

Mid-Year Report

by the

Auditor General



Public Accounts 2005

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Guide to using the Report

This Report summarises the conclusions reached following our financial and compliance audits. We sought to spread our reviews across Government Departments and reviewed specific Departments based on an ongoing audit plan. We have attempted to make this report as user friendly as possible and we have tried to adopt plain common language, although, this is not always possible due to the technicality of the issues raised.

This Report is divided into Ministerial Portfolios, each containing one or more departments or sections which were the subject of our review. Also included are a number of reports on non-central government organisations. Each audit report has the following structure:

Background

This section includes a brief description of the activities, roles and operations of the respective department or section. Where applicable it may include also new legislation governing such entity.

Key Issues

This section outlines any material findings or outcomes of our audit and any major developments impacting on the respective department or section.

Control Issues

This section outlines any shortcomings that came to our attention relating to the department's internal control and internal checking mechanisms. These controls should exist so as to serve as an effective safeguard of assets and resources.

Compliance Issues

This section summarises instances whereby the relative department or section lacked compliance with effective legislation and standing General Financial Regulations.

Recommendations

This section outlines our recommendations to the respective departments so as to encourage them to correct or mitigate the weaknesses that came to our attention. Normally, our recommendations are aimed at improvement of the internal control systems with an emphasis on prevention of errors or misuse.

Management Comments

Within this section we sought to include the Management's reaction to our comments and actions that they have taken or plan to take so as to rectify any shortcomings that came to our attention.

While some departments or sections in this report will have all the headings outlined above, this will vary depending on the size of the department or section and the findings of our audit. However, in all cases the structure flows in the order as outlined above.

Executive Summary of Findings

Executive Summary of Findings

This Part is intended to act as a quick reference to the Report by highlighting the main findings. It could thus facilitate the work of the main users of the Report, in particular, the Public Accounts Committee, Ministries and Departments concerned and other interested parties when referring to the contents of the Report.

Issues and Audit Concerns

The handover of **Pre-1998 Class 1 Social Security Contributions** from Social Security Department (SSD) to Inland Revenue Department (IRD) was late and improper, with IRD failing to verify information provided by SSD. IRD is not equipped with an official specialised software enabling quick data analysis, identification and generation of reports of Contributions' defaulters, but makes use of in-house developed programmes '*scripts*'. (page 30). The IRD did not accept to hold meetings with the NAO and failed to supply computer systems logins thus further limiting the scope of the audit.

An audit carried out on **Children Allowances** revealed that the Social Security Department failed to physically confirm custody of children and the composition of households as claimed by applicants. The Department also failed to verify income disclosed by beneficiaries for Children Allowance purposes with the respective declarations at the Inland Revenue Department. A number of overpayments or underpayments in allowances during the period under review were also highlighted in the report on page 16.

The **Industrial and Employment Relations Department** (page 27) lacked the adequate enforcement mechanism to recoup the amount of arrears due. In particular no form of security or guarantee was requested by Government from applicants upon the granting of loans. Furthermore, any form of checking with records held by the Inland Revenue Department and the Social Security Department in respect of the financial situation, employment and welfare state of defaulters could not be carried out as such access is currently not legally possible.

Customs Department lacked the formal established procedures and systems documentation in relation to **goods in transit** specifically for the carrying out of the general screening and the physical and documentary examinations. This weakness was also found in the special instructions for the issuing, management and use of guarantees and guarantee waivers, and detailed sub-classified information and data (page 34).

Potential risk areas concerning **Traditional Own Resources (TOR)** were identified during meetings with Customs as detailed in page 39. Main deficiencies concerned the compilation

of data in statements forwarded to the Commission on a periodical basis and release of goods by Customs prior to duty payments.

The **Public Debt Budgeting** process is not fully documented and lacks audit trail. Weaknesses included (page 43)

- inadequate formal public debt planning organisational structure;
- no formal debt management strategic plan;
- public debt mix lacking policy guidelines;
- non-functionality of the Public Debt Management Advisory Committee;
- inadequate formal authorisation procedures for the publication of Malta Government Stocks Annual Issuance Calendar and for new Government stock issues; and
- failure to set up the Debt Management Office.

Audit of salaries carried out at the **Courts of Justice** (page 84) as well as within the **Ministry of Education, Youth and Employment** (page 20 and 23) revealed lack of controls over attendance and overtime records. Medical certification could not always be evidenced to cover sickness absence.

The source of authority supporting the rate payable to transcribers of Court hearings was not made available. Furthermore though such tasks should have been performed after office hours, some officers were carrying out this job during normal working time.

Government owned vehicles have been availed of after office hours by untitled officers within the Ministry of Education. Moreover, no tax was deducted on this fringe benefit.

The **Government Quarry (Ta' Robba)** lacks adequate records of the material being used up. Instances were noted when exceptionally sized stone blocks from the Quarry were sold to private individuals for the nominal price applicable to sales to government entities. At the same time running period contracts are annually renewed with outside suppliers for the same stone products cut from the Quarry. Standing regulations governing attendance records are not being applied to the eleven (11) Quarry workers. These are said to be engaged on an unofficial 'task and finish' basis, however no formal daily routine tasks or production quotas are in place. (page 76)

An audit carried out at the **Bio Medical Engineering Stores** (page 70) located at Karen Grech Hospital revealed stock discrepancies between stock records and physical stocks. Details such as the unit cost and supplier details of various items are either incorrectly recorded or have not been inputted in the stock control system.

The **Paying Agency (PA)** within the Ministry for Rural Affairs and the Environment, responsible for the management of funds received from the European Union (EU) lacked cash flow management process. Payments to beneficiaries are effected subject to availability of funds and EU Commission deadlines. Besides the lack of segregation of duties, adequate internal controls are not in place and communication with the Integrated Administration and Control System (IACS) Department is weak. (page 60)

Shortcomings in the computerised system in use by the **IACS Department** were noted. Notwithstanding, the Department is placing heavy reliance on the inbuilt mechanisms of the system and is also very dependant on one officer who is responsible for a vast range of tasks. There is room for improvement on location spot checks as well as on subsequent quality control checks. (page 65)

A number of audits carried out on selected Non-Central Government Organisations (**NGOs**) and other Government Authorities revealed that the financial statements of Non-Central Government Organisations/Authorities did not fully comply with International Financial Reporting Standards (**IFRSs**). Weak control over the safeguarding of fixed assets resulting from incomplete Fixed Assets Registers was also generally noted. Other control and compliances issues were also being highlighted in the respective reports on pages 90 to 97.

Introduction

Introduction

In terms of Section 108 (5) of the Constitution of Malta and the First Schedule of the Auditor General and National Audit Office Act, the Public Accounts of the Government of Malta are to be audited and reported upon annually by the Auditor General to the House of Representatives.

This Mid-Year Audit Report relates to Public Accounts for financial year ending 31 December 2005. It summarises the findings of the financial and compliance audits on the Financial Statements and activities of the Malta Government, and a number of non central government organisations, which were concluded up to June 2006. The report is intended to complement the Annual Audit Report which will be published towards the end of the year.

The Report attempts to highlight the findings emerging from our reviews in a concise, clear and effective way.

We continued to focus on the audit of systems and issues relating to specific government activities. The more significant findings are being highlighted in the Executive Summary.

As is now customary in our Audit Reports on the Public Accounts, the audit findings are being reported in a standardised format including Background, Key, Control and Compliance issues. We also outline our recommendations and the management comments.

The Annual Audit Report to be published before the end of this year will incorporate audits carried out on 2005 Public Accounts during the latter half of this year. The Annual Audit Report will further include the Audit Opinion which will cover the audits carried out during the whole of 2006 in respect of 2005 Accounts. This will complete the whole statutory financial and compliance audit reporting cycle for 2006.

This report should provide useful material for the House of Representatives and for the future work of the Public Accounts Committee and in contributing to the improvement of public accountability and transparency.

Finally I would like to express my gratitude for the efforts and dedication of the officers who assisted me in the proper discharge of my responsibilities.



J. G. Galea
Auditor General

July 2006

Ministry for the Family and Social Solidarity

Social Security Department

Children Allowances

Background

Children Allowance benefit is regulated by the Social Security Act. The law also regulates the allowances paid in respect of Foster Children and Disabled Children. The Children Allowance scheme on its own represents approximately six per cent (6%) of total Social Security spending which during 2005 amounted to Lm221million (2004 - Lm207million). A total of 35,905 beneficiaries were benefiting from Children Allowance during 2005 (2004 - 37,809).

Key Issues

Investigations by Department

No physical investigations were being made by the Department to confirm whether custody of children and the composition of the household are in accordance to that disclosed by applicants.

The Department also lacked verification of income disclosed by beneficiaries for Children Allowance purposes with their respective declarations at the Inland Revenue Department for tax purposes.

No investigations were being carried out by the Department to identify whether any pre tax profits registered by Companies, were included with income declared by shareholders which were beneficiaries of Children Allowances.

Furthermore, current pre tax profits cannot be determined from audited financial statements since the deadline for submission of audited accounts to the Inland Revenue Department does not coincide with the filing of the application.

Overpayments/Underpayments

Out of a sample of eighty five applications, twenty four per cent (24%) of the beneficiaries were overpaid during the period under review and another five per cent (5%) were underpaid. Incorrect payments of benefits resulted from:

- Incorrect income considered in rate awarded to newly married couples and beneficiaries in receipt of pensions;
- Receipt of Children Allowance by mother children concurrently with their parents;
- Errors in inputting of applicant's details and income;
- Parents in receipt of child benefits for children that were not entitled for the allowance;
- Child not in custody of Children Allowance beneficiaries;
- Incorrect link between bank interests module and Children Allowance module on SABS (Sistema għall-Amministrazzjoni tal-Beneficji Socjali); and
- Incorrect amount of alimony received by beneficiaries included in benefit computation.

