **The effect is that revenue may be overstated. The net amount of revenue recorded, after deducting refunds, in the year ended March 31, 2014 was \$933,575.**

4.8 Unregistered private lodgings possibly not paying Hotel and Restaurant Tax – HR

The Hotel and Restaurant (Taxation) Ordinance requires that proprietors providing paid tourism lodgings should register their premises and charge Hotel and Restaurant Tax to their guests for onward payment to TCIG. It is possible that villa owners are not registered and therefore not paying taxes due on short term tourist rentals, particularly if the administration is done outside of TCI.

The lack of a robust compliance program that covers unregistered businesses together with the limited number of businesses prosecuted for non-registration or payment means that there is little to discourage those entities which choose to evade the payment of the Hotel and Restaurant Tax.

There is a potential loss of revenue to the Turks & Caicos Government in respect of the Hotel and Restaurant Tax. As an example the total Hotel and Restaurant Tax effect of the 690 properties listed in November 2014 on VRBO (Vacation Rentals by Owner), one of a number of websites offering private tourism accommodation for rent, using a 50% occupancy rate at an estimated average of

\$550 per night total accommodation tax payable for these properties would be approximately \$8M per annum. If only 10% of these properties did not pay the required Hotel and Restaurant Tax this would lead to a shortfall in Hotel and Restaurant Tax of approximately \$800K.

4.9 Revenue Control Unit did not subject tourism lodgings and restaurants to annual audit – HR

The Hotel and Restaurant (Taxation) Ordinance requires that tourism lodgings and designated restaurants pay Hotel and Restaurant Tax on a monthly basis. It is possible that certain establishments are not filing all their returns or are filing returns that understate the tax payable. Of the 380 registered hotel and restaurant tax payees in the year ended March 31, 2014, 264 submitted less than 12 monthly returns of which 132 submitted less than 6 returns. Even allowing for a summer closing it is expected that the vast majority of registered payees would submit a minimum of 9 returns in a year. It is possible that the numbers are the result of a change of ownership, a prolonged shut down or extended use by the owner, but unless there is a systematic follow up of the months with no submitted returns it is difficult to know.

The lack of a compliance program that covers the majority, if not all, of the potential population and the limited number of businesses prosecuted mean that there is little to discourage entities who choose to avoid payment of the tax. **There is therefore a potential loss of revenue to TCIG in Hotel and Restaurant Tax. As an example, the 132 properties which submitted less than 6 monthly returns reported revenue of \$770,000. If these are under reporting their revenue by an average of 20% the loss to TCIG would be in the region of \$154,000.**

4.10 No systematic compliance checks for compliance with business licensing requirements – HR

The Business Licensing Ordinance requires that all businesses on the Islands (with certain limited exemptions) are required to register and pay the required license fee. It is likely there are businesses in operation that have not paid the appropriate license fee. As an example, in reviewing the most expensive business license renewal category for the year ended March 31, 2014 (costing \$5,400) there were four (4) accountancy firms, eleven (11) lawyers, eight (8) development companies, five (5) quantity surveyors, three (3) water companies and eleven (11) other businesses registered.

The number of professional firms on the Island would seem to be significantly higher than the business license renewals. The lack of a comprehensive compliance program together with the limited number of businesses prosecuted for non-payment of the business license means that there is little to discourage businesses from avoiding the payment of business license fees.

There is a potential loss of revenue to TCIG in business license fees. In the most expensive category alone there could be a loss of TCIG revenue in excess of \$100,000.

4.11 No annual compliance checks for compliance with the Immigration Ordinance - MR

The Immigration Ordinance requires a valid work permit for individuals to work in the TCI who are not a Turks & Caicos Islander, or a Permanent Resident Card holder with permission to work, a British Overseas Territory Citizen, as evidenced by a passport or naturalization certificate, or the spouse of a Turks and Caicos Islander as evidenced by a Residence Permit. It is possible for individuals to enter the country illegally or under false pretences and work without a work permit in contravention of the Immigration Ordinance. The lack of a systematic compliance program and the fact that a limited number of employers are prosecuted for employing individuals without work permits means that there is little to discourage employers for avoiding obtaining a work permit and paying the associated work permit fees. **There is a potential loss of revenue to TCIG in work permit fees and labour clearance fees.**

4.12 Significant number of custom tariffs can lead to possible tariff shopping by importers – MR

The Customs Ordinance requires that goods imported into TCI should pay import duty using the appropriate tariff for the type of goods imported. The significant number of different tariffs (in excess of 6,000) and the oftentimes marginal difference in descriptions may lead to tariff shopping by importers. Customs officers may have difficulty in establishing the correct tariff rate for imported goods. It is likely that importers will always opt for the lowest rate. **There is a potential loss of revenue to TCIG in import duties.**

5. EXPENDITURE

5.1 Significant increase in IT costs from \$1.7M to \$3.5M and a \$6M contingent liability - HR

On 9th November, 2012 a consultancy contract, with a contract duration of 60 months from date of commencement of services, was entered into between TCIG and an information technology (IT) service provider (the service provider) for \$1,767,684. The associated payment schedule was spread in installments over the life the contract. It needs to be determined if it is a pay as you go scheme or a contract.

An unsigned "Development Proposal for additional provision for Wide Area Network (WAN), Local Area Network (LAN), LAN Managed services and internet service" (the proposal) with the service provider was also reviewed. The proposal "date submitted" was 21 May, 2013. It indicated that funding would come from TCIG's consolidated fund. The proposal was for an additional \$1.7 million. The purpose of the proposal appears to be to address additional provisions required such as cabinets, racks, structured cabling, uninterrupted power supply, high-end PC workstations, regular and rugged laptops, servers and network storage devices, checkpoint firewall, memory for PowerEdge servers, commercial and customized bespoke software and additional WAN/LAN Hardware and LAN managed services. The value of these additional provisions was to be financed over 60 months. This additional contract for \$1.7 million approximately doubled the original contract cost to \$3.46 million.

The significant increase in costs implies that the original scoping was not properly performed or that the second contract was for a new engagement. Confirmation is needed if adequate approval was provided for the original contract and the subsequent changes in scope / new contract and if the House of Assembly was required to assess this in accordance with the PPO.

The additional services outlined in the proposal involved the provision of assets to TCIG but allowed for payment for these to be spread over 60 months. This could therefore be deemed a financing arrangement entered into by TCIG. Section 34 of the PPO requires any alternative financing arrangement or private finance initiative to be suitably appraised by the House of Assembly to ensure that value for money is obtained and a robust cost benefit analysis is carried out. Section 34(2) of the PPO and Section 30(13) of the PFM states that any form of alternative financing requires approval of the Secretary of State together with a sound appraisal underpinning the proposed project before the financing means has been determined, a financial appraisal demonstrates improved value for money against a conventionally financed alternative, the long term affordability case has been assessed and agreed by the appropriate technical experts retained by the government and an independent opinion has been received from a qualified accountant of good standing on the correct accounting treatment in the government's accounts. Section 34(3) of the PPO and Section 30(14) of the PFM state any form of alternative financing must not be used for

a project where the fast pace of change in the sector makes it difficult to define effectively the outputs it requires in a long term contract (such as information and communication technology projects). Section 30(8) of the PFM states any form of alternative financing requires independent accounting, legal, financial, economic, environmental and other technical advice as appropriate to ensure robust investment appraisals. It is not clear whether the above was done. This transaction needs to be evaluated fully to determine if there were breaches in the PPO.

The commitment and contingent liabilities statement in the public accounts includes a “remaining cost on the Contract” of \$5,992,756. It needs to be determined if the obligation to pay some of these costs has already been incurred in 2013/14, and whether, under GAAP, it should therefore be included in liabilities. Overall the disclosures in the financial statements, including the future obligations to the IT Service Provider, are inadequate.

This contract is to be investigated further.

5.2 Netting of hospital revenues with hospital expenditures - HR

In reviewing the payments to IHC, it appears that co-payments collected by the hospitals, together with TCIG’s share of third party hospital revenues, are deducted from the amount charged by the hospital providers (IHC) to TCIG as hospital expenditure. This netting off needs to be corrected as it understates revenues and expenditures of TCIG. By separately recording the co-payments and third party revenues the true revenues and costs of the hospitals can be identified allowing for better informed financial decisions and management.

Based on the NAO review of three (3) invoices as noted in Table 5 it indicated that co-payment and third party revenues were deducted against expenditures incurred.

Table 5 – Co-payments and 50% Third Party Revenues deducted from amounts due to ClinCo

From:To	Invoice #	Date of invoice and period ended	Copayments collected and deducted against amount due to ClinCo	50% of Third Party Revenue deducted against amount due to ClinCo	Total
IHC to TCIG showing amounts due to Clinco.	IHCTCI 029	31 December, 2011 for same period	328,869	169,265	498,134
same as above	IHCTCI 045	6 March, 2013 for period ending 31 December, 2012	327,802	396,904	724,706
same as above	IHCTCI 059	20 February, 2014 for period ending 31 December, 2013	349,784	329,678	679,462
			1,006,455	895,847	1,902,302

5.3 Consolidated healthcare related costs approximate \$64M (split between TCIG and NHIB) - HR

The total healthcare costs incurred are currently split between TCIG and NHIB.

TCIG's financial statements for the year ended March 31, 2014 include both hospital provisional charges (to IHC's infrastructure company ('Infraco')) of \$24.5M and transfers to NHIB for medical treatment payments (to IHC's clinical services company ('Clinco')) of \$20.6M.

Per the audited NHIB financial statements for the year ended March 31, 2014 financial contributions made directly from NHIB to IHC, as directed by TCIG, were \$24.8M. This is \$4.2M higher than the transfer to NHIB from TCIG. In addition, NHIB paid additional healthcare expenses, such as overseas treatment, of \$14.2M.

The combined total healthcare costs incurred by TCIG and NHIB needs to be aggregated and disclosed. At the moment TCIG is paying both InfraCo and NHIB. NHIB in turn is paying both its own costs together with payments to ClinCo as directed by TCIG. As NHIB's payments to ClinCo exceed the grant provided by TCIG to NHIB, TCIG's financial statements currently understate by \$4.2M the full clinical costs paid to IHC. If TCIG's accounts were performed on a consolidated basis the total medical costs could be established. As noted in Table 6 below, the total healthcare costs combined is approximately \$63.5M (2013/14) and \$62.1M (2012/13) as opposed to the \$45.1M (2013/14) and \$42.5M (2012/13) reported by TCIG on a standalone basis. If one were to also include the amounts netted to hospital expenditures these can add approximately another \$500K - \$700K for the period. These healthcare costs may also exclude other costs such as TCIG payroll (Ministry of Health) and other NHIB operating costs (payroll, rent etc.).

Table 6 – TCIG and NHIB health related costs for the years ended March 31, 2014 and 2013

	2013/14	2012/13
Hospital Provisional Charges (TCIG Fin Stats)	24.5	24.3
NHIB Transfers (TCIG Fin Stats)	20.6	18.2
Additional contributions towards clinical costs as directed by TCIG*	4.2	5.8
NHIB Other Healthcare Expenses (in NHIB's Financial Statements, note 14)	14.2	13.8
Total	\$ 63.5	\$ 62.1

*Additional contributions identified in NHIB's Fin Stats;

Transfers made to IHC from NHIB	24.8	24.0
Less NHIB Transfers from TCIG	(20.6)	(18.2)
Additional contributions	4.2	5.8

5.4 Several repeat audit findings impacting approximately \$21.2M in expenditure – LR to HR

There were several repeat audit findings on weak expenditure controls, impacting approximately \$21.2 million of expenditures incurred throughout the Ministries and Departments. [The severity of these control weaknesses has decreased year over year and risks have moderated somewhat. However,](#) TCIG needs to strengthen these controls otherwise they are likely to occur again.