Fictitious ID card numbers

Foreign individuals, including individuals given a refugee status and who are benefiting from Children Allowances required to have their households duly recorded in SABS. It was common practice for such individuals to be identified with a fictitious identification number. The practice posed a

threat to the security of the system as fictitious household could potentially be set up.

Control Issues

Opportunities for improvement were identified in the following areas:

- Adoption of different policies by the Social Assistance and Children Allowance sections on matters concerning acceptance of evidence relating to custody of children. This resulted in the latter section having to accept the former section's decisions.
- SABS weaknesses in computations concerning joint custody in the case of separated couples; Inaccuracies in actual interests and income earned as opposed to those considered in computation of rates due; and insufficient controls where changes in custody of children are concerned.
- Acceptance of inadequate formats of declaration of income in the case of self employed individuals.
- Non confirmation of termination of employment with the ETC (Employment & Training Corporation) in instances where no income from employment was declared.

Recommendations

Key Issues

Investigations by Department

It is recommended that the financial year for benefits be based on a calendar year. The income considered for Children Allowance purposes shall be that earned during the period January to December preceding the benefit year by twelve months.

This would facilitate the exchange of information with the Inland Revenue Department or create a direct live link to the beneficiary's declared income. This would also lower the risk of under declaration of income and lessen the time taken for the

keying in of data. The Children Allowance section would thus be in a better position to focus its resources on investigating suspicious cases and thus reduce abuse.

The recommended change would also enable sufficient time for Companies' audited accounts to be filed at the Registry of Companies and the Inland Revenue.

Overpayments/Underpayments

The internal control system is to be enhanced to cater for the timely detection and prevention of errors. Personnel at the Social Security Department are to be well trained before being assigned their duties. Assessment and verification of new claims and/or changes in rates are to be carried out by two different pools of personnel. Verification should be carried out periodically for as long as the benefit is given. Furthermore, even though these inaccuracies can be identified with hindsight, they still need to be rectified.

The Social Security Department is to utilise the services of a lawyer to deal with legal interpretation as well as give assistance in the interpretation of certain complex clauses in the Act.

Fictitious ID card numbers

Management is to evaluate the most feasible option of monitoring the practice. SABS may be enhanced by being directly linked to the CDd (Common Database) so that such cases are easily identified and validated. Regular reports are to be generated by management to review new households created in this manner. The Refugee Commission is to be consulted so as to verify the legitimacy of the entitlement of fictitious identification number holders.

Control Issues

- Common policies are to be adopted between different benefit sections by the compilation of a procedures manual across the Department.
- The SABS system is to be enhanced for a

smoother running of the computations of benefit rates.

- A network of information sharing between the Inland Revenue and the Social Security is to be established.
- It is to be ensured that claimants, who do not declare any income, are not gainfully employed prior to processing any applications.

Management Comments

Management concurred with most of the findings and offered the following comments in view of the above shortcomings:

The Department had in the past considered shifting the benefit year but this was not considered viable due to technical and legal reasons. However, these problems have recently been addressed and the Department is undergoing an exercise to assess the advantages and disadvantages of such a proposal. The Department is also considering obtaining access to other sources of information, while preliminary investigations are being made against Inland Revenue income declarations after obtaining authorisation from the beneficiaries.

A number of the reported wrong payments were described by the Department as being only identified retrospectively. It

was also stated that all legal issues are being referred to the Attorney General's office when required.

Whilst acknowledging the risk involved in having a fictitious ID number for identification of certain individuals, this was described as the best way to deal with such a situation. Moreover the creation of a household is created and verified by two officials. The Department is also in liaison with the Public Registry on acquiring a direct link to the Common Database. Regular updates are also being received from the Refugee Commission.

The Department is currently carrying out an extensive exercise to compile a procedures manual for all line sections which will surely reduce inconsistencies between sections. The newly set up Benefit Fraud section is also contributing to the improvement of the Department's internal control system. The information database is also being enhanced, a data warehousing project is underway, and SABS is being continuously improved. It was also declared that it was customary for income declarations on inadequate formats to be duly investigated. Any unconfirmed employment will now be investigated against the income declaration at the Inland Revenue Department for taxation purposes.

Ministry of Education, Youth and Employment

Ministry - Wages and Salaries

Background

The budget allocation in respect of Personal Emoluments for the financial year 2004 stood at Lm749,000. This covered both the Ministry of Education (including the Private Secretariat Unit) and the Examinations Department. The budgeted figures were exceeded by nearly seven percent (7%) as the actual expenditure amounted to Lm800,722.

Control Issues

Opportunities for improvement were identified in the following areas:

Attendance Sheets

- Employees were recently required to enter the 'time-out' before leaving the place of work. It was observed that some officers were entering the 'time-out' for other employees who may have left the office earlier.
- On occasions, attendance sheets did not reflect the officers on the payroll.
- Not all attendance sheets kept at the various Sections within the Ministry were evidenced as being checked and certified correct. Instances were also encountered where a number of employees did not sign in.
- A number of attendance sheet entries held at the Information Management Unit (IMU) were overwritten or altered with correction fluid. This may indicate that access to such records is not restricted and that a number of officers may be signing the attendance

sheets one or more days in advance. Similar inconsistencies were observed while reviewing the attendance sheets at the Examinations Section, as in the case of an officer being on vacation leave but also signing in for work.

- Attendance sheets of the EU Affairs Section are not forwarded to Human Resources (HR) on a regular basis in order to update attendance records, whilst those of the IMU Section are not forwarded at all. Attendance sheets recording invigilation duty hours were disposed of by the Examinations Section since a year had elapsed from the completion of the examinations.
- During 2004 there was no formal officer in charge of attendance sheets at the Youths Section.

Overtime and Allowances Payments

- Although specified in the requisitions for overtime, no deduction was made for meal breaks when overtime is performed on Saturdays.
- Two (2) officers, employed within the Youths Section, out of a total of four (4) employees reviewed (who worked overtime during 2004) were underpaid since the overtime rates used were incorrect.
- On various occasions, discrepancies were noted when comparing the total number of overtime hours requested and subsequently approved, to hours actually worked.

- Instances were encountered where claims for overtime as well as for supervision and invigilation performed were unilaterally compiled by the officer actually performing the respective duties, without evidence that these were being independently checked at a later stage.
- From a sample of seven (7) employees from the Examinations Section, whose overtime and/or allowance for invigilation were checked for accuracy, differences resulted in the global payments made to five (5) of these officers.
- Due to lack of information and supporting documentation, allowances paid to certain officers could not be verified.

Documentation

- A list of employees reflecting all the Ministry's staff movements during 2004 was not available. Any required information had to be extracted from the payroll system.
- No temporary absence record sheets were being kept at the Stipends Office and at the Youths Section. Furthermore, retention of temporary absence sheets at the Customer Care Section could not be confirmed as these were not made available.

Incomplete Requests

- In the case of three (3) out of the five (5) officers who applied for reduced hours of work in the audit sample, the reason for the request to work on a reduced timetable was not specified, notwithstanding that this is a requirement of the Public Service Management Code (PSMC). Moreover, one of these requests was not confirmed by a formal approval.
- The majority of requests for payment of overtime and allowances, out of a sample of seven (7) employees at the Examinations Section, lacked the necessary details required from the Accounts Section. This indicated weak control over such payments.

Recommendations

Control Issues

Attendance Sheets

- Action is to be taken against employees breaching the regulations, as well as against officers collaborating with such employees.
- It is to be ensured that the attendance sheets reflect all employees included in payroll (excluding officers on performance contracts) and vice-versa.
- Attendance sheets are to be supervised daily by a responsible officer who is to collect records after official check-in time and duly note lateness or absenteeism on which disciplinary action could then be taken.
- All attendance records are to be kept and appropriately filed for future reference. Furthermore, both sections indicated are to be instructed to forward attendance sheets to HR on a regular basis. Follow-up of missing attendance records is also expected from the HR Section.
- Control could be enhanced by assigning an officer within another Section who can be held responsible for the attendance sheets of the Youths Section.

Overtime and Allowances Payments

- Whenever Saturday is considered a normal working day, deduction for break time is still to be applied, in consonance with normal working days. Overtime during such breaks is only to be permitted in exceptional circumstances.
- All manual calculations are to be double-checked by the compiler of worksheets. Requests for payment are to be independently checked for accuracy by the officer's superior before forwarded for payment. Furthermore, prior to effecting payment for overtime, officers are to ensure that hours approved, by the Permanent Secretary are not exceeded.

- All allowances paid to employees are to be backed up by the necessary computations and supporting documentation, which are to be appropriately authorised and filed for future reference.

Documentation

- A list of employees within the Ministry is to be diligently compiled and updated with any new recruitments, resignations and promotions.
- Each section at the Ministry is to maintain temporary absence records, with each entry duly authorised by the senior officer in charge.

Incomplete Requests

- All requests to work on reduced hours, including the reasons for such requests, are to be formally approved by the Head of Department as required by the Public Service Management Code and filed in the respective officers' personal files.
- Each request for payment is to be duly signed, stamped, dated and referenced by the officer in charge at the Accounts Section prior to being passed on for payment.

Management Comments

All recommendations outlined in the report have been accepted and appropriate action is already being taken.

Private Secretariat - Wages and Salaries

Background

The budget allocation in respect of Personal Emoluments for the financial year 2004 stood at Lm749,000. This covered both the Ministry of Education (including the Private Secretariat Unit) and the Examinations Department. The budgeted figures were exceeded by nearly seven percent (7%) as the actual expenditure amounted to Lm800,722. This was mainly caused by the transfer of staff of the Department of Youth to the Ministry's payroll and shortfalls in allowances and wages in the Approved Estimates for 2004.

Key Issues

Excessive Claims for Overtime Payments

During 2004, overtime payments made to a casual field officer on the payroll amounted to more than half her basic salary. A number of hours claimed could not be verified since 'time-out' was not always indicated on attendance sheets. On a number of occasions, claimed overtime hours were overstated, resulting in an overpayment. No contract of service was made available. Entitlement to overtime payments could therefore not be confirmed.