Repeat audit finding exceptions for financial controls include, but were not limited to, the following:

- Advances, including travel advances and loans, not managed in compliance with PFMR
- Beneficiaries approving their own payments
- Contravention of the Appropriation Ordinance
- Duplicate payments
- [Excess Expenditure per line item reduced significantly from \\$19M \(2012/13\) to \\$425k \(2013/14\)](#)
- Expenditure incurred despite no budgeted amounts
- Inadequate management of inventory
- Inadequate management of property, plant and equipment
- Inadequate maintenance of payroll information
- Ineffective controls to ensure warrants issued are not overspent
- Invoice attachments not checked for calculations. No proper review of payments
- Invoice certifications were not duly and competently performed
- Lack of and/or unable to view supporting documents on SmartStream
- Lack of supporting documentation on file
- Losses of public moneys and stores
- Losses not properly managed in accordance with regulations
- Mis-postings
- No Chief Financial Officer approval/business cases attached for payments \$10K and above
- No contracts and/or purchase orders to support expenditure incurred
- No reconciliation for some deposit accounts
- Payments charged to incorrect accounts. No reconciliations provided
- Projects approved in the appropriation ordinance 2013 were not undertaken
- Purchase orders not matched to invoices where applicable
- Transactions approved in SmartStream by the same person at both levels
- Warrants issued that were more than the approved budget for 2013/14
- Warrants issued where there was no budgeted figures

5.5 Several control exceptions and repeat audit findings in Development Fund expenditure – HR

There were several repeat audit findings and control exceptions identified when examining the Development Fund as follows:

- Projects identified as not being initiated by a warrant not investigated by SPPD
- Ineffective controls to ensure warrants issued were not overspent
- Projects approved in the Appropriation Ordinance not undertaken
- Over-expenditure compared to estimates
- Warrants issued for more than the approved budget for 2013/14 and warrants issued where there were no budgeted figures
- A lack of supporting documents to verify donor funding received
- One duplicate item was identified

5.6 Lack of supporting documentation for \$6.6M in journals – HR

Of 855 journals reviewed, 262 journals, with a dollar value of \$6,613,672, did not have supporting documents attached. There may be a risk of error, omission and/or fraud. In order to mitigate this risk it is recommended that full supporting documentation be attached to all journals made to ensure a proper audit trail.

5.7 Bulk Ticket higher by \$154K compared to on-demand prices - HR

TCIG purchases local air tickets in bulk. The price paid for bulk tickets from Grand Turk to Providenciales are approximately \$140 per return trip. The total spent for 2013/14 on local air tickets was \$359K. The current average cost of an on demand return ticket from Grand Turk to Providenciales is around \$80 which is 43% less than the average price paid by TCIG of \$140. This translates into annual potential savings of \$154K if one were to have purchased on demand over the course of the year. For 1 month this can approximate to \$13K savings. In addition it would generally be expected that bulk buying should be lower than individual purchases.

While it is expected that there would be some benefits to having pre-purchased tickets, it is recommended that this purchase mechanism be revised to achieve better value for money.

5.8 Poor vendor master file management – HR

As at March 11, 2014 TCIG's database contained 19,252 vendors. Such a large vendor list for an island the size of TCI indicates that the vendor list is not being actively managed. Key points identified were:

- No vendor master file policy to guide users on adding, changing vendor information, inactivating vendors and conducting of vendor due diligence
- No officers are responsible for reviewing and approving vendors, changes to information, inactivating or reactivating vendors and ensuring accuracy of the vendor information
- No vendor audits have been carried out in 2013
- No vendor due diligence have been carried out in 2013 either before or after vendors were entered into the system
- No officer is responsible for ensuring that vendors have up to date business licenses, outstanding fees or arrears with TCIG before they are paid
- Reports on vendor additions, deletions and record changes are not generated by a responsible officer for management review
- No cleansing of old or duplicate entries from the vendor master file on SmartStream
- No assigned limits based on license categories (for example contractors are categorized as petty, small medium and large). Payments to vendors are not strictly based on vendor license size
- Inaccurate vendor information within the SmartStream vendor master file such as:
 - 647 vendors did not have a country code
 - 11,747 did not have a listed city
 - 7,505 had information in city name but the following was noted:
 - 854 of the vendors had bank account numbers entered as city name
 - One had cell phone number entered as city name
 - 24 had information in street address but only nine were actual street information. Two of the nine records were duplicate vendors
 - No standard method for capturing names and address of vendor in the vendor master database. The database is case sensitive and a search can yield no result if the correct format is not used for the search criteria for the vendor's name
 - 203 duplicate vendors; 185 with two vendor records, 18 with three vendor records and 4 with four vendor records
 - 1,819 records show contact name as "Manager", 144 records show contact name as 'To Whom It May Concern', 6 show contact name as "Manage'
 - Initials used for person's name

5.9 IT Control Issues – HR

Tests carried out on 1,141 SmartStream transactions totalling \$76,785,366 (being all payments over \$5,000 across all ministries and departments) revealed that 72 transactions were approved at the first and second level by the same officer, and 82 transactions did not have relevant supporting documents attached. The expenditure of those transactions totalled \$18,184,531 (being \$4,456,340 and \$13,728,191 respectively).

A summary of journals by User ID for the 2013/14 period using IDEA was carried out. This identified 20,555 records had been entered and/or posted by a former employee of TCIG ('HSWASEY'). According to SmartStream the last payroll payment for this employee was September 2003.

Controls over providing and removing rights of access are inadequate and should be improved. It is recommended that the list be cleansed and appropriate controls are introduced for employee departures.

5.10 Excess Expenditure – MR

The following ministries and departments had excess expenditure of \$426K for 2013-2014, a significant reduction on the \$19M reported in 2012/13.

Table 7 – Excess expenditure per line item

Min	Prog	Description	Estimate SmartStream	Actual	Diff \$	Diff. %
6	14	Audit Department	-	(311)	311	-
7	24	Gaming Inspectorate	-	140	(140)	-
16	87	Labour Tribunal	305,293	318,629	(13,336)	(4)
51	60	Prison Services	2,027,523	2,206,357	(178,834)	(9)
51	86	Agricultural Department	482,885	490,023	(7,138)	(1)
52	45	EMS - Mechanical Services	533,551	541,564	(8,013)	(1)
52	81	EMS _ Project Management	332,266	338,316	(6,050)	(2)
54	17	Budget Office	195,741	206,323	(10,582)	(5)
54	21	Treasury Department	1,232,216	1,298,176	(65,960)	(5)
54	121	(No name here)	-	460	(460)	-
55	32	National HIV	285,215	293,879	(8,664)	(3)

		Prevention Unit				
55	89	Special Needs Unit	1,246,430	1,262,416	(15,986)	(1)
55	107	Emergency Medical Services	518,780	545,471	(26,692)	(5)
56	2	Human Resource Directorate	588,619	595,214	(6,595)	(1)
56	7	Unallocated Staff	277	5,257	(4,980)	(1,798)
56	92	House of Assembly	2,361,475	2,429,803	(68,328)	(3)
57	36	Education Administration - Zone 1	343,161	347,440	(4,279)	(1)
					(425,723)	

- There were 36 accounts, totaling \$104,477, within various ministries and departments that did not have estimates but expenditure was posted against them in contravention of PFMR Section 29
- There were 532 accounts, totaling \$1,432,107, within various ministries and departments that incurred expenditure in excess of the amounts allocated by the Appropriation Ordinance 2013-2014 and Supplementary Appropriations 2013-2014, in contravention of PFMR Section 51(1)
- The statement of excess expenditure was not laid on the Table at the House of Assembly as required by PFMR Section 51(3). The Table below shows that there was one Ministry that had excess expenditure of \$25K.

Table 8 - Excess expenditure per department

MINISTRY	ESTIMATES	ACTUAL	VARIANCE
01	3,316,760.35	2,846,158.80	470,601.55
03	21,006,561.11	20,432,202.17	574,358.94
04	11,312,292.45	10,763,696.17	548,596.28
05	5,710,817.91	3,649,244.29	2,061,573.62
06		(310.78)	310.78
07	2,868,722.01	2,779,767.24	88,954.77
14	25,061,098.95	21,478,093.82	3,583,005.13
16	5,836,719.21	5,546,109.59	290,609.62
51	7,684,562.65	7,470,060.73	214,501.92
52	14,197,908.75	13,870,202.14	327,706.61
54	11,282,260.89	10,716,393.01	565,867.88
55	56,282,650.25	55,654,711.19	627,939.06
56	3,891,287.98	3,916,555.26	(25,267.28)
57	21,562,927.98	21,319,027.78	243,900.20

58	1,264,598.16	1,186,790.89	77,807.27
Grand			
Total	191,279,168.65	181,628,702.30	9,650,466.35

5.11 Expenditure arrears management – MR

A review was carried out on the expenditure arrears for 2013-2014. The following issues were noted:

1. Total expenditure arrears for 2013/14 were \$1,577,097 as detailed below

Table 9 - Expenditure Arrears

Min	Description	Arrears
1	Governor's Office	1,300
3	Police	56,603
4	Attorney General's Office	354,911
5	Judiciary	1,590
16	Min of Border Control & Labour	31,431
51	Min of Environment & Home Affairs	12,104
52	Min of Government Support Services	333,518
54	Min of Finance, Trade & Investment	594,134
55	Min of Health & Human Services	126,665
56	Office of the Deputy Governor	17,502
57	Min of Education, Youth Sports & Culture	47,339
	Total SmartStream	1,577,097

2. The total arrears for the Ministry of Government Support Services was overstated by \$280,381 on treasury statements
3. Actual expenditure and arrears was compared to the 2013/14 ministry appropriations. The results are shown in Table 10. Four Ministries would have exceeded their budget allocation if all expenditure incurred in 2013-2014 was paid, and therefore recorded, in the year

Table 10 – Total expenditure and expenditure arrears summary

Description	Appropriation	Actual	Arrears	Actual Arrears	Diff. (Actual Arrears & Estimates) \$	Diff. (Actual Arrears & Estimates) %
Governor's Office	3,316,760	2,846,159	1,300	2,847,459	469,301	14
Police	21,006,561	20,432,202	56,603	20,488,805	517,756	2
Attorney General's Office	11,312,292.	10,763,696	354,911	11,118,607	193,685	2

Judiciary	5,710,818	3,649,244.	1,590	3,650,834	2,059,984	36
Audit	-	(311)	-	(311)	311	-
Office of the Premier	3,391,686	2,779,767	-	2,779,767	611,919	18
Statutory Charges	25,061,099	21,478,094	-	21,478,094	3,583,005	14
Min of Border Control & Labour	5,836,719	5,546,110	31,431	5,577,541	259,178	4
Min of Environment & Home Affairs	7,684,561	7,470,061	12,104	7,482,165	202,396	3
Min of Government Support Services	14,197,909.00	13,870,202	333,518	14,203,720	(5,811)	(0)
Min of Finance, Trade & Investment	10,973,142	10,716,393	594,134	11,310,527	(337,385)	(3)
Min of Health & Human Services	56,282,650	55,654,711	126,665	55,781,376	501,274	1
Office of the Deputy Governor	3,891,289	3,916,555	17,502	3,934,057	(42,768)	(1)
Min of Education, Youth Sports & Culture	21,349,083	21,319,028	47,339	21,366,366	(17,284)	(0)
Office of the Director of Public Prosecution	1,264,598	1,186,791	-	1,186,791	77,807.	6
Total SmartStream	191,279,167	181,628,702	1,577,097	183,205,799	8,073,369	4

6. ASSETS

6.1 Assets reported at higher than their likely recoverable amount - HR

There are a number of assets included on the statement of financial position at higher amounts than are likely recoverable, thus inflating the reported position. These include:

- Deposits held at TCI Bank Limited - \$965,889
- Loans receivable - General - \$8,973,303
- Loans receivable - TOLCO - \$2,752,422
- Loans receivable - Insurance - \$325,933
- Loans and advances recommended for write-off - \$2,573,918
- Others (including staff loans and advances, travel advances, other receivables and advances) - \$298,378

The statement of financial position is not accurately reported if assets are held at amounts greater than their recoverable amounts. While the PFMO contains specific requirements for amounts to be written off to be approved by the House of Assembly it does not contain any similar requirements for amounts to be provided for in the financial statements prior to House of Assembly approval of the write-off.

Part XI Section 52 (5) of the PFMR states that the *“statements to be provided include but are not necessarily restricted to those contained in Schedule 2 to the Ordinance; and this is because the fundamental requirement is to ensure that the financial position of the Government is fully disclosed to the House of Assembly; and therefore the Accountant General shall provide such other accounts or provide such additional information as he or she considers necessary to achieve this objective.”* This forms the basis for the overarching need for TCIG’s financial statements to reflect fully its financial position.

Accounting officers must recommend, where appropriate, adjustments against the carrying value of assets. These adjustments should be reflected as provisions for impairment against the carrying value of the term deposits.

By providing against the carrying value only, no write off has occurred, simply a provision to more accurately reflect in the reported financial position the estimated recoverable value of the asset. At the appropriate time, approval should be sought from the House of Assembly for write offs. In the case of TCI Bank Limited, this would likely be at the conclusion of the liquidation process.

6.2 Significant assets with an estimated value of \$50M not recorded in financials - HR

Property, plant and equipment, investment property, intangible assets and infrastructure assets are not recorded in the financial statements in accordance with GAAP to reflect an accurate representation of TCIG's total assets.