Advisors on Payroll

- Actual hours worked by the part-time advisors could not be confirmed as records of hours worked are not kept by the Ministry.
- One advisor was overpaid the equivalent of one month's salary during 2004 and had

his tax undercalculated by failing to aggregate his part-time income to his full-time income derived from the same employer.

- Another advisor has been receiving double the allowance since entering into agreement with the Secretariat.

Control Issues

Opportunities for improvement were identified in the following areas:

Attendance Sheets

- Attendance sheets of the Secretariat and those of the Policy Unit (within the Private Secretariat) were not being certified correct. Various inconsistencies were encountered while reviewing these sheets, including the omission of signing out times.
- An officer could not be traced to attendance sheets during most of 2004.

Claims and Payments for Overtime

- A number of overtime hours have been unjustifiably claimed by an officer since they overlapped with the hours in which he was carrying duties elsewhere.
- Overtime records were not being accurately maintained. Unrecorded hours were noted when these were compared to attendance sheets.
- The calculation of overtime hours leading to the entitlement of payment of the monthly additional bonus has been carried out incorrectly in a number of cases. Furthermore, such computation is carried

out on a monthly basis while both the authorisation and the actual payment of the bonus are calculated on a four-weekly basis, thus hindering verification of payments.

Absences and Leave

- Control over the normal working hours within the Private Secretariat was lacking and no temporary absence sheets were being maintained.
- Vacation leave cards of a number of employees were not being updated.
- Medical certification could not be evidenced to cover sickness absence as per attendance sheets in a number of instances. Furthermore, sick leave records subjected to the audit sample were not updated.

Fringe Benefits

- The vehicles supposedly for general use appear to have been assigned to specific officers during 2004. On many occasions, details in the log books indicate that these vehicles were being availed of after office hours by officers not entitled to a government expensed vehicle. Moreover, no tax on fringe benefit was being deducted from salaries.
- Official authorisation could not be evidenced to change a car allowance entitlement, granted as per Ministerial Secretarial Agreement to a Projects Co-ordinator, to the use of a fully expensed office car.
- An officer receiving transport allowance opted to revert to the full use of an office car (as per original agreement). However, this officer was already making use of a car prior to the date of change in fringe benefit. Consequently he was receiving transport allowance while also making use of an official vehicle.

Lack of Documentation

- In the absence of documentation relating to their previous employment, the

completeness and accuracy of tax paid according to FSS rules could not be confirmed in the case of the five (5) officers, who either commenced or terminated their employment with the Secretariat during 2004.

- The verification of Social Security Contribution calculations was hindered in the case of new officers joining the Secretariat, as increments in salaries due from the date of engagement up to the first payroll were included with allowances. In addition, instances were also encountered whereby income supplement, which should have been paid pro rata, was paid in full not taking into consideration the contract effective date.
- Authorisations for payment of qualification allowance (which was not supported by evidence of certificate) and allowance in relation to cleaning duties could not be traced to the respective officers' personal files. Moreover, no supporting documentation was obtained in respect of an allowance paid to an Office Coordinator.

Erroneous or Unjustified Payments

- Allowances for overtime allegedly carried out during 2003 were paid to a Secretariat Messenger in 2004, notwithstanding the fact that attendance sheets clearly indicate that no overtime work was carried out.
- Overpayments were made to various officers following incorrect calculation of salary, allowances or income supplement.
- Adjustments to salaries established by Ministry of Finance Circular 1/2004 were not reflected in the case of at least five (5) officers in salary scales fourteen (14) to twenty (20) and / or receiving an allowance based on these scales.

Compliance Issues

Hours Worked by Casual Typist/Clerk

Occasionally, an officer employed as a 'casual typist' worked more than the maximum of forty hours established by the

Public Service Management Code (PSMC). Authorisation to work these extra hours was not evidenced.

Furthermore, the same employee, reverting to a reduced hour timetable, claimed overtime and was paid accordingly, in breach of the PSMC which clearly states that employees on a reduced timetable are not entitled to payment for overtime work.

Staff Complement and Secretariat Vehicles

Documents showing approval for recruitment from the Office of the Prime Minister (OPM) were only available for six (6) officers working with the Secretariat. During 2004 a total of thirty-three (33) officers were working within this Section, twenty-five (25) of whom receiving benefits. This exceeded the stipulated staff complement by thirteen (13) officers.

In addition, the number of vehicles held at the Secretariat for general use at end 2004 was four (4). This also exceeded the maximum indicated by the respective guidelines by two (2) vehicles. No approval from the OPM has been granted.

Recommendations

Key Issues

Excessive Claims for Overtime Payments

While overtime records for 2004 are to be reviewed, the officer could still be asked to justify past claims for overtime. Payments that cannot be validated are to be recouped.

Advisors on Payroll

Number of weekly hours performed by these advisors is to be certified by a responsible officer. Furthermore, the correct tax rates should be applied and any overpayments made are to be refunded.

Control Issues

Attendance Sheets

All attendance sheets are to be supervised on a daily basis, to ensure completeness and correctness, and duly certified by the officer in charge.

Officer Not Traced to Attendance Sheets

The situation appears to have been rectified in 2005 and the officer started signing in again. However, controls have to be put in place to ensure that such a situation is not repeated in the future.

Unjustified Overtime Hours Claimed

Officers are to be instructed to sign out (on the attendance sheet) at the exact time they leave the workplace.

Overtime Database Records

Overtime hours worked are to be properly recorded in the individual officers' databases. The details on these databases are to be checked against recorded hours in the attendance sheets prior to the payment of allowances.

Calculation of Overtime Hours

The calculation of overtime hours should be carried out in accordance with the 'Engagement of Staff for Ministers' Secretariats' guidelines.

Temporary Absence

Any absences from work are to be duly authorised and documented in the temporary absence sheets.

Vacation and Sick Leave

Regular reconciliations between attendance sheets and sick leave as well as vacation leave cards are to be performed so as to ensure proper recording. Furthermore, any sick leave days taken are to be covered by a medical certificate.

Use of Secretariat Vehicles

It is to be ensured that vehicles are utilised only for office duties and pooled as necessary. This can be achieved through regular review of the vehicles' log books, where the purpose of the trip should also feature.

Change in fringe benefits

Any changes in fringe benefits have to be approved by the Management and Personnel Office and subsequently, the respective officers' Agreements amended accordingly.

Moreover, it is recommended that the officer making use of a government expensed car prior to the date of change in fringe benefit is asked to refund any transport allowances paid to him while making use of the official vehicle.

Lack of documentation

All relevant documents (including copies of FS4s and FS3s of the previous employment) pertaining to each officer are to be kept in the respective personal files for ease of reference.

Erroneous Payments Made to Officers

Each situation is to be rectified by requesting reimbursement from the officers of the extra amounts paid to them. The

salaries of officers affected by the foregoing Circular are to be reviewed and consequently the necessary adjustments affected.

Compliance Issues

Hours Worked by Casual Typist/Clerk

The PSMC requires that any additional hours over the maximum of forty hours have to be absolutely necessary. In such cases, proper authorisation is to be given and documented. Furthermore, no more overtime payments are effected while the employee is working on a reduced timetable.

Staff Complement and Secretariat Vehicles

Any departures from requirements set out in the 'Engagement of Staff for Ministers' Secretariats' guidelines are to be duly authorised by the OPM. Any correspondence in this respect and subsequent approvals are to be duly filed for future reference.

Management Comments

Management has agreed with the recommendations made and action has already been taken to comply accordingly.

Industrial & Employment Relations Department

Arrears of Revenue

Background

The arrears of revenue due to the Industrial & Employment Relations Department consists of outstanding repayment of loans under the "Self Employed Loan Incentive Scheme". The aim of the scheme was to assist individuals to start up a business enterprise. Responsibility for the repayment of these loans was originally under the Ministry of Finance.

Key Issues

Enforcement/Arrears Collection

No adequate enforcement effort is being made by the Department to recoup the amount of arrears due. Furthermore no checking was carried out against records held by the Inland Revenue Department and the Social Security Department in respect of the financial situation, employment and welfare state of defaulters as such access is currently not legally possible.

A complete list of individuals who benefited from the loan and/or are currently repaying the bank is not available.

No form of security or guarantee was requested by Government from applicants upon the granting of these loans.

Control Issues

Opportunities for improvement were identified in the following areas:

- Arrears collected during the year represent only 6% of arrears due by individuals effecting payment and 3% of total arrears due. Estimated repayment periods due to

irregular or immaterial amounts range from thirteen to seventy years.

- Reminders/requests for payment and judicial letters sent to defaulters are not followed with further legal action by the Department.

Recommendations

Key Issues

Enforcement/Arrears Collection

The financial situation, the employment and welfare state of each individual defaulter should be examined by personally requesting a copy of their latest FSS/Income Tax return. Otherwise, specific information regarding defaulters could be requested from the Department/Entity concerned.

Scheme beneficiaries presently repaying the loan should also be monitored so that the Department would be in a position to identify potential new defaulters earlier on.

Control Issues

- The Department should seek to reach agreements with defaulters to ensure the payment of more substantial and regular monthly installments, especially from those defaulters which are still gainfully employed.
- Judicial letters should be followed up with the appropriate legal action. The Department should also assess the viability of initiating legal proceedings against a defaulter by evaluating the arrears due vis-à-vis estimated legal expenses and taking

into consideration the financial situation of the defaulter. Considering the estimated legal fees involved as a percentage of the amounts in default, such course of action may still be considered feasible as a long term proposal.

Management Comments

Management has remarked that efforts have been made to obtain access to records in respect of defaulters, held by the Inland Revenue Department, the Social Security Department and the Employment & Training Corporation. To date, these efforts have proved futile and obtaining such access is not possible, mainly due to confidentiality and data protection legislation.

Management also pointed out in some detail the substantial funds required to institute legal proceedings against defaulters and it was suggested that this course of action may be counterproductive in the long run when one considers that there is no guarantee that the amounts due would be recouped.

On the other hand, management concurred that no guarantees were requested from loan applicants when the scheme was launched. The bank granted loan facilities to the beneficiaries and the Government had guaranteed those loans itself. Furthermore, no other individuals who have benefited from the scheme are currently repaying the bank.

Ministry of Finance

Inland Revenue Department

Enforcement of Class I Social Security Contributions

Background

Since 1978, the Inland Revenue Department (**IRD**) was vested with the responsibility of administering the collection of Class I Social Security Contributions (**Contributions**), whereas the Social Security Department (**SSD**) was in charge of the enforcement of Contributions due. With effect from 1998, the enforcement of collection of Post-1998 Contributions was transferred to IRD.

Responsibility for the enforcement of Pre-1998 Contributions was transferred to IRD with the coming into force of Act III of 2005 on 3 January 2005, amending the Social Security Act. The powers vested in the Director of Social Security to collect these Contributions could also be exercisable by the Commissioner of Inland Revenue (**CIR**).

Key Issues

Meeting with NAO

It was not possible to assess the adequacy of internal controls in place and verify the level of enforcement of Contributions' Current Year forms' submission, since the Director Operations declined an invitation to a preliminary meeting. Moreover, no views or comments were submitted on the discussion points.

Computer System Logins and Other Information not provided

The following requests were not complied with:

- The logins, hindering the conduct of walk

through tests designed to evaluate the controls exerted by IRD for the collection and enforcement of Contributions.

- Duties and Responsibilities of FSS and Collection Sections.
- Rules and Regulations for Enforcement and Collection of Contributions.
- A List of Reports dealing with Contributions' enforcement.

Improper Handover of Pre-1998 Contributions' Responsibility to IRD by SSD

- IRD stated that notwithstanding the fact that *"the Director (Social Security) has been requested to take necessary steps from the operational aspect to implement Cabinet's decision in liaison with the Commissioner of Inland Revenue"*,¹ CIR was not contacted on the matter.
- The handover of Pre-1998 enforcement responsibility was made during one meeting with SSD in April 2005.
- SSD was not asked to inform IRD of any new Pre-1998 Defaulters identified following the transfer of responsibility.

Verification of Information provided by SSD

- The balances claimed as due by SSD were not reviewed and verified for correctness.
- The list of Pre-1998 balances due with payments forwarded to IRD but which were

¹ Letter dated 18 November 2004 addressed to the Auditor General by the Permanent Secretary, Ministry for the Family and Social Solidarity refers.

not accounted for by SSD were not updated as a consequence of lack of communication between the two Departments.

Enforcement Responsibilities not clearly reflected in relative Performance Agreements

Discrepancies were noted between Appendix A of the Performance Agreements 'The Officer's overall objectives for the next three years', of the Director Operations and the Director Administration and Enforcement, as against their actual work related to the enforcement and collection of Contributions.

IRD lacks Specialised Software

- IRD has no official specialised software in place enabling quick data analysis, identification and generation of reports of Contributions' Defaulters. IRD claimed that although such software was requested from MITTS in 1998, it has been postponed due to urgent departmental requirements. It is favourably noted that in-house developed programmes '*Scripts*', enabling extraction of defaulters' reports, were developed. However, these *scripts* necessitate various manual interventions.
- *Scripts* developed are tested by the Department, but are not being independently tested by MITTS. There might be the risk of human error or abuse in the process of developing *scripts* and consequent generation of defaulters' reports therefrom.
- A sample of the reports generated by the Computer Section within IRD in 2005, could not be processed in order to verify their accuracy and completeness, since *scripts* are not user friendly.

Control Issues

Opportunities for improvement were identified in the following areas:

Lack of Planned Generation of Timely Reports

- The Computer Section was not instructed to issue, on a regular basis, reports of defaulters. Such Reports are extracted only whenever a request is made by Top Management. This could lead to time lags in the identification of new defaulters.
- Requests to the Computer Section for Contributions related reports are not formally forwarded in writing, thus posing limitations on the audit trail.

Lack of Official Documentation for Enforcement Policies and Procedures

There are no formal written policies and procedures in place regulating enforcement procedures and relative parameters, enforcement actions' deadlines, management reporting and communication lines.

Compliance Issues

No Adequate Reporting of Arrears of Revenue

The composition of its arrears of Contributions could not be analysed neither could balances due be calculated efficiently.

- Due to the lack of specialised software for Contributions, IRD is not in a position to generate an accurate annual list of arrears of Contributions and as a result it is not complying with the General Financial Regulations 1966 and the relevant yearly Treasury Circular.
- Although IRD claimed that through the use of *scripts*, the total amount of arrears from defaulters could be analysed between actual and estimated amounts, this was not done in the 2004 Arrears of Revenue Return.
- Reliable estimates of the amounts in default cannot be made since generally employers do not update the Employment and Training Corporation with additions/reductions in their

recruited employees. Estimates are then based on the last Contributions form submitted, irrespective of the year it relates to.

Recommendations

Key Issues

Improper Handover of Pre-1998 Contributions' Responsibility to IRD by SSD

IRD and SSD should ensure that the transfer of enforcement responsibility is made in the most effective and efficient manner by keeping open communication lines for any queries which IRD could have with regards to its new duties. IRD is to request SSD to keep them informed on a regular basis of new Pre-1998 defaulters identified by the latter.

Verification of Information provided by SSD

IRD should:

- review the files maintained by SSD for every Pre-1998 defaulter and analyse thoroughly the breakdown of the balances claimed as due by the latter. Any discrepancies noted should be adjusted; and
- carry out an exercise to update the Pre-1998 balances with any payments which could have been received before 3 January 2005 and not recorded by SSD in the relative defaulters' accounts.

Enforcement Responsibilities not clearly reflected in relative Performance Agreements

- The functions, responsibilities and objectives relating to the collection and enforcement of both Pre and Post-1998 Contributions' arrears should be clearly reflected in the Performance Agreements of the respective Directors.
- CIR may wish to consider appointing an acting Director Operations.

IRD lacks Specialised Software

In light of the new responsibilities entrusted to IRD, the Department should give high priority to the installation of a software programme for Contributions' arrears.

Control Issues

Lack of Planned Generation of Timely Reports

- IRD should establish regular timing for the issue of defaulters' reports and adhere to it, enabling immediate identification and enforcement action, especially where amounts in default are substantial.
- Requests for defaulters' reports should be made in writing, enabling Top Management to be in a position to follow-up the enforcement work on Contributions as carried out by the different Sections concerned.

Lack of Official Documentation for Enforcement Policies and Procedures

IRD should set up formal written policies and procedures, related to enforcement and collection of Contributions.

Compliance Issues

No Adequate Reporting of Arrears of Revenue

IRD should give priority to set up the necessary software infrastructure from which it could extract and analyse detailed statements of arrears.

Management Comments

- Director (Operations) presented CIR with an explanatory report regarding his refusal to hold a meeting with NAO. CIR fully endorsed this report forwarding, amongst others, the following remarks:
 - that the Director was *".....unable to entertain the request at a time when I was trying hard to get to grips with the difficult situation created by the concurrent departure of two senior officers holding key*

positions within the directorate and attending to my own workload.;

- *Furthermore, as the year nears its end I have additional tasks to address in preparation for the coming year's changes in forms and returns, explanatory literature about new arrangements, process design and software requirements.*
- *I applied for the post of Director (Operations) on the premise that I would be assuming the responsibilities of my predecessor with the same resources including three Assistant Directors. During my term as director I had, at most, one Assistant Director, at any point in time."*
- IRD is encountering problems to keep constant communication with SSD due to reallocation of SSD staff.
- SSD never supplied a cut-off date, after which IRD will be in a better position to update the pre-1998 balances.
- The Department is contesting that there is a specific software that processes information in batch to determine employers who are defaulters in both tax and social security contributions withheld by employers from employees. This software was implemented in April 2003 with the first runs taking place in May 2003.
- The legislative provisions when applied to the letter (as the software does) will generate a number of reminders which will not result in collectible amounts, having additional taxes or penalties raised

because documents have been submitted late but payments would have been effected. The whole process is thus being reviewed gradually to mitigate this problem.

- The whole process, including report generating featuring defaulters, is currently under review. A major effort of software enhancements is carried out to improve processing in view of depleting and insufficient human and financial resources.
- Further accuracy on contributions will be achieved after the SSD start exporting credits on a regular and reliable basis to IRD. The software that considers credits has been developed but is not fully implemented and has never been reviewed as data has not been given on a reliable and regular basis by SSD.
- The ETC project is progressing slowly due to major discrepancies with the PE numbers and employee relationships in the ETC Database. A major review of the data is in progress and is approximately 70% complete.

Management failed to forward comments on the following issues raised:

- Computer system logins and other information not provided.
- Enforcement responsibilities not clearly reflected in relative Performance Agreements.
- Lack of official documentation for enforcement policies and procedures.

Customs Department

Community Transit

Background

Community transit, regulated by the Community Customs Code and Implementing Provisions (**IP**), is a Customs procedure which allows goods not in free circulation and those few Community goods for which Community transit is required, to move within the European Community (**EC**). Under this procedure, the payment of any customs duty, or other charges, is duty suspended.

Community goods, as opposed to non-Community goods, are those goods which have Community status and can move within the EC without any Customs controls. These goods:

- originate in the Community; or
- have been imported from a non-EC country and have been put into free circulation in the Community per Article 79 of the Customs Code; or
- have been manufactured in the Community from materials or parts imported from a non-Community country, provided the imported materials or parts are in free circulation.

There are two types of Community transit movements:

- The External (T1) procedure, which is used for non-Community goods on which import duties have not been paid and for Community goods subject to a Common Agricultural Policy (**CAP**) refund.
- The Internal (T2) procedure, which is used for Community goods:

- moving from one Member State to another through an EFTA country;
- moving overland to an EFTA country; and
- when moving from San Marino (with some exceptions) and when moving to or from Andorra.