Per a Ministry of Government Support Services listing there are approximately 169 buildings owned by TCIG, with a conservatively estimated value of \$50 million, throughout the TCI such as schools (secondary and primary), office buildings, community centers, clinics, houses and other properties. Some of these are owned by statutory bodies. The listing provided contained parcel numbers and status of the buildings but did not provide valuations for any of the properties.

There are also some other capitalisable assets that are also not included in the financial statements and include, but are not limited to, the following:

- Carnival Infrastructure Projects \$225K
- Helena J. Robinson (HJR) High School – new block \$880K, complete and furnish new block - \$1.2M
- New Block at the Ona Glinton Primary School - \$2.1M
- New reverse osmosis (RO) plant and equipment \$830K and \$668K (completing the new RO plant)
- New vehicles for the Police - \$815K
- NJS Francis Building acquired from the NIB during FY 2012/2013 for US\$5.9M plus US\$385K of furniture and fixtures
- North Caicos Deep Harbour land acquisition \$1.6M
- Repairs to the Causeway Bridge \$966K and continued work on the Causeway Bridge - \$1.5M
- South Caicos Community Centre \$136K

The omission of such significant assets reduces the meaningfulness of the accounts (in particular in years where there are major asset additions or disposals (e.g. crown land sales or major capital works)). There is also a higher misappropriation risk while recording is weak as unrecorded assets may be sold off at a 'loss' compared to their value while reporting a 'gain' on sale in the statement of financial performance due to no carrying value. This is a major issue especially because land, in particular, has allegedly repeatedly featured in sales at below market value, transferred at \$0 value, or acquired via illegitimate or unethical means and / or stamp duty is not paid in full. It represents huge potential losses to TCIG if not accurately monitored, recorded and tracked. Also, due to the lack of monitoring of assets, no real account is taken of maintenance costs for all assets which can impact budgeting accuracy.

TCIG should carry out a valuation of all its assets, even on a piecemeal basis. GAAP requires that valuations/revaluations should be carried out with sufficient regularity. This has been a repeat audit item. It is recommended that the asset register be progressed immediately and, over the medium term, bring the assets onto the statement of financial position together with appropriate note disclosures.

6.3 \$2.5M Belize Bank / British Caribbean Bank (BCB) account not clarified – HR

In an effort to write-off a \$2.5 million bank account balance reported in TCIG's general ledger as held at BCB, journals of totalling approximately \$86 million were posted. While the supporting documentation for these journals covers the investment movements into, and out of, the account, it does not cover the other deductions from the account including where the associated expense entry was posted (refer below). Additional supporting information, including bank statements and expense account entries are required. There are also two (2) credit memos, one when the account was opened for \$1,603,000 and another for \$14,427,000 as well as a "Ck Deposit BBL" for \$13,000,000 that need to be traced back to the source documents.

Table 11 – Extract of some transactions from the Belize Bank Account

Date	Description	\$
21-03-2007	Debit memo	2,500,000.00
22-05-2007	Debit memo	5,000,000.00
03-07-2007	Debit memo	5,000,000.00
19-07-2007	Debit memo	3,000,000.00
25-07-2007	Debit memo	3,000,000.00
20-08-2007	Debit memo	5,000,000.00
31-08-2007	Debit memo	5,000,000.00
04-10-2007	Debit memo	1,000,000.00
22-09-2006	Credit Memo	14,427,000.00
19-07-2007	Ck Deposit BBL	13,000,000.00

Overall, if the general ledger accounts reported an asset of \$2.5 million, but the bank account has no funds, then the balance presented in the general ledger must have been used for something that was not recorded. The expenditure of these funds could not, therefore, seemingly have been recorded in the statement of financial performance. It is an error, omission or fraud.

Given the above I am not satisfied that this write off is clarified at this stage. As soon as pertinent evidence is obtained that the transactions from the bank account are verified together with the

corresponding transactions in the general ledger, the remaining amount which was not accounted for in TCIG's books should be examined in detail.

All Journals totalling \$86,017,664 (Ref. 2012/13 Audit Report – Adjusting entries discovered after the reporting period) should be reversed until such time as the error, omission or fraud is detected and/or the House of Assembly gives approval for a write-off.

This exemplifies the critical importance of strong internal controls and accurate financial reporting.

6.4 Prior Year Adjustments of \$5.8M between 2011-2014 not properly accounted for – HR

Prior year adjustments were made of \$4.6M (net) in 2011/12 (refer below), \$1.1M (net) in 2012/13 (refer below) and \$81K (2013/14). These changes have been made without proper disclosures and, where applicable, appropriate retrospective adjustment (for errors and changes in policy), or current year adjustment (for changes in estimates). The changes impact several statements of financial position and financial performance accounts.

TCIG should re-examine the treatment it has adopted for prior year adjustments, in particular when the prior year adjustment is material. If the prior year adjustment is material the accounting and disclosure requirements of IPSAS 3.54 need to be met.

In addition, if the adjustments involved the write-off of assets of TCIG it should be determined whether the appropriate House of Assembly approvals were obtained.

Below is a summary of the net adjustments in 2011 and 2012. Sufficient supporting documentation, together with the reasons for the adjustment was not provided.

Table 12 - Prior year adjustments

2012/13 Adjustments to prior-year balances	Amount (\$)
Adjustment to TCI payroll clearing account	480,890.93
Adjustment to correct staff advances balance	(16,980.13)
Adjustment to correct loan balances	684,509.56
Adjustment to correct bond repurchase balance	5,381.09
Adjustment to correct hypothecated account expended	(201,760.33)
Adjustment to correct value of paid up shares held with CDB	422,713.58
Adjustment to correct entries to Crown Agents bank	(51,261.44)
Adjustment to correct entries to Belize Bank/BCB	(2,425,638.63)
Total Net prior year adjustments for 2012/13	(1,102,145.37)

2011/12 Adjustments to prior-year balances (assets and cash balances)	Amount (\$)
Adjustment for net receipts against expenses held in cash accounts	2,200,776
Adjustment for salary expenses held in bank accounts	(481,465)
Adjustment for non-salary expenses held in Crown Agent bank accounts	200,100
Adjustment for Prior Year (PY) project expenses held in advance accounts	465,155
National Health Insurance set up costs held in advances accounts	1,755,692
Adjustment for special security expenses held in advance accounts	52,954
Adjustment for PY utility bills held in advances accounts	784,940
Adjustment for PY travel expenses held in advance accounts	141,759
Adjustment for PY non-salary recurrent expenses held in advance accounts	211,440
Adjustment for property loan balance	2,593
Adjustment for PY non-salary recurrent expenses recorded in accounts payable	(765,164)
Total Net prior year adjustments for 2011/12	4,568,778

6.5 TC Invest loans not properly reflected in TCIG's Financial Statements - HR

On October 1, 2012 TCIG brought into its books certain assets (net value of \$4.2 million) previously owned by TC Invest. Certain loans determined as non-performing were sold to TOLCO.

An analysis was performed by the NAO which compared the latest available audited financial statements of TC Invest as at 31 March, 2010 to the amounts brought in by TCIG on October 1, 2012. **Differences were identified. The differences appear to be, based on limited information, between the reported values of the loans per TC Invest and the value TCIG brought the loan into their books at.** There should be an analysis of the movement in TC Invest assets between April 1, 2010 and September 30, 2012 to determine the reasons for the changes and to ensure proper rules-based accounting was used to bring these into TCIG's books.

Table 13 – TC Invest Mar 2010 Audited Fin. Stats. vs. Sept. 2012 TC Invest unaudited Fin. Stats.

	March 2010 Audit	Unaudited September 2012
Cash and Cash Equivalents	861,312	2,373,366
Fixed Assets	1,326,760	-
Loans Receivable	24,277,782	14,683,475
Outstanding Loans/Debts	(18,456,592)	(12,828,097)
Net Assets Introduced	8,009,262	4,228,744

It appears that accrued interest due on the TC Invest loans was possibly removed prior to transfer to TCIG. It has not been possible to confirm the amount removed but, if this interest was due, then

it should be, at a minimum, tracked. A lack of rules-based accounting impacts the reliability of the financial statements.

The inclusion of TC Invest balances in 2012/2013 should have had far greater disclosure including a line by line summary of the assets and liabilities taken on by TCIG, the basis on which the assets and liabilities were included (e.g. book value, fair value etc.) etc. In addition there should have been far greater disclosures on the sale and purchase agreement for the identified non-performing loans with TOLCO, including the terms and conditions.

Also, while there was a review initiated by TCIG in the 2014/15 period on the accuracy of reporting of loans sold to TOLCO, it is important to ensure key monitoring checks are being performed by TCIG on the continuing accuracy of reporting by TOLCO, such as whether interest continues to be charged on the portfolio by TOLCO and, if so, who is entitled to the interest charged and whether, if securities were provided on loans included in the portfolio, appropriate insurance coverage is being maintained by the borrower or TOLCO to protect the value of the security. **There is a potential loss of revenue for TCIG if the returns provided by TOLCO are not examined for accuracy and completeness and/or if interest is still able to be charged, and collected, on some of the loans in the portfolio, and TCIG has retained a right to some, or all, of that interest. There is a potential loss of the value of the realisable security if it is not properly insured and an event happens to reduce the value of that security (for example a fire).**

6.6 No proper due diligence or tendering procedures followed in relation to non-performing loans – HR

In 2012/13 loans identified as non-performing were sold to TOLCO. A timeline of circumstances surrounding this sale were as follows:

1. 30 July, 2012 – TOLCO was registered/formed
2. 31 August, 2012 - A Sale and Purchase Agreement (SPA) between TCIG, Turks & Caicos Islands Investment Agency (TC Invest) and TOLCO was entered into for the sale and purchase of identified non-performing loans due to TC Invest
3. 30 September, 2012 - TC Invest was dissolved and TCIG agreed to accept the rights and obligations of TC Invest under the SPA
4. 3 October, 2012 – Ordinance 33 of Public Procurement Ordinance was made on this day.

The non-performing loan portfolio sold by TC Invest to TOLCO was listed as \$7.7M. The purchase price payable by TOLCO (buyer) to TC Invest (seller) was 40% of all loan capital and interest received/collected. There was no up-front payment. TC Invest retained beneficial ownership in 40% “of the land shares created by the Security Documentation in relation to the Portfolio”.

Table 14 - Non performing loans sold

Original Principal	Balance Outstanding	Interest Balance	Other charges	Total Balance (amount sold)
6,139,655.07	6,235,962.54	1,435,100.74	74,130.54	7,745,193.82

*It is not clear how the valuation was determined.

Only 40% of the total receivable balance was recorded in TCIG's accounts i.e. \$2.8M. However, this amount is approximately \$250K less than 40% of \$7.7M. If TCIG were operating on a consolidated basis, the full amount should have been recorded as a receivable in TCIG's books. Given the materiality of the remaining 60% it would have been advisable to recommend these amounts for write off to the House of Assembly.

TCIG receives a detailed statement of collections from TOLCO along with its quarterly payment. As at 31st March, 2014 a total of approximately \$92K was received from TOLCO. The funds collected by TOLCO and shared with TCIG so far appear to be in the ordinary course of collections and not by way of foreclosure sales.

I have expressed serious concern with this arrangement particularly since 2 of the 3 directors of a company owning 42.5% of TOLCO either have been or are the subject of a series of alleged questionable dealings in relation to fraud, accounting improprieties among other matters. **Reputational risk is therefore considered high and should be considered in relation to the SPA.**

A proper process was not conducted to ensure that the owners were experienced and specialized in debt recovery. No proper due diligence was done to ensure that there was no conflict of interest or at a minimum have any conflicts declared. No proper due diligence was done to ensure that the companies with whom TCIG representatives engage in have a good reputation especially in large commercial contracts.

After interviewing several key officers and reviewing several documents, recommendations were made and action is being taken. The whole transaction should be evaluated and accounting entries corrected where necessary in respect of these transactions to accurately reflect the commercial arrangements per the SPA either by write-off, bad debt or discounting.

Far greater attention should have been paid in executing any agreement of this magnitude and required far greater scrutiny than other standard agreements, if only for the sheer value of the

amount. The signatories to the agreement should have paid greater attention to this transaction including the purchasers who would have considered entering into this type of arrangement.

It is recommended that a mechanism (checklist) of activities/tasks must be completed prior to signing off on large contracts. TCIG should also ensure criteria for the performance of the particular service contract is properly evaluated prior to execution. Consideration should also have been given to following some form of tender procedure, irrespective of whether the Public Procurement Ordinance was yet to be in effect.

A review was initiated by the NAO during 2014 and a further full special audit is anticipated to be done in the upcoming period. Included in this review will be using the rights, under section 3.3 of the SPA, for TCIG to, at its own expense, have an independent annual audit of the collections received.