Issues mentioned and potential risk areas identified in this report are based solely on information obtained through meetings held in conjunction with the European Court of Auditors (**ECA**) Community Transit Questionnaire. This information was obtained through replies to a questionnaire regarding Community transit system, in preparation to audit missions foreseen in selected EU Member States. Due to time constraints, procedures and figures provided, for the period 1 May 2004 till 30 June 2005, were not tested to verify their completeness and accuracy.

Through this questionnaire, ECA sought to obtain an overview of the organisational structure and tasks of the administrative units involved in transit, as well as a basic understanding on the volume and management of Community transit operations carried out in all Member States. The audits carried out in selected Member States included an assessment of the functioning of the New Computerised Transit System (**NCTS**) and targeted the management of guarantees, enquiry and recovery procedures in Community transit.

NCTS provides for the input of electronic declaration and processing. It is based on technical standards (Functional Transit

Standard Specifications), established by the Commission and designed to enhance management and control of Community and Common Transit. Since 1 July 2005, all transit declarations must be made electronically by the trader via NCTS. NCTS is used by all the Member States of the EC, plus the EFTA countries.

Every country had to appoint a software house to develop a tailor-made system based on these standards. However, certain countries opted for a package with minimum requirements, issued by the Commission free of charge, referred to as Minimum Common Core (**MCC**). This is interfaced with NCTS. Malta uses MCC.

Key Issues

Lack of Established Procedures and Systems Documentation

It was noted that Customs lacks formal established procedures and systems documentation regarding:

- Guidelines or instructions for carrying out physical and documentary examinations related to transit are not in place. Examinations carried out are based on general unstructured guidelines that have been formulated through practice.
- Customs does not have a system, in the form of standard forms, data flows, etc., for collecting the results of examinations related to transit for analysis at central level. Such information is included in the general reporting of results of examinations.
- Currently, no standard forms are used for communication of general physical examination results. However, a standard form exists for reporting examinations of full load containers or group cargo, for local destination or in transit, when the examination is made outside the Freeport area. A copy of this form was not forwarded to NAO.
- There are no official written guidelines for general screening.

- Special instructions for the issuing, management and use of guarantees and guarantee waivers in transit do not exist. Malta makes no use of comprehensive guarantees.

Apart from the above, it could not be concluded whether established procedures and systems documentation are in place since:

- a brief description on how enquiry procedures (incoming and outgoing) related to transit operations are carried out and monitored in the local customs administration, by the Central Transit Office, was not given; and
- details regarding task description, information flows and control measures in place at different levels in relation to recovery procedures related to transit operations, were not provided to NAO.

Lack of Detailed Sub-Classified Information/Data

The following are instances when Customs Officers stated that data requested was either completely nonexistent or else could not be filtered to indicate figures relevant for transit operations:

- Information regarding Transshipment Shipping Bills (**TSBs**) – a paper based procedure, containing details of merchandise, used for non-Community goods arriving at Malta Freeport and transported to another local destination - issued between May 2004 and June 2005 in relation to national Community transit procedures was not available.
- Data maintained by CIS, on the number of physical examinations carried out in Malta, is not filtered to indicate which of these physical examinations relate to EU transit.
- Sub-classification details of major documentary offences were provided. However, these were not classified on a monthly basis. Additionally, the following details were not provided to NAO:

- Minor offences sub-classifications.
- The total number of transit units which passed through Malta during the period May 2004 till June 2005.
- Particulars about the number of physical examinations carried out on goods, whose destination was Malta and which were targeted as high risk by Customs.
- Additional breakdowns, regarding offices of departure and destination.
- Figures regarding amounts involved following enquiry procedures were not made available.
- Non-fiscal offences are not inputted in Customs Electronic System (**CES**) as opposed to major offences. These were recorded in a manual ledger up to December 2004 but has since been discontinued during 2005, leading to lack of audit trail in this regard.

Control Issues

Extent of Verifications made to ensure that Guarantees are Sufficient to Cover Duty Payable, is Questionable

The extent of verifications made by Customs Officers, to ensure that guarantees are sufficient to cover the duty value of goods, is questionable. Customs Officers stated that no detailed checks are executed on goods which arrived in Malta from a non-EU country and are in transit to another EU country. The officer only checks that the nature of the product in transit tallies with that described in the declaration.

The Relationship between Customs Debt Unit (CDU) and Other Units, Responsible for the Establishment of Guarantees is Unclear

Customs intended to have all guarantees dealt with at central level, i.e. by CDU. However, individual Sections within Customs still deal with guarantees and the role of CDU seems to be limited to maintaining guarantee

records based on information forwarded by the Sections in question. CDU does not have an active role in the administration of guarantees and collection of any potential subsequent debts. The roles and responsibilities with respect to guarantees, both by CDU and other Sections, are undefined. In fact, CDU could not comment about the frequency of groupage bond guarantee revisions.

With regard to transit guarantees, CDU acts according to instructions received from other responsible Sections, i.e. it does not follow-up guarantees but simply closes them off when it receives instructions in writing to do so. However, from a Common/Community Transit Procedure Guarantee document copy provided to NAO, as a documentation sample, it is evident that acceptance of individual guarantees on behalf of Customs is being done by the Customs Debt Manager, who endorses acceptance of individual guarantees accordingly.

Compliance Issues

Lack of Compliance re Guarantee Waivers

The individual guarantee must be used when the regular transit procedure is used by a trader who does not yet have a track record, qualify for a simplification or uses the transit system only incidentally. The individual guarantee has to be furnished for every transport movement, covering the full amount of customs duties, and other charges, like VAT or excise duties.

However, guarantee requirements can be relaxed given that compliance with a set of general simplification conditions are met and sufficient authority to use a particular simplification is received from the Customs authorities. The latter enables Customs to check compliance with the general and specific conditions governing the simplification concerned.

Customs Officers stated that verbal instructions were received to waiver

guarantees in case of particular traders, thus going against the requirements of the Customs Code and IP.

Old Transit System (OTS) Transit Procedures vs Manual Ledger Details

The Customs Economic Processing Unit (CEPU) provided monthly breakdowns on the number of OTS transit procedures for the period May 2004 till June 2005. Due to time limitations, figures provided were not cross-checked against the manual ledger by NAO prior to submitting the questionnaire to ECA. However, from subsequent manual ledger screening carried out it was noted that:

- the number of OTS transit procedures processed during March 2005 per summary sheet does not correspond to manual ledger details;
- although most T1s are consecutively numbered, there were some exceptions. In a particular case, the same T1 number was used on two (2) different dates and for different export vessels and exporters;
- several T1s were issued without supporting guarantees;
- the amount of duty payable was not always noted. It is not clear whether this implied a nil amount or otherwise, because in certain instances there were notes indicating duty paid. Again, it is not clear whether in these instances duty paid represents a portion of or total duty payable;
- it is not the norm to have the person endorsing his own updating of records;
- generally, manual records are not cross-referenced to relevant files for quick retrieval of supporting information; and
- in certain instances, it was noted that deposits had been refunded. However, this practice was not consistently applied.

Management Comments

Action was or is being taken with regards to irregularities noted. Customs further remarked that:

- Several training courses are organised by the Customs Training Unit on the basis of the annual Training Programme. However, whilst it is acknowledged that training is fundamental for efficient and effective operations, yet such training cannot substitute system and procedure documentation.
- Soft and hard copies of the Transit Manual are available in all Customs offices involved in the transit procedure. Customs officers were also provided with easy guidelines on the use of MCC.
- A system for collecting the results of examinations related to transit for analysis at central level *".....is already available in the Risk Analysis Report entered in the CES."*
- For communication of general physical examination results, the *".....standard Risk Analysis Report in CES is utilized.....supplemented with the Risk Information Form (RIF) referred to by CIS. Completed RIF's are forwarded to CIS by DG himself."*
- Lack of official written guidelines for general screening by the Verification Unit, is not perceived by the Department as being a problem since officers follow rules and procedures as detailed in the Community Customs Code, Customs Code Implementing Provisions and Standard Audit Manual. Officers can also make reference to the Customs Portal, featuring 900 questions and answers plus 20 different guidelines on Customs procedures.
- The Department is contending that a brief description on how enquiry procedures related to transit operations are carried out and monitored in the local customs administration, by the Central Transit Office, was provided to NAO. It is to be

noted that evidence at NAO indicates otherwise.

- Job descriptions exist for positions in Management as they all have a title description. However, it is not the case when no specific job title exists. To counter this disadvantage, the Department has established general objectives for the various sections within Customs.
- With regards to lack of information concerning TSBs issued in relation to national Community transit procedures, the Department commented that its *“.....function is to monitor that all third country goods, covered by a T1, are properly accounted for.”*
- The number of physical examinations carried out in Malta is not filtered to indicate which physical examinations related to EU transit, since no distinction was made between different kinds of cargoes. CIS keeps full records of every examination in the Risk Analysis Report in CES and in RIFs.
- Certain details requested by NAO were not available since only breakdowns, considered as essential to the Department's operations, are produced.
- With regards to enquiry procedure amounts, Customs pointed out that *“.....NAO were provided with actual customs records about the limited amounts of revenue that were in the process of recovery in July.”* However, details provided to NAO were limited to the number of enquiry notices started in 2004 and 2005, sub-classified by country, and respective results.
- The Department considers that its current reporting systems satisfy the need for accurate, reliable and real time data. According to Customs, the production of excessively detailed statistics would be a waste of time and resources.
- Guarantees are normally raised on documents provided by the trader. In exceptional circumstances, usually where goods or the trader have a high risk profile, a physical check is also undertaken in order to ensure that documents accurately reflect the nature and value of the goods.
- The Department is of the opinion that its management policy, allowing guarantee related decisions to be taken by the respective head of section or at times even at the level of Director or Assistant Director, is the most practical and safe solution based on experience and expertise not theoretical ideas. The CDU's role is to extend guarantees in good time. On the other hand, CDU stated that it acts according to instructions received from other responsible Sections. It does not follow up guarantees but simply closes them off when it receives instructions to do so.
- T1s issued without supporting guarantees were in respect of '0' rated goods.
- Records are normally updated by a member of the staff of a particular section while the endorsement is effected by the officer in charge.
- Cross-referencing of manual records is not considered necessary since T1 manual records are identified by the relative T1 number.
- All refunded deposits are authorised by the Head, Industries Section.

Customs Department

Traditional Own Resources

Background

Traditional Own Resources (**TOR**) are considered as the 'natural' own resources, since they are revenue collected by virtue of Community policies rather than revenue obtained from the European Union Member States as national contributions. Own resources currently come from customs duties, agricultural levies, sugar contributions, a fixed-rate portion of value-added tax (**VAT**) receipts and a fixed-rate levy on gross national income (**GNI**).

Potential risk areas were identified during meetings held with Customs Department, in conjunction with the ECA mission held in September 2005, in respect of the Statement of Assurance for the Financial Year 2005 (DAS 2005) concerning TOR. Issues mentioned are based solely on information obtained through meetings held and as observed during the European Court of Auditors (**ECA**) TOR audit. Detailed findings and observations, in connection with TOR, which resulted consequent to the ECA's audit were presented in the ECA audit report.

Audit programmes – dealing with central Customs accounts, B accounts, national Customs supervision, inland Customs office controls and Customs entries - were forwarded to NAO and Customs, prior to the audit. NAO was also requested to forward information, including a description of TOR accounting practice, to the ECA. NAO opted to act as an observer rather than participate in the ECA audit, as detailed in Article 248(3) of the EC Treaty.

Key Issues

Deficiencies re 'A' and 'B' Account Statements

The monthly 'A' Account is compiled from Customs Electronic System(**CES**) extracted data and data obtained from Post Office branches. Data reflects monthly duty payments inputted in CES by Cash Offices. Maltapost and its Branches also gather duties on behalf of Customs and forward the funds accordingly. Maltapost has access to CES, through its Head Office. Hence, parcel post duties which originate at Maltapost Head Office are immediately entered into CES by the latter and automatically allocated to respective status. This does not apply to duties collected by Post Office Branches since these do not have access to CES. The latter duties have to be added to the 'A' Account Statement by Customs Debt Unit (**CDU**).

The 'B' Account should be used for any duty amounts which either have not been paid or guaranteed, or have been guaranteed but are being challenged by the trader. Amounts have to be transferred to the 'A' Account and paid immediately, once the trader accepts liability for payment.

The following points were noted in relation to 'A' and 'B' Account Statements:

- CDU stated that the 'B' Account is not used since generally goods are not released prior to receiving cheque payments for any outstanding amounts, from traders. Even when payments are not effected immediately, amounts are still added to the

- 'A' Account, to be passed to the Commission. The issue of unlawful introduction of goods in Malta per Articles 202(1)(a), 202(2) and 233(d) of the Customs Code, was being overlooked by Customs and a nil 'B' Account Statement was being sent to the Commission, on a quarterly basis. Typical 'B' Account amounts include duties due on inland seized smuggled goods and additional duties due following post clearance audits.
- The computer generated report which was originally being used by Customs to compile the 'A' Account Statement was incorrect, due to a system bug, resulting in amounts in excess of actual TOR due being passed to the Commission. This resulted since Customs relies exclusively on system generated data and does not check or reconcile any of these figures. Customs argued that now another report is being used to compile the 'A' Account Statement and that this report is providing the right information. However, a thorough systems audit needs to be carried out to ensure its reliability.
 - CDU does not reconcile 'A' Account Statement details with those of supporting declarations. Figures provided to the Commission are as generated by the system.
 - CES does not have a separate code for agricultural duties. When compiling the 'A' Account Statement, the Computer Section is requested to filter details regarding agricultural duties, to be shown separately in the 'A' Account Statement. Checks on data extracted by the Computer Section are not carried out.
 - CDU is informed of total duty collected by Post Office Branches. However, it is not provided with information supporting the amount.
 - Management control on building the 'A' Account Statement seems to be deficient. Any checks made should be documented. Manual declaration inputs should be double checked by a second responsible person, to detect any errors of origin and correct them immediately.
 - Although uncollected dues would have already been transferred to the Commission through the 'A' Account, these could involve certain declaration errors (for example double entries) which have remained undetected and amounts kept outstanding as pending declarations. If traders fail to pay within ten (10) days from the departmental letter date, and in the absence of adequate guarantees, CDU stated that the Enforcement Unit should be asked to try and collect dues at the traders' premises. However, till August 2005, CDU never liaised with the Enforcement Unit to collect outstanding duty and VAT dues.

By so doing, Customs is safeguarding the Commission by sending funds immediately, including uncollected ones. However, from the Government of Malta's point of view, this situation is leading to cash flow discrepancies as well as to unnecessary administrative work, in cases of funds which have to be reclaimed back from the Commission.
 - The Customs Department Malta Manual on Procedure to Compiling 'A' and 'B' Account was prepared by Customs in 2004. This Manual provides an overview of the operations and procedures involved. NAO noted that the Manual should be updated to reflect actual procedures being implemented. It should provide detailed sub-classifications of procedures, tasks, roles, responsibilities and controls. The Manual should manifest best practice with regard to 'A' and 'B' Account compilations.

Release of Goods Prior to Duty Payments

CDU noted that there were instances when goods were released prior to payments being effected. CES would not be indicating the correct status of the goods in question, since the system would still show the Status of the goods as if not released. Although CDU noted that the probability of such an occurrence is remote, yet there is the risk that once goods are physically released, related TOR payments would have been transferred to the Accounting Module for

inclusion in the 'A' Account, whilst in actual fact amounts would still need to be collected by Customs.

Control Issues

Stock Control and Other Deficiencies Noted During Visit to Hal Far Groupage with ECA Auditors

During the visit to Hal Far Groupage, the following points were noted:

- There is no procedures documentation. Training courses are provided instead. However, this could lead to lack of continuity in cases of staff turnover.
- Community and third country goods were stored together:
 - Items were not adequately tagged to indicate origin.
 - Not all non-EU goods were actually in non-EU bays – this could cause misplacements especially if items are not tagged.
 - Not all non-EU goods were adequately sealed.
- No regular stock controls are executed to ensure that warehouse stock items correspond with details per stock records.
- There seem to be inadequate controls with regard to temporary storage periods. According to the Community Customs Code, Article 49(1)(b), such goods should be released within twenty (20) days. However, it was noted that Customs takes action to remove such goods after three (3) months. This is the time stipulated by the Customs Ordinance, Article 19(2), prior to Government expropriating the goods (Customs Ordinance Article 20(1)). There seems to be a conflict between local legislation still in force and EU Customs legislation, which should prevail.

It is not always possible to ascertain the length of temporary storage from boxes since not all Groupage operators display this information. Stock which should have

long gone out of temporary storage was still being kept there.

- Transit Accompanying Documents (T1/T2) are not being released by Customs immediately upon arrival of goods at Hal Far. Customs is informing the country of departure about the arrival some days after the actual arrival, when the trader presents the relevant documents and the release operation is completed.

Unauthorised System Generated Refunds (SADRs)

An SADR is automatically created by the interface location between the Import and Accounting Modules in CES. It may be created for several reasons. For example, if a trader becomes aware that a wrong HS Code was entered in his declaration, he must inform Customs about the matter, and the latter must decide whether to allow a change in HS Code, and hence automatically generate a refund, or else refuse the request and generate a refund to the trader, through a refund entry by CDU, at a later stage.

When checking SADRs created, CDU noted that unauthorised personnel were entering the system and creating unnecessary SADRs. This situation arose due to:

- lack of sufficient inbuilt controls in CES, to prohibit such modifications from being carried out; and
- high staff turnover. New recruits at the Verification Unit were not cognisant of the fact that they were creating SADRs and were not informed immediately not to enter in particular system modules.

SADR problems were also encountered due to system interface problems. For example, the system automatically created an SADR when an attempt to modify data in a barred trader's account was made. To modify erroneous SADRs, the CDU, Verification Unit or Airfreight Section must recoup erroneous refunds from the importers' suspense accounts.

When contacted about the lack of

preventive controls with regard to new SADR creations, the Computer Section confirmed that it is aware of this problem but stated that having the necessary controls in place involves a time-consuming exercise. The required amendments might be effected in the future. However, the Computer Section did not indicate any timeframes. This Section is not aware of whether similar problems are faced in other countries using a comparable system, such as Cyprus.

Compliance Issue

Lack of Adequate Communication Documentation re Deferred Payments

Deferred payments that can be granted on SADs are not permitted on post entries since the post entries utility in CES does not function for deferred payments. Therefore, post entry amounts have to be settled there and then. CDU stated that it has verbally informed the trader, instead of informing him in writing, that Customs granted the deferred payment facility.

Management Comments

Action was taken or is being taken to address irregularities noted. Management further remarked that:

- Although the CES was not immediately updated to record funds as settled, in actual fact the funds due were already collected. Inland seizures of goods are “..... normally entered in the ‘B’ Account once they are reported to the CDU”.
- Release of goods prior to duty payments occurred in isolated instances and during the initial period of CES operations.
- With regards to lack of procedures documentation at Hal Far Groupage, Customs noted that a manual outlining procedures was handed to NAO. NAO considers this presentation as a general

overview of procedures adopted at Hal Far Groupage.