The signed SPA was 60% in favour of TOLCO and 40% for TCIG. Another option mentioned to TCIG representatives was to recover the debt at a cost of 15% plus letter writing fees, with the balance for TCIG. During our enquiries, it was indicated that this would have resulted in repayment over a longer period of time and the objective was to get this debt off earlier rather than later. This should have been considered in relation to the other options.

Consideration should also have been given to following some form of tender procedure such as the old Financial Instructions Chapter 17 and 18 on Tendering or the upcoming Public Procurement Ordinance, which were passed very shortly after the sale on 3rd October 2012.

6.7 Inconsistency in inventory values by \$1.1M – HR

Due to lack of resources the NAO was unable to perform physical verification of stores throughout TCIG and instead relied on the information provided by the Board of Survey 2014 (BOS). A review of the BOS information, TCIG's 2013-2014 first draft financial statements and supporting documents revealed the following:

1. Note 17 (Inventories) of TCIG's first draft financial statements for 2013-2014 disclosed total inventories of \$580,937. Per the BOS documentation total inventories were \$1,694,614. Included in the BOS total, but not in Treasury's supporting statements, were various stocks of text books and stamps sold by schools and post offices throughout TCI totalling \$1,113,677. This has since been corrected.
2. Accounting Officers for the following ministries did not provide Treasury with complete and accurate information for stores within their ministries and departments:

Table 15 – Difference between Statement of Unallocated Stores and Board of Survey information

Ministry	Statement of unallocated stores and other assets 2013-2014	BOS March 31, 2014	Difference
	\$	\$	
GSS	502,001	1,561,629	1,059,628
Education	6,083	60,030	53,947
Finance	-	72,956	72,956

6.8 Losses not managed in compliance with regulations – HR

According to Section 17 of the PFMR cash losses are losses of cash by fraud, theft, errors, omissions, uncollectable arrears of revenue or other irregularities, including unauthorized or excess payments. Based on this definition, the statement of losses needs to be revised to incorporate uncollectable arrears of revenue. As previously identified TCIG has historically reported some large arrears including approximately \$19.3M in scholarship fund contribution arrears and \$38.2M in business licence arrears. These two large amounts need to be reviewed for accuracy and recoverability.

The total reported TCIG losses of public money and stores for 2013-2014 were \$14,538. This included unpaid Christmas Advances for waged staff of \$1,731 (GSS), loss of a laptop valued at \$800 during business travel valued at \$800 (Ministry of Education) and the loss of various stores and equipment valued at \$4, 157 (Ministry of Health).

The Judiciary provided a nil losses return to Treasury however, during June 2013 there was loss of cash totalling \$13,088 at the Magistrate's Court in Provo. The absence of a loss register, as required by PFMR 15(2), at the Judiciary was highlighted when NAO reviewed the controls after the loss at the Magistrates Court in Providenciales. Loss registers were also not maintained as required at the Ministry of Education and the Royal Turks and Caicos Islands Police Force. The Accountant General's Office did not maintain a Register of Losses for 2013-2014 for all TCIG losses as required by PFMR 15(1).

6.9 \$1.2M outstanding checks not cleared by Nov 2014 – HR

One of the bank reconciliations included \$6,945,995 of outstanding checks processed in March 2014 that had not cleared the bank account by March 31, 2014. Based on the limited work performed US\$1,186,148 of these checks had still not cleared the bank by November 2014, 8 months later. The bank reconciliation also included \$138,308 of outstanding checks processed prior

to March 2014 that had also not cleared the bank at March 31, 2014. Based upon the limited work performed, \$71,144 of these checks had still not cleared the bank by November 2014. **Included in the checks remaining uncleared by November 2014 were some very substantial amounts including, but not restricted to, \$520,691 (March 2014 check) and \$37,944 (December 2013 check) to one company, \$98,000, \$25,320 and \$6,500 (all March 2014) to one supplier and \$73,650 to another supplier.**

The cause is not known. It is possible that the checks were cancelled and subsequently reissued however an explanation was not received in the required timeline. Based on how TCIG currently accounts for expenditure, expenses are recognised at the time checks are processed or cash is paid. Unlike accrual accounting, this method of accounting increases the possibility that checks are processed early, or late, to ensure that a transaction is recorded in a certain time period rather than in the period to which it should relate. Checks not banked within 6 months become stale and have to be re-issued which can further complicate matters especially for the larger material amounts.

6.10 Stamp duty receivables not recorded – HR

In 2010 TCIG provided the opportunity to pay stamp duty in four (4) equal instalments. The instalment payment option was removed in 2013 via amendment to the Stamp Duty Ordinance. While requests for information as to how many took up the instalment option were not made, it would be likely that some persons would do so. On the assumption that some did take up the instalment option it would be expected that TCIG would have recorded the instalments still due as an asset as the underlying transaction giving rise to the liability by the purchaser, being the asset purchase, had already occurred thus giving TCIG the right to receive stamp duty, however, no receivables have been recorded for stamp duty still payable by instalments at March 31, 2014. As stamp duty payable by instalments is not recorded as an asset by TCIG there is an increased risk that amounts due are not collected on a timely basis, if at all, and / or penalties established under the Ordinance are not enforced. **In addition, any stamp duty payable by instalments that is written off may potentially not go before the House of Assembly as the asset was not recorded in the accounting books and records as a receivable.**

6.11 Staff loans not managed in compliance with the PFMR – MR

A review was carried out on 283 staff loan and advances accounts for the period 2013-2014 to ascertain whether they were in compliance with PFMO 32 and PFMR 81, 82 and 83. The results of the review are as follows:

- a) No advance warrant was prepared and approved for advances during the year ended March 31, 2014 as required by PFMO 32 (b) and PFMR 81 (1)

- b) All advances and loans issues during the year ended March 31, 2014 were not retired. The staff advance account balance at March 31, 2014 was \$66,606 which included unpaid advances and loans totalling \$55,696 (twenty-nine (29) loans and advances) from the previous financial year (2012/2013)
- c) There were thirty-one (31) advances totalling \$64,143 with repayment periods more than the maximum three months as required by PFMO 32(b)
- d) Six (6) employees were issued advances during the year that had not repaid their outstanding balances for previous loans and advances
- e) Twenty-two (22) employees were issued more than two advances/loans during the financial year
- f) Unpaid TCIG Christmas Advances from the previous year (2012) totalled \$5,388. At least three (3) persons with outstanding Christmas Advances totalling \$4,100 had left the service
- g) An ex-employee of TCIG had an outstanding balance of \$55,930 at 31st March, 2014. The ex-employee entered into a payment plan whereby they are required to pay TCIG \$750 per month until the balance is repaid. The total repayments for 2013/2014 were \$1,700 when the amount that should have been paid per the payment plan was \$9,000

6.12 Travel advances not managed in compliance with the PFMR – MR

There were nine transactions where officers approved at level one or level two their own travel advances totalling \$15,194.94.

Ministry	Exception \$	Number of exceptions
Governor's Office	4,064.40	3
Attorney General's Chambers	10,030.54	4
Ministry of Finance	1,100.00	1

Claims retired to Treasury were compared to transactions in general ledger account 32401 (International Accommodations and Subsistence) to ascertain whether all claims were reviewed by Treasury. The results of this review are seen in the following table:

Table 16 - Travel claims retired compared to not retired

Ministry	Subsistence Total	Claim retired to Treasury	Claims not retired
Governor's Office	7,929.40	1,000.00	6,929.40

Police	26,182.63	350.00	25,832.63
Attorney General's Chambers	34,286.81	3,200.00	31,086.81
Judiciary	2,734.00	-	2,734.00
Office of the Premier	65,239.87	21,755.00	43,484.87
Ministry of Border Control	10,100.00	2,400.00	7,700.00
Ministry of Environment	4,725.00	800.00	3,925.00
Ministry of Government Support Services	18,250.00	1,540.00	16,710.00
Ministry of Finance	55,613.58	17,258.04	38,355.54
Ministry of Health	20,972.80	-	20,972.80
Office of the Deputy Governor	20,062.17	8,150.00	11,912.17
Ministry of Education	9,663.58	-	9,663.58
Office of the Director of Public Prosecutions	7,800.00	2,800.00	5,000.00
Totals	283,559.84	59,253.04	224,306.80

In addition the following points were noted:

1. Total subsistence paid from general ledger account 32404 (Minister Travel Allowances) for the year to March 31, 2014 was \$40,768 compared to total claims submitted to Treasury for review of \$5,600
2. There were twenty-four (24) subsistence transactions totalling \$18,823 that did not have Chief Executive Officer approval attached to the SmartStream invoice
3. A review of the claims retired file at the Treasury revealed the following:
 - a) Forty-nine (49) travel advance claims were reviewed by Treasury out of approximately 209 travel advances issued
 - b) One (1) Officer received an advance of \$3,500. The officer incurred expenses totalling £2,465.52 and was therefore required to retire the balance of \$1,034.38. The exchange rate was not considered when reviewing the claims
 - c) One (1) officer received an advance of \$800. They retired \$410 but did not provide receipts to support the expenses incurred
 - d) There were five (5) claim totalling \$3,626.46, £1,281.20 and BDS\$1,152.36 where receipts supporting the claims had the total outstanding but the claims were processed by Treasury
 - e) In one (1) case the receipt attached to an officer's accommodation claim had been altered by changes to the figures on the receipts
 - f) In at least five (5) cases officers were reimbursed for expenses incurred over and above the DSA in contravention of section 15.4 of TCIG's travel policy
 - g) An officer was issued a travel advance of \$3,000. Included in their subsequent expense claim was non-business related expenses, such as an Apple adapter (\$52.57), clothes (\$37.79) and make-up (\$91.89). The officer hotel bill was also overstated by \$222

4. Twenty-nine (29) transactions were tested to ascertain whether public officers submitted their expense claims and receipts, and repaid any surplus, within 15 days upon return as stipulated in section 15.8 of TCIG's travel policy. The results of the review were as follows:

Time	Within 15 days	Between 15 days and 2 months	Between 3 and 4 Months	Between 7 and 8 Months
No.	4	19	4	2

A request was made to the Office of the Premier for the published overseas travel report at the end of the financial year including overseas travel of the Governor, Premier, each Minister and Senior Government Officers, and the Chairman and Chief Executive Officers of Statutory bodies, as required by Section 12 of TCIG's travel policy. As at the date of this report this information had not been provided for review.

5. Travel Registers were reviewed for the following ministries. The results of the review were as follows:

- Ministry of Health and Human Services - Did not have date of retirement of advance or the receipt number for any retired amount
- Ministry of Finance – Complete and accurate, it contained relevant information to enable monitoring of travel and to ensure that advances are retired
- Ministry of Environment – Did not contain dates for retirement of advance, receipt numbers for amounts retired to Treasury and payment dates
- Office of the Premier – Travel advance information was not entered for three officers (entry contained officers names, dates of travel destination, airline but did not contain amount of advance issued, total travel expenses and amount retired to Treasury). Also it did not record date of retirement of advance and receipt numbers for items that were retired

7. LIABILITIES

7.1 Consolidated financial statements are mandatory under IPSAS 6 or IPSAS cash basis - HR

TCIG's financial statements currently only include the financial performance and financial position of the Government and do not include the financial performance and financial position of all entities it potentially controls, either directly or indirectly. IPSAS 6, *Consolidated and Separate Financial Statements*, and IPSAS cash basis of accounting require consolidation. TCIG should examine whether, under IPSAS 6 and/or the IPSAS cash basis of accounting, it meets the requirements for consolidation and, if so, whether it should include in its financial statements the financial position and financial performance of the statutory bodies and other entities controlled.

TCIG does not currently have a complete overview of the Government's financial performance and position. At present, the best available information on the Government's financial position is provided by the annual financial statements of the Consolidated Fund, but these are incomplete. These statements only aggregate the operations of Government ministries. They do not incorporate the considerable operations of statutory bodies. A complete overview can only be achieved by aggregating (consolidating) the financial statements of all Government's public funds and controlled organizations. It is therefore currently extremely difficult for an interested party to understand the full extent of Government's revenues, expenses and its financial position. Increasingly third parties, such as credit rating agencies, lenders etc. need to understand the full Government position, including statutory bodies, to prepare their reports appropriately. In order to take into account the non-consolidation of controlled entities TCIG is having to adjust its reported financial position and financial performance by the inclusion of certain controlled entities when presenting its financial information to these third parties. This would not be required if a consolidated financial position and performance was reported.

Significant financial activities of Government occur outside the Consolidated Fund. TCIG could potentially take advantage of the non-consolidation by raising or reducing taxes/fees/charges via statutory bodies with no impact on revenues reported by TCIG as these are not currently reported in TCIG's financial statements. In addition, TCIG could use statutory bodies to borrow additional funds without any impact on the reported financial position of TCIG, as the loans are not included in any form of consolidated position, or make payments on behalf of TCIG without any impact on the reported statement of financial performance.

For example the TCIG financial statements do not currently include:

- TCI Airports Authority - Revenue of US\$26.4M (per 2013 audited financial statements)
- TCI National Health Insurance Board - Revenue of US\$26.1M (per 2014 audited financial statements)

- TCI Financial Services Commission - Revenue of US\$8.4M (per 2014 audited financial statements)

The revenue for these three statutory bodies alone totals US\$60.9M, or 29.5% of the reported revenues of \$206.8M for TCIG for the year ended March 31, 2014.

Even if consolidation is not required under IPSAS 6, TCIG should consider the benefits of a high level consolidation (total revenue, total expenses, assets (with cash separately identified) and liabilities (with loans separately identified)) as part of their standard reporting procedures.

7.2 Proper accounting treatment required for the \$116M Hospital PPP - HR

According to TCIG's Framework Document 'public borrowing' includes;

- conventional borrowing from commercial and concessional institutions;
- the capitalised value of all alternative financing transactions (including PFI/PPP arrangements) that will place future financial obligations (in terms of increased expenditure or reduced revenue) on TCIG;
- the risk weighted debts and PPP/PFI arrangements of statutory bodies;
- borrowing that is contracted by TCIG, but then on-lent; and
- any other debt guaranteed by TCIG

In addition, according to the 2013/14 FSPS, *"the capitalised value of all alternative financing transactions (including PFI/PPP arrangements) that will place future financial obligations (in terms of increased expenditure or reduced revenue) on the Turks and Caicos Islands Government will be recorded by the government as public debt."* It was also noted that public debt includes per this statement totalled \$398M, of which \$115M was referred to as "PPP – Hospital Debt "Various Lenders".

Further the PFMO Section 30(8), (10), (13), (14), and Section 69(1) should be considered in establishing the proper treatment of the PPP from an accounting and legal standpoint.

TCIG currently has a major PPP in respect of the construction of the hospitals located in Grand Turk and Providenciales (the Hospital PPP). This contract impacts both the current financial year but also the obligations of TCIG for approximately the next 20 years. The notes to TCIG's 2013/14 financial statements include some references to the PPP however we were not able to verify these as they were provided outside our fieldwork timeline.

Due to the significant size of the Hospital PPP there is a risk that, if the current accounting was not deemed to be accurate, very material changes would be necessary to TCIG's financial statements

which, if made, may influence the users of the financial statements. Certain users of TCIG's financial statements are already separately adjusting them for the impact of the PPP. This should not be the case. The FSPS is also being adjusted to take into consideration the PPP obligations.

An independent accounting and legal opinion should be obtained as to how the Hospital PPP should be accounted for under IPSAS. TCIG should consider this opinion and the impact on TCIG's financial statements. If at all possible TCIG should amend its accounting to agree with the accounting requirements given in the independent opinion. There should be a level of reconciliation or reporting between the accounting for the Hospital PPP in the financial statements and the required inclusion of PFI/PPP liabilities as public debt in the FSPS.

In addition, the limited disclosures in the first draft 2013/14 financial statements were inaccurate. They indicated \$67.5M of construction costs and \$13.1M of ring-fenced equipment. However, the total hospital debt is in the vicinity of \$116M.

Revised figures were provided, as noted below, but validation and a proper review of these figures is required to ensure their integrity and reliability. As these figures were provided late in the audit process they could not be validated or verified. However, they must be highlighted in the audit report, particularly as there were significant differences reported year over year as noted in Table 17. The unreported or undisclosed difference was \$37.3M when compared to last year's financial statements.

Table 17 – Comparison of reported hospital project costs between 2012/13 and 2013/14

Hospital Project Costs	Providenciales Location US\$	Grand Turk Location US\$	Both Locations US\$	Total \$ 2013/14	Total 2012/13	Unreported difference
Pre-construction costs	6,788,191	3,394,095	-	10,182,286		10,182,286
Hospital Building	38,572,650	28,437,351	-	67,010,001	65,500,000	1,510,001
Equipment - Medical	6,922,263	3,361,392	-	10,283,655	10,283,655	-
Equipment - Information Technology	1,733,374	1,199,913	-	2,933,287	2,933,287	-
Project Management Fees	4,709,023	1,445,412	-	6,154,435		6,154,435
Professional Fees	2,805,657	2,071,950	-	4,877,607		4,877,607
Implementation Management Fees	816,769	388,055	-	1,204,824		1,204,824
Accommodations			3,600,000	3,600,000		3,600,000
Capitalized Interest	-	-	9,788,638	9,788,638		9,788,638
Total Hospital Project Costs	62,347,927	40,298,168	13,388,638	116,034,734	78,716,942	37,317,792

Estimates of Long Term Liabilities	1 Year to March 31, 2015 US\$	Years 2 - 5 to March 31, 2019 US\$	Over 5 Years to February 28, 2033 US\$	Total US\$
Unitary Charges	17,265,287	73,538,448	312,228,666	403,032,401
Total Unitary Charges	17,265,287	73,538,448	312,228,666	403,032,401

7.3 Inadequate contract management of health costs – HR

Whatever the potential value for money of a PPP finance deal when it is first entered into, subsequent poor management of the contract can result in higher costs, wasted resources, impaired performance and criticism.

PPP's generally come with common risks, including the risk of mismanagement and wastage of funds, inadequate rights to unanticipated profits arising from the exploitation of assets that is contributed to the partnership, the risk that contributed assets are disposed of by the partnership and avoidance of the partnership being classified as a public undertaking so as to limit public scrutiny. There is also the risk of unclear governance arrangements, dispute resolution arrangements may lead to exceptional privileges being granted, TCIG may not seek sufficient information to provide assurance on how the partnership is performing, PPPs may set up subsidiaries to perform some of its functions, making it more difficult for the public sector to monitor overall performance. There is the risk of early sell-off of the arrangement as returns on these types of financing arrangements are sold and transferred to others.

Information currently available indicates inadequate management of health costs overall and, in particular the PPP contract management has been weak and needs to be addressed.

Consideration should be given to the benchmarking of the construction costs to similar hospitals, in particular the cost of construction per hospital bed and the bed to population ratio. Due to the seemingly extremely high build cost and low bed to population ratio TCIG needs to re-examine the costs incurred.

7.4 Inadequate Treasury management – HR

Cash resources held by TCIG appear to be at levels substantially in excess of those required to maintain a suitable level of liquidity. At March 31, 2014 large cash resources (\$70.9M) are being held in low interest bearing accounts (0% to 0.4%) while interest is paid on loans totalling \$208M (excluding loans due by statutory bodies) at higher interest rates (0.9% to 8.75%). Total finance costs reported for the year ended March 31, 2014 were \$7.4M.

It is a requirement of the PFMO that cash resources are managed efficiently and cost effectively. If TCIG is not managing its treasury function effectively, both at a standalone and at a consolidated basis, there is an unnecessary expenditure of public funds. Funds saved could be used to increase public expenditure, increase debt repayments or reduce taxes/fees levied. Whilst it is recognized that a number of these borrowings may have early settlement penalties, and that appropriate consideration will also need to be given to the future repayment/refinancing of the HSBC Bonds in 2016, there would still appear to be very considerable scope for net finance costs to be significantly

reduced through the repayment of loans, in particular those with the highest interest rates, even taking into account any early settlement penalties.

There was a scope limitation on our work as loan agreements were not provided for review despite these being requested. It was not therefore possible to review the terms and conditions of the loans including redemption penalties (if any). For all future loans TCIG should ensure it negotiates early redemption terms.

7.5 Unfunded Actuarial Valuation of \$84.8M – HR

TCIG is responsible for various long term liabilities to its current and former employees, including House of Assembly members. Pension and gratuities paid in the year ended March 31, 2014 were \$4.9M of which pensions represented just under \$4M. Per the PFMO TCIG is required to ensure independent actuarial assessments of contingent liabilities, including pension and healthcare liabilities, are conducted every two years and the results are reported to the House of Assembly within two months.

While the future pension liabilities of TCIG were reduced with the introduction of the National Insurance Board in the early 1990s, there remained a high probability that the actuarial present value of its obligations was still a very significant amount based on the current pension expense of just under US\$4M per annum and continued obligations. It was understood that disclosure of the type of scheme (defined benefit or defined contribution) together with a breakdown of the short, long, medical, retirement and termination benefits was to be done. Not including pension liabilities on the statement of financial position also impacts the amount expensed.

A pension actuarial valuation report was eventually provided in early February, 2015 but this could not be substantially reviewed in time for the release of this audit. This actuarial assessment valued the unfunded liability as \$84.8M which confirms the NAO's position that this was a substantial TCIG liability. It also identified errors in several employee records. This needs a further detailed review which will be done.

7.6 Determination of creditors and timing of payments - HR

Due to the adoption of the modified cash basis of accounting there is no clear criteria for items that are included as accounts payable, contingent liabilities or excluded in full. When items are included in creditors, the associated expense is included in the statement of financial performance. Where items are included as contingent liabilities no expense is recognised in the statement of financial position.

Limited information was provided on the various amounts reported as creditors and contingent liabilities. It was not possible to determine, therefore, how it was determined claims would be classified. Based on the limited information received it would appear that items included in creditors could alternatively have been included as contingent liabilities and items included as contingent liabilities could have been included, in whole or in part, as creditors. **Information requested for audit must be provided on time to prevent scope limitation.**

A clear policy should be established as to what criteria need to be met for a claim to be included as a creditor and what criteria need to be met for a claim to be included as a contingent liability. Without a clear policy treatment of claims, and associated expenses, is open to interpretation.

Also, based on TCIG's method of accounting, there is an increased possibility that checks are processed early, or late, to ensure that a transaction is recorded in a certain time period rather than in the period to which it should relate, as under an accruals basis of accounting.

7.7 Insufficient audit evidence – HR

Sufficient appropriate audit evidence was not provided on time for a number of accounts. This included refundable deposits, loan agreements, creditors, contingent liabilities and actuarial valuations. A lack of sufficient audit evidence limits the scope of the audit procedures.

In addition, no deposits have been recognised for known liabilities. For example no liability has been recognised for repatriation deposits held on behalf of work permit holders. These are repayable to the employer upon evidencing that the employee has been repatriated. It is assumed that the repatriation deposits are included as revenue upon receipt which is not the appropriate accounting treatment as they are repayable once certain criteria have been met. The accounting adopted for other deposits paid is not in accordance with GAAP and should be examined and revised.

7.8 Unrecognised accrued interest payable – MR

Finance costs are recorded based on the actual interest payments made to creditors during that period. As a result interest due, but not yet paid, on loans outstanding as at March 31, 2014 was not recorded as a liability together with the associated interest expense.

In reporting periods with significant changes in the loan balances the interest expense reported in the statement of financial position may be materially misstated. Accounting for interest expense on a cash basis does not give TCIG an accurate picture of the total obligation of TCIG to lenders at the end of the reporting period or the associated interest expense for a particular period. We recommend TCIG modify the basis of accounting from cash to accruals for interest expense.

At a minimum TCIG should disclose in the notes to financial statements the outstanding interest which has not been paid at the reporting date. This will enable TCIG to make decisions based on more accurate information. It is also recommended that the full extent of the accumulated interest due and payable at the end of every financial period be included in the financial statements so that it is easier to report under the PFMO, Part V, Loans, Guarantees and Grants (Section 37 (4)) which requires full information on the extent on the total indebtedness by way of principal and accumulated interest.

8. DISCLOSURES

8.1 Non-compliance with Generally Accepted Accounting Practice – HR

Section 45 of the PFMO indicates that all public accounts shall be prepared in accordance with GAAP. The TCIG Public Financial Management Framework states that TCIG will ensure that public accounts are “*prepared on a timely basis in line with International Financial Reporting Standards and International Public Sector Accounting Standards*”. Also per the PFM Regulations Section 52 (5) **there is a fundamental requirement to ensure that the financial position of the Government is fully disclosed to the House of Assembly.**

It is not clear what GAAP is followed together with what departures, if any, there have been from that GAAP. IPSAS is the recognized GAAP for public entities. TCIG should therefore be looking to comply with IPSAS wherever possible with exceptions kept to a minimum and for valid reasons only. IPSAS only permits either the cash or accruals basis of accounting. Under either basis compliance is required with all of the requirements of the standards. The modified cash basis of accounting adopted by TCIG is not a recognised basis of accounting. However, there is the United States Other Comprehensive Basis of Accounting (OCBOA) which does refer to modified cash basis of accounting or modified accrual basis of accounting. **In summary, the financial statements must fairly represent the economic and financial position of TCIG.**

While the first draft financial statements presented on 31 July, 2014 recognise that they are not fully compliant with IPSAS they state that they comply with IPSAS as much as possible. This statement is not valid. To enhance the usefulness of the financial statements to the users of the financial statements use of IPSAS wherever possible is strongly encouraged. The statement was subsequently removed, but this point is left in here for emphasis.