- The use of tags by operators is not an established procedure. According to Customs, it is enough that goods are stored in an identified area.
- Non-EU goods are not sealed.
- Due to lack of computer hardware, Customs was not in a position to monitor stocks through CES. However, bond operators are obliged to keep complete stock records.
- Goods overdue in temporary storage are now being monitored by the CES manifest module. Overdue goods are being transferred to the Government Bond set up at Hal Far thus limiting the possibility of goods being misplaced.
- T1 documents are settled immediately when presented to Customs Office at Hal Far. Customs Officer at Hal Far is not in a position to follow up and close transit procedure if the place of destination in the T1/T2 Documents is incorrect.
- In many cases it is not possible for operator to present T1 document at time of entry at Hal Far because T1 may be in possession of the Importer.
- The absence of sufficient inbuilt controls in CES to prohibit unauthorised modifications represents a file access problem. *“New access groups will be created with correct permissions but at present the Ministry is holding discussions with suppliers to conclude the contract.”*
- SADR problems encountered due to system interface problems represent *“.....a system bug that still has to be resolved.....The only solution until this bug is solved was to grant access to all officers.”*

Public Debt Budgeting

Background

The public debt definition applied by Government refers to Budgetary Debt, thus excluding Extra Budgetary Units' (EBUs) and Local Councils' debt. Contingent liabilities do not form part of the public debt definition.

The Maastricht debt refers to General Government Debt, i.e. Central Government Debt (Budgetary Debt and EBUs debt) and Local Councils' debt. Although Government started referring to "The Concept of General Government" in the 2005 Budget Speech, the 2005 estimates were based on the Budgetary Debt concept.

Malta's debt composition is dominated by domestic borrowing, which consists of Malta Government Stocks (MGS) and Treasury Bills. Foreign debt is always project oriented and only constitutes a small share of total debt.

When Malta joined the Exchange Rate Mechanism II (ERM II), in May 2005, it made a commitment to contain current Government expenditure and lower the high debt level.¹

The purpose of the audit was to examine procedures adopted by the Ministry of Finance (MF) and the Treasury Department

for public debt budgeting purposes and if indicated to propose recommendations for improvement.

During the audit, reference was made to Treasury files and several other documents, as detailed in Appendix 1 to this report. A list of INTOSAI Public Debt Committee reports, referred to in the research and planning stage of this audit, is provided as Bibliography to this report.

Key Issues

Limitation on Scope of Audit

Testing of systems and procedures supporting public debt budgeting could not be performed since the public debt budgeting process is not fully documented and lacks audit trail. This report is thus compiled solely on information obtained through meetings held. All meetings with Treasury and MF officials were documented and referred for their comments and further clarifications.

However, up to the report writing date, the National Audit Office (NAO) did not receive comments from:

- MF Permanent Secretary regarding his views on the setting up of a Debt Management Office (DMO); and
- MF, Director General, Financial Administration,² following a request to expand further on the Ministry's role in the monitoring of project oriented loans.

The MF Public Debt Management Advisory Committee (PDMAC) papers were

¹ Governments deficit as a percentage of Gross Domestic Product (GDP) fell from five per cent (5.1%) at end 2004 to almost four per cent (3.9%) in 2005. The debt to GDP ratio was almost seventy-seven per cent (76.7%) in 2005. These ratios will have to be in line with the Maastricht Treaty criteria i.e. reduced to three per cent (3%) and convergent towards sixty per cent (60%) respectively, if Malta is to adopt the Euro in 2008. (Source: Central Bank of Malta (CBM), Annual Report 2005)

² Officer retired from Public Service.

not made available. As a result, the PDMAC terms of reference and the regularity, with which PDMAC meetings are held, could not be ascertained.

Inadequate Formal Public Debt Planning Organisational Structure

Since a formal documented public debt planning organisational structure is not in place, it could not be ascertained whether sufficient structured planning is being executed.

No Formal Debt Management Strategic Plan

- A debt management strategic plan has not been formulated. Failure to have an adequately documented public debt strategic plan could lead to:
 - the non-attainment of specific objectives, such as:
 - guaranteeing sufficient liquidity to pay current obligations;
 - a target average debt maturity;
 - a target average debt servicing cost; and
 - a desired mix of foreign currency debt and active domestic debt; and
 - inefficient public debt control management.
- The Public Debt Section within Treasury does not have written public debt procedure guidelines to follow, which could give rise to inadequate debt management and insufficient controls being exercised on activities carried out by Public Debt Section personnel.

The fact that Public Debt Section personnel have interchangeable roles could avoid languishing of duties when the responsible persons are away. However, it could pose accountability problems, particularly if there is insufficient evidence to indicate who actually performed a particular task.

Public Debt Mix lacking Policy Guidelines

- There is no written policy regarding the attainment of a balanced public debt mix - according to financial, legal and risk factors, between short and long term, local and foreign debt. The types of communication that should be present among the parties involved in the planning and monitoring processes, as well as relative roles and responsibilities, are not documented in a formal public debt planning and monitoring procedures manual. Hence, the type and level of interaction among the parties involved as well as whether a macro, consolidated perspective is adopted for public debt planning and monitoring could not be ascertained.
- Projections may be revised several times due to changing conditions and circumstances. However, changes and related underlying assumptions are not sufficiently documented, authorised and filed in a structured manner to enable quick retrieval and provide an adequate audit trail.
- A detailed plan of local public debt fund allocations, against pre-specified expenses and projects, is not in place. Debt finances one part of capital expenditure, but neither MF nor Treasury is in a position to directly relate a specific debt to a particular capital project.

Non-functionality of the PDMAC

- The role of the PDMAC, as it was originally set up, had to address the macro public debt planning agenda. However, the main focus of most PDMAC meetings was on operational matters surrounding local debt issues and little reference was made to foreign debt.
- The PDMAC may not be fulfilling its task once it:
 - does not meet regularly or at least prior to every stock issue;
 - is not giving advise to Government on long term borrowing strategies;

- does not discuss foreign loan financing;
 - is not involved in the determination of annual local public debt thresholds; and
 - does not have an active role in establishing bond issue amounts and related servicing costs, prior to the issue of bonds.
- In response to the question on the current role of the PDMAC, the Permanent Secretary, who chairs the Committee, explained that over time, the role of the PDMAC changed. Tasks originally undertaken by the Committee are now being executed by the different parties concerned, as part of their day-to-day operations. The need for a PDMAC meeting may only be felt in exceptional cases.

Inadequate Formal Authorisation Procedures for the Publication of MGS Annual Issuance Calendar and for New Government Stock Issues

There are no formal authorisation procedures for the publication of the MGS annual calendar and for new Government Stock issues:

- Treasury seeks approval for the issue of the MGS Annual Issuance Calendar from the Permanent Secretary, MF. The Budget Operations Division (**BOD**) is not involved in the approval of the MGS Annual Issuance Calendar.
- Prior to initiating procedures for the issue of new local loans, the Accountant General requests approval from the Permanent Secretary, MF.

Lack of Communication between MF and Treasury Department

- Policy decisions, regarding GDP and deficit targets, are taken by MF and are not discussed with the Treasury. The annual local public debt projections are made by the Treasury on the three (3) year Public Sector Borrowing Requirement (**PSBR**) forecasts.

- Treasury is not officially informed about potential new foreign loans although it is responsible for compiling foreign loan servicing cost projections. Foreign debt servicing costs “projections” as prepared by the Treasury, are only based on existing loan agreements.
- Even though BOD and Treasury carry out interconnected tasks, yet they fall under different MF Directorates.
- No discussions, regarding public debt servicing forecasts, are held between Treasury and BOD, even though the latter receives public debt servicing cost projections from the Treasury.

Failure to Set Up the Debt Management Office (DMO)

- *DMO: Way Forward*

The establishment of a DMO, with the aim of strengthening public debt management, was mentioned by the Minister of Finance in the 2003 Budget Speech. Procedures to set up this Office have not yet been concluded.

A Treasury Restructuring report, dated April 2004, by the Management Efficiency Unit (**MEU**) is waiting the approval of the Permanent Secretary, MF.

- *Inadequate Treasury Staff Expertise*
 - The posts of professionals, comprising of a systems manager, a principal (public entities) and financial economist, are still vacant.
 - Treasury Department lacks expertise regarding:
 - Risk management techniques.
 - Market mechanisms.
 - Capital market resource mobilisation.
 - Analytical tools.
 - Management information systems.
 - Complex debt instruments.

and as a result the Treasury:

- does not have independent risk and market evaluations and has to rely on external feedback; and
 - suffers from deficient risk management and may not be in a position to address issues which are fundamental for satisfactory and professional debt planning and monitoring.
- *System Errors and Failure to adjust Treasury Debt Planning and Management Practices accordingly*

Certain system errors have remained unresolved and as a result the Commonwealth Secretariat Debt Recording and Management System (**CS-DRMS**) is not being used by Treasury Public Debt Section. Due to delays regarding the setting up of the DMO, Treasury cannot take advantage of the help offered by Commonwealth Secretariat.

There is the danger that CS-DRMS might become obsolete or need to be upgraded by the time it starts being implemented.

Although action to install a debt management IT system has been taken, Treasury's debt planning and management practices to date have not been re-engineered in line with the facilities offered by the computerised information system.

- *Utilisation of British Government Funding*
- Funds, to cover the costs of the technical assistance provided in setting up the DMO, were received from the British Government. However, Treasury was not in a position to negotiate a contract for the second phase of the project as the necessary approval has not yet been granted.

Inadequate Storage of Communication Documentation by Treasury

The validity and completeness of random 2004/5 e-mails examined do not constitute sufficient audit evidence that all relevant MGS issue communications between Treasury and

MF and within Treasury are being documented, for easy future retrieval.

Inadequate Means of Disaster Recovery at Treasury

Treasury does not maintain hard disk backups nor is the Department equipped with a server to back up data on a daily basis. A lot of data is stored locally and cannot be exclusively obtained, in real time, from other sources. Although certain data could be retrieved from documents held at Treasury and from other institutions, in case of a disaster, it would be difficult to ascertain the completeness and accuracy of restored information.

Control Issues

Evidence supporting Debt Related Decisions and Communication not provided by MF

- Informal meetings are held at MF regarding revised financial projections.
- The absence of documentation, of decisions taken, reasons supporting them and appropriate approvals, leads to an inadequate audit trail.