A ‘departure’ from an accounting standard has a specific meaning in relation to financial statements. Under IPSAS a departure from a standard is considered a rare event and only in the circumstances that “*compliance with a requirement in a Standard would be so misleading that it would conflict with the objective of financial statements*” (IPSAS 1:31 (*Presentation of Financial Statements*)). When a standard is departed from there is significant disclosure required including “*the financial impact of the departure on each item in the financial statements that would have been reported in complying with this standard.*”

Given the above it is not considered that the accounting policies adopted meet the PFMO requirement to comply with GAAP.

It is not possible to comply with the TCIG Public Financial Management Framework requirements to prepare the financial statements in accordance with International Financial Reporting Standards

(IFRS) **and** IPSAS due to the divergence of these standards unless two separate financial statements are prepared. However, it is clear that compliance with internationally recognized accounting standards, be it IPSAS or IFRS, is intended.

Given the absence of a recognised accounting framework, such as IPSAS, the accounting policies selected are open to adjustment based on the requirements of TCIG and are discretionary. The financial statements are not comparable to other entities. The requirements of the PFMO to have financial statements that comply with the generally accepted accounting practice are not met. The basis of accounting excludes various assets and liabilities. This exclusion may impact effective stewardship of these assets.

Accurate and reliable financial information is critical to both accountability and decision making in the public sector. IPSAS are currently the only internationally recognized accounting standards for public sector bodies although it would also be possible to adopt IFRS to align the policies with those adopted by the statutory bodies. TCIG should examine all of its accounting policies for compliance with IPSAS. Where TCIG identifies accounting policies that are not in compliance with IPSAS a decision should be made as to whether TCIG intends to amend its accounting policies to ensure compliance and, if so, in what time period this change will be achieved, or whether the accounting policy will not change, in which case consideration will be given by the Auditor General as to whether the audit report will be modified in this regard.

There should be a managed transition to full IPSAS compliance even if transition to full accruals accounting is not achieved in the medium term.

8.2 Inadequate Basis of Accounting – HR

TCIG's financial statements adopt a modified cash basis of accounting. The modified cash basis is a method of accounting that utilizes both the cash and accruals basis of accounting. Subsequent discussions with Treasury indicate that it is a cash basis of accounting with some modifications. The actual modifications made, and the accounting policies adopted, were not clearly stated in either the first draft financial statements or the revised draft presented on 15 January, 2015.

The cash basis of accounting is inadequate to deliver the minimum financial statements as per Schedule 2 of the PFMO and in accordance with Section 45 of the PFMO which requires GAAP. Further the cash basis of accounting is not sufficient to meet the requirements under Schedule 2 of the PFMO which refers to assets, liabilities, commitments and contingent liabilities, arrears, advances etc. most of which would be non-cash type transactions.

In addition the cash basis of accounting, by itself, would not give the users of the financial statements, including the House of Assembly, crucial information for evaluating the TCIG's financial position and performance as required under PFMR Section 52 (5).

The cash basis of accounting is also weak when accounting for contracts straddling the year end as payments made may not accurately reflect the percentage completion of the project. Payments made be accelerated or delayed to meet, or avoid exceeding, budgeted amounts.

8.3 Risk of bad debts increases and non-approval of write-offs - HR

By adopting the cash basis of accounting there is a higher risk of bad debts increasing as debts may not be monitored as closely as they would be if they were included on the statement of financial position. In addition, by not including debts on the statement of financial position there is a high risk that the requirements of the PFMO for write-offs to be approved by the House of Assembly may be inadvertently by-passed. This is clearly evident with the revenue arrears.

8.4 Large number of issues presented in TCIG's financial statements – LR-HR

The first draft of TCIG financial statements presented by the Accountant General to the Auditor General on July 31, 2014 contained a large number of issues. These included, but were not limited to typographical errors, addition errors, unclear accounting policies and accounting treatments, classification errors, incomplete and/or inadequate disclosures and omission of accounts specifically required under Schedule 2 of the PFMO.

The second draft of TCIG financial statements presented by the Accountant General to the Auditor General on January 15, 2015 also contained a large number of issues. These issues were consistent with the issues identified on the July 31, 2014 draft.

It is not the responsibility of the Auditor General to identify the issues highlighted above. Rather, it is the responsibility of the Auditor General to provide an opinion on the financial statements as presented. In the interest of providing more meaningful financial statements the Auditor General worked with the Accountant General's office in highlighting the above issues. However, this resulted in additional time and costs for the Auditor General's office and a delay in the Auditor General submitting his report beyond the 4 month requirement of the PFMO, Section 48(3). The disclosures in the financial statements are incomplete but improving. As a result the users of the financial statements are not able to obtain all of the information that would be expected about the financial performance and financial position of TCIG.

There were a number of changes made that could not be audited by the Auditor General given the revised financial statements.

8.5 Inconsistency in the application of the basis of accounting – HR

TCIG's 2012-2013 financial statements indicated the use of a Modified Cash Basis of Accounting (MCBoA), which applies cash basis and accruals basis accounting depending on the types of transactions (both cash and non-cash), and compliance with IPSAS "*as much as possible*".

In addition, the MCBoA has been used for the last 6 years. TCIG has suggested that the basis of accounting should have been a cash basis of accounting, as modified to meet Schedule 2 of the PFMO. This is a fundamental error or misinterpretation which needs to be addressed.

It should be noted that for the 2011/12 audit both the cash basis and accruals basis of accounting was used together with IPSAS accruals basis of accounting standards 1-5, 14, 19, 23, 24 and 26 used. The cash basis of accounting was used instead of IPSAS 9, 12, 13, 17 and 21. The same basis was used for 2012/13 and intended to be used for 2013/14.

We cannot have frequent changes or interpretations in the bases of accounting which skew the comparative accounts. Rules-based accounting should be practiced which removes discretion. The flexibility to decide how a transaction is treated is not optional it is mandatory, it should be in accordance with TCI laws and should be in accordance with GAAP. The risk of material misstatement is therefore high and misappropriation of assets is high and should be addressed.

8.6 Non-transparent economic value transactions not recorded – HR

The cash basis of accounting is not sufficient to deal with non-cash transactions or events as these can simply not be reported. This does not provide an accurate picture of TCIG's financial performance or position. For example, there are many non-cash concessions (tax expenditures) provided to several companies and individuals which over the past 3 years have totaled over \$78.7 million that were only disclosed because they were identified during the 2012/13 Audit. It is conceivable that concessions given may have been between 20% - 30% higher than the reported amount because the system is weak and does not capture everything. Further some of the concessions may not have been justified and could have seen abuse of the concession granting mechanism.

Leases of crown land are another example in which the cash basis of accounting stops short of being able to record these transactions because they are non-cash events, yet lands are leased at "peppercorn" rents. Because they are non-cash it does not mean that TCIG has not given up economic value. In fact it is quite the opposite. Economic value has been given up with impending benefits which have not been measured or monitored and therefore may not be transparent it its award.

Similarly development orders which provide incentives, subsidies that are provided and debt forgiveness arrangements, are non-cash transactions which, when not reported, do not provide an overall true and fair view. The risk is increased significantly as these transactions are one-way transactions which benefit the receiver and there is no way to ensure that the transaction is above board and transparent. By reporting non-cash transactions these encourage transparency, reduce the risk of fraud and initiates value for money reviews and checks on compliance with laws and regulations.

We also have innovative types of agreements and transactions which, if left unaccounted for, can mislead users of the financial statements. Examples are the transfer of the non-performing loans under TC Invest to TCIG, the PPP in relation to the hospital contract and the non-recording/forgiveness of stamp duty on property transactions. These are the types of transactions entered into where the substance of the transaction may not be recorded due to the basis of accounting used.

Rules based accounting is strongly recommended.

There must be a fundamental recognition and shift in thought so that the focus should be on economic events and not only cash based events.

8.7 Lack of disclosure of related party transactions – HR

It is important to have systems and control to identify and disclose all related party transactions as they carry increased risk. The related party definition under GAAP is wide and includes a large number of persons such as personnel from the United Kingdom, House of Assembly members, Permanent Secretaries and other Accounting Officers. It also covers their close family members. Related party transactions are particularly important, albeit difficult, given the size of TCI. Currently there exist insufficient disclosures and inadequate controls to manage and monitor related party transactions. While there have been efforts to manage and disclose these related party transactions, it remains inadequate.

There were several transactions with statutory bodies that were not reflected in TCIG's books during the 2011 - 2014. Significant examples include, but are not limited to:

- the purchase from NIB of the N.J.S. Francis building including furniture and fixtures totalling \$6.285M;
- the granting of a licence to NIB to occupy the Honourable Headley Durham building with an agreed lease term for 999 years at a total cost of US\$1,327,808 (US\$1,257,808 to the building and US\$70,000 to the leased land);
- NIB agreeing to pay TCIG an amount of US\$3.15M in respect of interest accrued on the US\$6.15M paid to TCIG by NIB for medical treatment costs relating to employment injuries for the period from April 6, 1992 to March 31, 2010;
- TCIG agreeing to pay NIB US\$900,410 in respect of interest accrued pursuant to its lease of the N.J.S. Francis Building; and
- Forgiveness of surcharges due on NIB contributions of \$11,855,351 due to NIB amnesty.
- Further transactions not properly recorded.

Table 18 - Number of related party transactions between TCIG and Statutory Bodies

Description	2014	2013
Payment of Contributions to NIB	3,374,326	3,073,711
Not clear - Contributions – private sector	2,173,106	2,015,033
TCIG payment of contributions on behalf of civil servants	1,201,220	1,021,301
Rental payments to NIB	128,000	496,240
Receipts from Treasury bonds held with NIB	150,000	150,000

Interest payments	67,498	496,240
Purchase of the Hon. NJS Building	-	5,900,000
Receipt of interest on unpaid employment injury benefits in prior years from NIB	-	(3,150,000)
Purchase for acquisition of Hon. Headley Durham Building	-	(1,257,808)
Interest paid on unpaid rent in prior years	-	900,410
Payment for purchase of furniture and fixtures from NIB	-	385,000
Receipts for lease of crown land	-	(70,000)
Treasury bonds – at par	1,050,000	1,200,000
Interest payable	11,461	11,461

Other examples could be provided with other statutory bodies such as the NHIB (receivable from TCIG of \$1.764M, grants received from TCIG of \$18.5M, contributions towards clinical costs as directed by TCIG of \$24.8M and accounts payable of \$2.264M), the TCI Financial Services Commission (payable to TCIG of \$3,735,737 at March 31, 2014, paid to TCIG during the year of \$2,384,965) and the TCI Airports Authority (\$2M paid to TCIG in 2012/13 (being \$4M less than the budgeted amount of \$6M due to TCIAA taking over the airport fire services from TCIG)).

Related party relationships within the public service

A review of 108 statements completed by public servants for related parties and code of conduct compliance submitted revealed a number of issues which have to be further reviewed. The controls around these are weak and needs to be strengthened.

In summary, TCIG's financial statements do not currently include sufficient disclosures on related party transactions and balances, including those with key management personnel and their close family members as well as significant influence. Far greater transparency and accountability is needed in the area of related parties and significant influence.

8.8 Inadequate system to deal with third party payments and in-kind services – HR

International assistance agencies, donors and other parties may provide financial support to a recipient government in different form, in some cases cash in the form of grants. In other cases, rather than providing a recipient government with cash to acquire the resources it needs to undertake agreed programs or to repay debt, a donor may directly pay a supplier for the assets or services acquired by the recipient government, or may directly repay the debt of that government.

In these cases, the recipient government does not receive cash or make cash payments – rather, payments to settle certain of its obligations are made on its behalf by a third party (the donor).

There should be controls in place to capture these types of transactions or events which bring economic value to the TCIG. IPSAS requires that third party payments only need be disclosed on the face of the Statement of Cash Flows during the reporting period the entity has been formally advised that such payments have been made, or has otherwise verified their occurrence.

Third party payments and in-kind services, if any, are not currently disclosed by TCIG. The United Kingdom has funded a wide range of technical assistance in the key areas highlighted in the Commission of Inquiry report, including public financial management, crown land, public sector reform, legislative drafting, immigration and customs. Canada has provided and funded the Commissioner and Deputy Commissioner of Police for over 2 years. Whilst the FCO and DFID remain the two government departments most closely involved in the territory, other government departments (e.g. BIS, UKBA, MOD) have also provided invaluable resources. It is not sure if this support continues but if it does it's not recorded or disclosed. Also DFID utilizes CARTAC to provide training and other assistance to the overseas territories which should be disclosed.

Under IPSAS cash basis of accounting TCIG should disclose total external assistance received or paid during the period and total external assistance paid by third parties during the period to directly settle obligations of the TCIG or purchase goods and services on behalf of the TCIG. While there may be some disclosures, it is not sufficient to enable users of the financial statements to get a fuller picture. Disclosure of the significant classes of providers of assistance such as, for example, multilateral donors, bilateral donors, international assistance organizations, national assistance organizations or other major classes as appropriate for the reporting entity will identify TCIG's extent of dependence on particular classes of providers and will be relevant to an assessment of the sustainability of the assistance. This Standard does not require the disclosure of the identity of each provider of assistance or the amount of assistance each provides. However, disclosure of the amount provided by each provider in the currency provided is encouraged. Where an entity elects to disclose the value of external assistance received in the form of goods or services, it should also disclose in the notes to the financial statements the basis on which that value is determined.

8.9 Treatment of shareholding in Provo Water Company Limited – HR

IPSAS 7, *Investments in Associates*, requires the equity method to be used for all investments in associates in which an entity has significant influence. Under the equity method the investment is originally recorded at cost. The investment is subsequently adjusted at each financial reporting date to reflect the investor's share of post-acquisition changes in net assets of the Company.

Prior to its disposal in the financial year ended March 31, 2013, TCIG owned 46% of the ordinary shares of Provo Water Company Limited (PWCo.). TCIG accounted for its shareholding in PWCo. at cost, being US\$46 (being 46 shares at US\$1 each). Upon disposal of its investment in PWCo. for \$7,500,000, TCIG recognized a gain on disposal of \$7,499,954.

Failure to adjust the carrying value of the investment to reflect the post-acquisition changes resulted in TCIG not recording its share of the gains / losses in PWCo.'s financial position and performance in the period to which they related. In addition, upon disposal the gain reported was higher than would have been reported if IPSAS 7 had been followed. Failure to correctly account for investments in associates reduces the meaningfulness of the financial statements. In addition, it increases the risk that such investment may be disposed of without being recorded or recorded at under value. Also, in years of large gains or losses associated with the investment or in the year of disposal the results reported in the statement of financial performance are distorted.

TCIG should examine whether it holds any other investments which meet the criteria of IPSAS 7 and adjust its accounting policies to comply with IPSAS 7 for any such investments.

8.10 Material changes made between both drafts of the financial statements submitted – HR

The following changes to the balances presented were identified between the first draft financial statements, as presented on 31 July 2014, and the revised draft, as presented in January 2015. These changes were not highlighted to the Auditor General upon presentation. They also cannot be audited given the resubmission of the accounts on 15 January, 2015.

Statement of Financial position

- 2013 loans receivable – Increased from US\$12,687,311 to US\$12,768,253. Associated change to the note in the accounts
- Flow through of this change to net liabilities, consolidated fund and total fund balances

The purpose of this seems to be to amend the 2013 balance sheet for the impact of the prior year adjustment

Comparative statement of actual and budget

- Revised final budget figures
- Final budgeted revenue up by US\$4,000,000 to US\$213,989,267
- Final budgeted expenditure up by US\$1,055,701 to US\$191,279,168
- Resulting in final budgeted surplus up by US\$2,944,299 to US\$22,710,099
- Associated changes in the difference between actual and final budget column

Accounting policies / Financial Risk management – major changes to disclosures of policies

Statement of Stores and Other assets

- Increase in 2014 reported amounts from US\$580,937 to US\$1,738,732
- Increase represents GSS, up from US\$502,001 to US\$1,604,760 and the Ministry of Education, up from US\$6,083 to US\$61,119

Revenue Arrears

- Decrease in 2014 reported scholarship contributions from US\$3,241,887 to US\$3,236,887
- Increase in 2014 Ministry of Environment and Home Affairs from US\$nil to US\$673,258
- Overall increase in reported 2014 arrears from US\$14,570,326 to US\$15,238,584

Commitments and contingent liabilities- Overall decrease from US\$26,722,034 to US\$11,746,034 due to removal of SHN medical bills of US\$14,976,000

Losses of public money and stores - Overall increase from US\$14,538 to US\$27,626 due to new line item for judiciary of US\$13,088

Expenditure arrears, PPE, Comparative Information – notes removed

9. Sensitivity Analysis on Key Risk Areas

The table below represents a rough sensitivity analysis done on several areas in which risks exist.

Some of the risks identified are the risks of non-reporting and risks of under-reporting of revenues, risk of incorrect application of tariff rates, risk of non-payment of licence fees due, risk of recoverability of funds due, risk of concession abuse, risk of economic value lost, risk of over-payments, risk of omission, risk of error, risk of inadequate monitoring, contracts and treasury management. These are intended to give the readers a general understanding of the potential impact on areas where risks are identified.

Table 19 - Sensitivity Analysis on key risks areas

	Criteria	\$ Value	Risks	Risk Error %			
				1%	5%	10%	20%
VRBO's not registered	690 properties (at \$550 per night and a 50 % occupancy) using 12% rate	8,311,050	Not reporting	83,111	415,553	831,105	1,662,210
Hotel and Restaurant Tax	380 payees 264 have less than 12 receipts, 132 have less than 6 receipts. They report around \$770,000 per annum.	770,000	Not reporting	7,700	38,500	77,000	154,000
Stamp duty vehicles	Of the 30 payees, 8 have less than 12 receipts. Revenues received approx \$1 million (assume 8/30)	266,667	Not reporting	2,667	13,333	26,667	53,333
Hotel and Restaurant Tax		40,948,208	Under-reporting	409,482	2,047,410	4,094,821	8,189,642
Import/Customs Processing Fees/Fuel Tax	There are over 6000 tariff rates. Given the number of tariffs and marginal descriptions, a risk exists that incorrect application of the rates may occur or the importer opts for the lowest rate	52,701,565	Incorrect application	527,016	2,635,078	5,270,157	10,540,313
Business Licence	Specific category of professionals, lawyers etc.	361,800	Non payment	3,618	18,090	36,180	72,360
Revenue Arrears	Scholarship Fund	20,300,000	Recoverability	203,000	1,015,000	2,030,000	4,060,000
Advance deposits	Deposits for Students Accommodation (assume 100 students @ 750 deposit) over last 3-5 years	75,000	Recoverability	750	3,750	7,500	15,000
	Business Licence Arrears	4,600,000	Non payment	46,000	230,000	460,000	920,000
	Business Licence Arrears aging report (last 3 years)	12,000,000	Recoverability	120,000	600,000	1,200,000	2,400,000
Concessions	Consider minor concession changes	30,454,339	Concession abuse	304,543	1,522,717	3,045,434	6,090,868
	No. of entities receiving concessions 1650	1,650	Economic value foregone \$10,\$20, \$30, \$50	16,500	33,000	49,500	82,500
Travel	Consider managing travel	900,000	Overcharging	9,000	45,000	90,000	180,000
Repayment of Higher Interest Loans	TCI Bank Limited Loan	8,666,667	High Interest	86,667	433,333	866,667	1,733,333
	HealthCare loan	118,000,000	High Interest Rate Risk	1,180,000	Not reasonable to assume		
	Annual Operational Health Care Expenditure	25,000,000	Overcharging, Omission, Error etc., incorrect expenditure disclosure, inadequate monitoring and management	250,000	1,250,000	2,500,000	5,000,000
				\$ 3,250,053	\$ 10,300,765	\$ 20,585,030	\$ 41,153,559

10. NAO MANDATE & OBJECTIVES

The National Audit Office (NAO) is a governance institution established under Section 97(1) of the TCI Constitution. Its operational requirements are established under the NAO Ordinance dated 16th March, 2012. According to the NAO Ordinance Section 18(1) the NAO will report on the results of its examination and audit of TCIG's financial statements, as prescribed under Section 44 of the PFMO, and certify whether the accounts represent a true and fair view.

There is a general public expectation that an opinion is provided, taking into consideration the public accounts, risks, internal controls, compliance, regularity, propriety and value for money. The objectives of this audit are outlined in Section 49(1) of the PFMO and Section 18(1) of the NAO Ordinance.

The PFMO allows four months after the financial year end (March 31) for the presentation of financial statements by the Accountant General (due 31 July). It is my responsibility under Section 49(1) of the PFMO and Section 18(1) of the NAO Ordinance to then form an independent opinion, based on the audit, on those statements and to report my opinion within a further four months (due 30 November).

According to the NAO Ordinance, Section 7(2) and Section 18(1), in carrying out his functions the Auditor General shall do so through the application of internationally recognised auditing standards.

The NAO is required under the laws to examine, audit and certify where appropriate whether or not the accounts and statements represent fairly the financial position of TCIG and that it has been conducted with regularity and propriety. Further the NAO must ensure that reasonable precautions have been taken to safeguard the proper collection and payment of monies and to ensure that all expenditure to which such examination and audit relate has been lawfully incurred. The NAO is also required to assure the internal control system and internal audit services is adequate and that satisfactory management measures have been taken to ensure that public or other resources are procured economically and utilized efficiently and effectively.

This audit report was delivered beyond the reporting deadline due to staff losses and a request by this office for the Ministry of Finance to revise the financials taking into consideration some recommendations specifically in relation to the Financial Statements. These revised financial statements were subsequently submitted on 15 January, 2015.

11. NAO ACTIVITIES AND CHALLENGES

There were several compilation engagements and assessments conducted during the year and leading up to the formulation of the TCIG 2013/14 audit report. A shortage of staff prevented the NAO conducting proper audits of certain areas but we did manage to complete expenditure compilations for 12 departments, a vendor master file review, and reviews of the SmartStream approval process, fixed asset management, TC Invest and concessions. The IT Audit and contracts audit were deferred to 2015 together with a quality assurance review of the Sports Commission audit.

Statutory Body Audits

In order to deal with the additional requirements under Section 18 of the NAO Ordinance I have started working with local audit firms to establish agreed upon procedures to be able to form an opinion on this section for the Statutory Bodies. However, this will be on a phased basis. NAO involvement in the statutory body audits has, to date, been non-existent and therefore necessary work is anticipated to ensure that all 2014/15 statutory body audits can be delivered to the House of Assembly in accordance with Section 18 of the NAO Ordinance certification requirements, once qualified and experienced audit professionals are either recruited or retained from the audit firms to conduct these audits. NIB's 2013/14 Financials will be the first to be forwarded to the House once the Section 18 NAO requirements are met. I have inserted myself into the process and have already met with PwC and KPMG regarding the requirements and members of the NAO will be assigned to these audits in the coming months.

I will be concentrating my efforts on these statutory bodies over the next year to ensure that they are assessed for compliance, value for money and, with the assistance of Internal Audit Department, internal controls.

Statutory Body	Audits performed by	Years of audit outstanding	Comments
NIB	KPMG	Up to date	No attestation would be provided by the NAO unless the audit firm is <u>DIRECTLY</u> supervised by the Auditor General or <u>another qualified and experienced professional auditor conducts the work under the supervision of the Auditor General.</u>
Civil Aviation Authority	WB Financial	Up to date	Same as above.
NHIB	PwC	Up to date	Same as above

Airports Authority	PwC	Up to date	Same as above, A special audit is to be conducted in the airport expansion project.
Financial Services Commission	PwC	Up to date	Same as above
Telecommunications Commission	PwC	Up to date	Same as above
Ports Authority	SNG Financial	3 years outstanding	Engagement signed 31 st March 2014. Engagements completed by end Jan 2015. Further investigation is required into this statutory body.
Community College	-	Number of years outstanding	A joint effort between an external audit firm and NAO auditors will be made to complete several years of outstanding audits.
National Trust	PwC	Up to date	Requests have been made for another independent audit. NAO staff to undertake this audit.
Tourist Board	-	Number of years outstanding	An external audit firm will be appointed to lead this audit with NAO staff supporting the effort.
TC Invest	-	-	To check if this is a separate statutory body now.
Sports Commission	Ceased operations	5 ½ years – at Quality Assurance stage	A quality assurance review is required for this given the sensitive nature of this audit.

Administrative Areas in Progress

- Website development and Ethics Hotline – A website will be developed to place audit reports and encourage whistleblowing through an ethics hotline.
- A central server needs to be established separately to preserve confidentiality of the work that the NAO does. This is to be determined based on funding and office availability.
- An educational platform is to be established, evaluating alternative options available before a decision is made.
- Forensic audit tools are being evaluated. Forensic audit services are to be evaluated in relation to in-house development. This is critical. No development can take place without the proper organizational placement of the NAO.

- Intelligence gathering systems are being established. No development can take place without the proper organizational placement of the NAO.
- Audit software evaluations have been completed. Software to be purchased.

Approval for audit office in Providenciales

The audit and detection risks remain high in part because there is not a visible audit presence in Providenciales. Auditors are meant to be mobile. Approval was sought and obtained for the opening of an office in Providenciales. Given the high cost of opening the office it was agreed that the office would not be opened until staff had been recruited to occupy it which saved approximately \$8,000.

In a general consolidation of the assets, liabilities, revenues and expenditures of both TCIG and the Statutory Bodies, these total roughly \$1.325 billion requiring audit coverage (Assets \$400M, Liabilities \$300M, Revenues \$350M and Expenditures \$275M [approximations]). These amounts exclude significant long term debts and commitments, contingent liabilities and pension and other related liabilities. Including these would increase the amount to approximately \$2.5 billion. On this basis alone, direct supervision is required for all statutory body audits as envisaged in the PFM laws and therefore demands a permanent presence of both the NAO and Internal Audit Department in Providenciales. Institutions charged with acting in the public interest should also ensure that they have the capability, in terms of appropriate, competent, and knowledgeable personnel resources, to ensure that adequate audit coverage is achieved.

It is absolutely critical that the NAO and the Internal Audit Department are appropriately resourced to cover these areas and it is hereby acknowledged by the Auditor General that steps are being taken in the right direction to see that it is so.

Declaration

The Auditor General is authorized to work across the islands and relocated to Providenciales in 2013/14. This resulted in savings of approximately \$24,000-\$32,000 by limiting travel to Providenciales each week at a cost of approximately \$1,500 - \$2,000 per week (assuming 3 days in Providenciales). The challenge has been finding temporary offices for the Auditor General and the Deputy Governor and Audit Committee Chairman has committed to seeing what offices are available. It is hoped that this will be resolved soon as the majority of the audit work is done in the field across the islands and a minority, unfortunately, done at my home office. While I do not support this position it became necessary given the monumental task of completing the TCIG audit, a shortage of in-house qualified staff, a restriction on opening the office until 2 additional staff were recruited, a lack of government office availability, not being able to accept office space by external

audit firms due to potential conflict of interests, the need to control contract audit costs and it being a lower cost option. Consideration should be given as to whether it is reasonable to have 15 members of staff in the Internal Audit Department and the NAO combined, all based in Grand Turk and none in Providenciales.

Shortage of Staff

The NAO currently has a staff of 7. In the past the staff complement was around 17, but account must be taken of the creation of the new Internal Audit Department. The work required of the NAO, however, has quadrupled with the introduction of new laws to increase transparency, accountability and good governance, yet the staff required in the NAO has been significantly depleted. With the increased budget it is hoped that this will be able to attract much needed professionally qualified and experienced personnel.

The interpretation that the Auditor General cannot recruit his own staff to be able to independently operate is incorrect and is preventing this Office's development. One only need to look at the Cayman Islands Office of the Auditor General to note that it is a public office under the Cayman Islands Constitution yet they do their own recruitment and operate independent of the Government and statutory bodies. This must be dealt with as it can compromise the NAO's ability to properly complete its work.

Risk Assessment

The NAO Ordinance was created to allow operations independent of government and accountability was placed in the Governor and House of Assembly, not to the Public Service for recruitment of staff or Ministry of Finance for its funding.

There are a number of risks to which the NAO is exposed such as:

- confidential data being illegally accessed because of the weaknesses in the IT system
- quality assurance and quality control risk is being addressed but the risk is still considered to be high
- document management
- risk of independence and undue influence
- audit coverage risks, detection risks and performance risks remain high while control, process and compliance risks remain moderate
- much needed qualified and experienced audit professionals are required to reduce the risks to an acceptable level

If staffing challenges remain, the only other alternative to the NAO achieving its mandate will be to retain external audit firms to assist.

It is acknowledged that there will be increases to the budget for 2015/16 and this is certainly a boost in ensuring that proper audit coverage is increased so as to reduce the high detection risk. In terms of quality and meeting auditing standards it is essential that we have qualified and experienced professionals (who maintain their continuing professional education) to conduct our audits. Apart from meeting quality standards it is also fundamental from a credibility perspective to the House of Assembly and audited entities, and ultimately the general public. From the starting point of meeting professional standards it would be extremely challenging if not impossible to demonstrate compliance with requirements for professional competence without professionally qualified staff at least managing and supervising audit engagements, particularly if financial and value for money reporting is being carried out under any reporting framework.

Audit of the NAO's Accounts

We look forward to having the NAO audited during the 2nd quarter of 2015 so as to be able to complete this prior to commencement of the 2014/15 TCIG Audit of its Financial Statements. It is recommended that the NAO Ordinance be amended to have this audit done annually without the need for any entity recommending that one be done as we should be held to the same standards as other entities that are audited.

TCIG Audit Process

Given the staffing shortages, a general estimate was provided estimating the cost to perform the TCIG audit of between \$500K and \$750K in 2012/13. The NAO could not afford this option and therefore had to, on a phased basis, examine where would be the high risk areas to audit. Two key areas were identified but, given cost constraints, the full audit could not be conducted in the revenue area so an internal controls audit was done (cost approximately \$63,500, reallocated from amount approved for recruiting a Senior Financial Audit Manager which was not filled). During this time, the NAO lost two assistant auditors who resigned to take up positions in the Ministry of Finance. The balance sheet and note to the financials were another risk area identified and audited (approximately \$60,000, reallocated from amount approved for recruiting an Audit Principal which was not filled) and a quality assurance was conducted on a third risk area identified in expenditures (approximately \$17,500, taken from consultancy fees). Further, another Auditor/Administrative Secretary proceeded on maternity leave and no replacement could have been secured at that time.

Amounts have been allocated for other quality assurance reviews (approx. \$14,000) and assistance with bringing some statutory body audits, updating the audit processes, establishing additional

audit programs, conducting joint audits and training and developing of staff in new audit methodologies and approaches (\$54,000).

Training and Development

All staff were trained in value for money audits from the MIS Training Institute, North America, costing approximately \$28,000 including travel, accommodation etc. There was also training for one Audit Manager and one conference attended in December 2014. Training has also been extended to the auditors and scheduled for the entire staff on IFRS and IPSAS (specific targeted training) anticipated to cost approximately \$30,000.

The Grand Turk Office is headed by an Acting Senior Audit Manager who is supervised by the Auditor General.

Specific targeted development will be completed this year even though specific measures have already been implemented so that key staff can focus on their development areas. This involves, not only qualifying but also addressing specific capacity building areas which must be applied in their everyday work life after training has been provided. It is of no use to have training that is not applied in the everyday work setting.

Joint audits will also be conducted but the approach to training and development must come from the ground up, recognizing the core purpose of the NAO is to audit the many ministries, statutory bodies and other agencies. New audit software and revised programs are also to be purchased or created to assist with training and development.

It is also recommended that a training and mentorship program be instituted to progress new and existing audit staff into fully qualified and experienced auditors which will be done in Providenciales and Grand Turk.

Travel

The Auditor General scheduled 2 foreign trips, both of which related to the development of the forensic audit function, securing intelligence services and external audit assistance on special audits (cost approximately \$2,500). One trip was deferred given the timing and is anticipated to take place in 2015. Further matters on this will be developed once the office in Providenciales is up and running.

12. LIMITATIONS

The parameters within which this audit was conducted provides findings related to the implementation of policy. It does not comment on policy initiatives. Further the opinion is arrived at by taking into consideration a combination of matters and not any individual matter. The findings are based on evidence suitable for an audit of this nature to recommend further investigation but not sufficient for civil or criminal action.

The entity's management responses and adjusting entries after the year end were not subjected to detailed auditing procedures applied in the audit of the financial statements and, accordingly, I express no opinion on them.

Our report may not have considered issues relevant to any third parties. Any use such third parties may choose to make of this Audit Report is entirely at their own risk and we shall have no responsibility whatsoever in relation to any such use.

This Audit Report focuses on the annual public financial statements provided to the NAO on 31st July, 2014 and the revised submission on 15th January, 2015. Material changes in the 15th January, 2015 revised financials were not able to be reviewed but a request has been made to obtain the journals made to include in this report.

The intended users of the audited financial statements wish to be confident about the reliability and relevance of the information which they use as the basis for taking decisions. Audits therefore provide information based on sufficient and appropriate evidence, and auditors should perform procedures to reduce or manage the risk of reaching inappropriate conclusions. We afforded the Ministry of Finance an opportunity to include recommendations prior to issuance of this Audit Report which have also been highlighted.

Insofar as discovery is continued in this matter, I reserve the right to supplement or otherwise amend this report regarding assumptions, interpretations, theories of corruption/fraud, and statements of opinions.

13. Key Definitions

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.

A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Applicable financial reporting framework—The financial reporting framework adopted by management and, where appropriate, those charged with governance in the preparation of the financial statements that is acceptable in view of the nature of the entity and the objective of the financial statements, or that is required by law or regulation.

The term —fair presentation framework is used to refer to a financial reporting framework that requires compliance with the requirements of the framework and:

- (a) Acknowledges explicitly or implicitly that, to achieve fair presentation of the financial statements, it may be necessary for management to provide disclosures beyond those specifically required by the framework; or
- (b) Acknowledges explicitly that it may be necessary for management to depart from a requirement of the framework to achieve fair presentation of the financial statements. Such departures are expected to be necessary only in extremely rare circumstances.

The term —compliance framework is used to refer to a financial reporting framework that requires compliance with the requirements of the framework, but does not contain the acknowledgements in (a) or (b) above.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Assets are resources controlled by an entity as a result of past events and from which future economic benefits or service potential are expected to flow to the entity.

Capital Expenditure means the acquisition, construction or development of any tangible capital asset valued in excess of \$75,000 which is distinguished from current account expenditure for repair and maintenance in that it enhances the service potential of a capital asset and therefore consists of a betterment (enhancing the output of the asset, or extending its useful life). There are two types of capital expenditures –

- Capital acquisitions include vehicles and heavy equipment, plant machinery and equipment, vessels and boats, furniture and fixtures, office equipment, computer hardware and equipment and computer software;

- Capital developments include land, building and infrastructure.

Commitment means future expenses and liabilities incurred whether by contract or otherwise.

Contingent liability means a liability that will necessarily arise or come into being if one or more certain events occur or do not occur.

Economy means the acquisition of the appropriate quality and quantity of financial, human and physical resources at the appropriate times and at the lowest cost.

Efficiency means the use of financial, human and physical resources such that output is maximized for a given set of resource inputs, or input is minimized for a given quantity and quality of output provided.

Effectiveness means the achievement of the objective or other intended effect of a program, operation or activity.

Expenses are decreases in economic benefits or service potential during the reporting period in the form of outflows or consumption of assets or incurrences of liabilities that result in decreases in net assets/equity, other than those relating to distributions to owners.

Generally Accepted Accounting Practice means accounting practices and procedures recognised by the accounting profession in the Islands and approved by the Accountant General as appropriate for reporting financial information relating to Government, a department, a fund or a statutory body.

Internal control is the whole system of financial and other controls, including the organizational structure, methods, procedures and internal audit, established by management within its corporate goals, to assist in conducting the business of the audited entity in a regular economic, efficient and effective manner; ensuring adherence to management policies; safeguarding assets and resources; securing the accuracy and completeness of accounting records; and producing timely and reliable financial and management information.

Liabilities are present obligations of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits or service potential.

Non-current assets are assets that, by their nature, have useful lives extending over more than one fiscal year, and include all major items of furniture and equipment for either Government offices, quarters, plant, equipment, and larger tools for Government works, vehicles and launches, owned by the Government of the Turks and Caicos Islands.

Propriety means the requirement that expenditure and receipts must be dealt with in accordance with the intentions of the House of Assembly and, in particular, those expressed through the Public Accounts Committee.

Public property means resources owned by the Government or in the custody or care of the Government.

Regularity means the requirement for all items of expenditure and receipts to be dealt with in accordance with the legislation authorising them, including this Ordinance and any applicable delegated authority, regulations, directives and instructions issued under this Ordinance.

Resources include moneys, stores, property, assets, loans and investments.

Revenue is the gross inflow of economic benefits or service potential during the reporting period when those inflows result in an increase in net assets/equity, other than increases relating to contributions from owners.

Value for money means the economic, efficient and effective utilisation of resources.

Vote means a group of estimates of expenditure, including statutory expenditure, for which an appropriation has been made by an Appropriation Ordinance or a Supplementary Appropriation Ordinance.

14. DETAILED AUDIT ISSUES AND EXPLANATIONS

These are included in a separate document called Detailed Audit Findings.