Insufficient Reasons provided in the 'Variances in Revenue for Financial Year' Statement in Part I of the Annual Financial Report

The uses of this statement, comparing annual budgeted revenue estimates (including local and foreign loan proceeds) with respective actual amounts, are restricted since:

- detailed reasons for variations identified are not provided; and
- variances are not sub-classified to help users, better ascertain the nature of variances.

Continuous Public Debt Budgeting Approach

No evidence was found supporting a continuous public debt budgeting approach,

through joint MF and Treasury coordination and communication.

Inadequate Treasury Bill Authorisation and Communication Documentation at Treasury

- In cases when the Assistant Director, Administration, feels that there might be inaccuracies in projected revenue figures in the weekly Swing Operation Report, he verbally communicates his concerns to the Cash Office and the latter rechecks amounts accordingly.
- Any envisaged daily cash deficiencies detected by Treasury's Accounts Section, are normally verbally communicated to the Accountant General.
- The Accountant General grants verbal approval to the Assistant Director, Administration to proceed with the:
 - printing and distribution of the Treasury Bills issuance calendar; and
 - allotment of Treasury Bills.

In both cases, approval is always granted following verbal discussions between the Accountant General and the Assistant Director.

Verbal approval does not constitute sufficient audit evidence and indicates the absence of satisfactory procedural controls.

Treasury Bill Tender Forms received by Treasury not stamped

Treasury Bill tender forms, posted in the tender box located at the Treasury's Customer Care, are not stamped by Treasury, to indicate receipt dates, resulting in lack of controls ensuring that late tender forms received, are not accepted, except in genuine cases.

Market Intervention through Sinking Fund Investments

Sometimes Treasury temporarily utilises Sinking Fund Deposit amounts, to fund cash flow requirements. However, the Accountant General stated that Sinking Fund amounts

are not being used to invest directly. Rather when insufficient amounts are raised, Treasury Bills are not wholly rolled over and in cases of exceptional shortfalls in revenue or unforeseen urgent payments, funds from the Sinking Fund Deposit account at CBM are temporarily transferred to the Public Account. These funds, together with accumulated interest, are re-transferred to the Sinking Fund Deposit account, during the year but prior to year end.

It was noted from filed correspondence dated October 2004 that the use of the Sinking Fund to underwrite any stock not fully subscribed, had been suggested. Although this practice is allowed by the Local Loans (Registered Stock and Securities) Ordinance, Article 27 (1), IMF had advised that intervention of sinking funds in Treasury Bill/Bond issues is not reflective of a liberalised market. Treasury stated that when Sinking Funds are used to underwrite stock, the cut-off rate is used in order to inhibit market intervention. However, no written policy, in this regard, was made available to NAO.

Sinking Fund Transfers not accounted for separately

All Sinking Fund transfers to the Public Account are transferred to one account – Contributions to Sinking Funds account. Similarly, only one Public Debt Cashbook is maintained in the Department Accounting System (DAS) for all related transactions.

Incomplete Sinking Fund Transaction Records at Treasury

Whilst transfers between the Sinking Fund Deposit account and the Public Account, are recorded by CBM, corresponding transactions are not recorded immediately by Treasury in DAS implying that Treasury's records would not be updated to provide a true and fair view of the state of affairs, at a particular point in time.

The CBM Credit Advice sent to Treasury is utilised to enter the amount transferred in a Suspense Account. It is only when funds, together with accumulated interests, are

transferred back to the Sinking Fund Deposit account that a commitment is created through DAS using the Suspense account. The premise behind this approach is that these funds, together with accrued interest, will, at the earliest possible but prior to year end, be re-transferred to the Sinking Fund Deposit account.

In one out of three batches of Sinking Fund transfer related documents inspected at random, it was noted that no accrued interest was transferred back to the Sinking Fund Deposit Account, without a valid explanation forwarded.

Lack of Evidence showing that Treasury makes reference to Previous Years' Variances in Public Debt Planning

No evidence was provided to indicate that when making Government Stock projections, Treasury makes reference to past years' performance, to check whether any variances arose from factors which might be repeated in the coming year(s).

Compliance Issue

Non-enforcement of Cash Flow Projection Circulars 10/2001 and 6/2003 by Treasury

Except in the case of major revenue generating Departments (namely the VAT Department, the Inland Revenue Department and Customs Department) Treasury does not enforce the requirements of Circulars 10/2001 and 6/2003. This is done irrespective of the counter-provisions contained in Circular 6/2003.

Recommendations

Key Issues

Inadequate Formal Public Debt Planning Organisational Structure

A detailed formal documented public debt planning organisational structure should be set up.

No Formal Debt Management Strategic Plan

- A written public debt strategic plan should be formulated, taking into consideration short, medium and long term public debt objectives and action necessary to attain such objectives. The strategy should address the debt management necessary, to raise the required amount of funding, pursue its risk and cost objectives and achieve any other public debt management goals set by Government.
- Public debt procedure guidelines should be devised and explained to Treasury Public Debt Section personnel, to ensure compliance accordingly.
- Procedures to be adhered to will have to be designed to ensure that sufficient inbuilt controls are present to warrant transparent and proficient debt management.
- Treasury Staff with interchangeable roles should be identified and controls established and enforced to allow quick identification of the person who actually executed the task.

Public Debt Mix lacking Policy Guidelines

- A macro approach to public debt planning and monitoring should be adopted whereby the mix of short and long term, local and foreign debt, should be analysed strategically and established to achieve common sustainable goals, resolved in the public debt strategic plan. The public debt mix should be ascertained after taking into consideration key financial, legal and risk issues.
- To achieve this target, all parties involved in public debt issues should provide their input and actively communicate and participate in the attainment of common goals.
- Reasons justifying public debt mix decisions taken should be suitably documented for future reference.

- A detailed plan of local public debt fund allocations against pre-specified expenses should be compiled and utilised for monitoring, performance measurement and variance analysis. Regular debt monitoring should be exercised through a well-defined, structured and organised process.

Non-functionality of the PDMAC

- The role of the PDMAC should be clearly defined and communicated to the parties originally involved.
- The Committee should be responsible for establishing a global concrete long term public debt strategy, including the public debt mix, as well as align and review short term decisions, in order to achieve established long term targets accordingly. Clear terms of reference should be formulated.
- It is important for Government to be able to have a team of professionals to work hand-in-hand with and establish criteria, as well as take the necessary action to attain public debt objectives.

The team should consist of individuals with experience in the fields of investments, economics, statistics, corporate finance and risk management. Its role should be that of ongoing comprehensive public debt planning and risk management. All decisions taken should be supported with documented justifications and written approvals.

Inadequate Formal Authorisation Procedures for the Publication of MGS Annual Issuance Calendar and for New Government Stock Issues

- Formal MGS issue approval procedures should be established and documented.
- As much as possible, a prospective approach to stock issues should be adopted. Discussions and approvals should be sought in anticipation of such issues. The time period, within which such approvals should be granted, should be clearly stipulated and established in such

a manner so as to provide adequate lead time prior to the issue proper.

- Treasury should only proceed with new issues once the appropriate authority to do so is received, as highlighted in the procedures:
 - In circumstances whereby, due to other fundamental duties, the Parliamentary Secretary and/or the Permanent Secretary cannot provide their approvals, a written authorisation stating that the MF Director General, Financial Administration, can take stipulated decisions in their absence should be made.
 - Decisions taken by the Parliamentary Secretary should be final and should not be superseded. The Permanent Secretary should put forward his recommendations to the Parliamentary Secretary prior to the latter granting his final approval.
 - In exceptional circumstances, when authorised amounts need to be changed, these should only be made by the Minister or Parliamentary Secretary and documented accordingly. Verbal communications do not constitute sufficient evidence of decisions taken.

Lack of Communication between MF and Treasury Department

- Policy decisions taken by MF should be communicated in writing to all key players who influence public debt decisions, particularly the Treasury Department. All documents should be stored in a systematic manner for quick future reference.
- Communication channels have to be specified and the timeliness of reporting enforced.
- Even if Treasury does not have first hand influence in foreign loan planning, prior to compiling foreign loan servicing cost forecasts, it should liaise with MF to obtain an understanding of projected foreign loans and the likelihood of their realisation. In

case of loans, the realisation of which is still uncertain, a note stating the estimated amounts should be included in forecasts prepared to guide users accordingly. In this manner, the value added of projections will be enhanced.

- In view of the fact that the roles and responsibilities of BOD and Treasury are interrelated, these should be accountable to the same Directorate General.
- Since BOD is ultimately responsible for formulating public debt servicing cost projections, it should have more active input in their formulation, other than assessing the mathematical correctness of amounts provided by Treasury. Treasury and BOD could discuss projections prior to their preparation, to ensure that both parties are engaged in estimate formulation.
- All communications between BOD and Treasury, which ultimately result in revised public debt servicing cost estimates, should be documented and adequately stored for quick future reference.
- Extracts of foreign institution reports received by MF and CBM, which could influence public debt decisions based on recommendations put forward by Treasury, should be made available to Treasury on a timely basis.

Failure to Set Up the Debt Management Office

DMO: Way Forward

- In order to ensure effective debt planning and management, the current Treasury Public Debt Section needs radical restructuring.

Inadequate Treasury Staff Expertise

- The staff complement, necessary for effective functioning of the DMO needs to be clearly defined and related job descriptions and responsibilities portrayed.

- Professional, qualified and experienced personnel to occupy headship positions need to be employed. These should participate in decision making procedures, particularly those involving intricate debt instruments and guide existing staff, accordingly.

Current Public Debt Section personnel should be provided with continuous training regarding finance issues, to help them in their day-to-day operations.

System Errors and Failure to adjust Treasury Department Planning and Management Practices accordingly

- Effort should be made by Treasury and MF to have:
 - system errors corrected; and
 - intensive training, regarding retrieval and interpretation of data, provided to staff.
- Information System personnel needs to be employed, to keep abreast with IT developments and ensure:
 - real time access to DMO staff;
 - timely information system updates; and
 - security of data.

Utilisation of British Government Funding

- Prior to making official requests for funds, MF and Treasury should discuss the matter. Discussions should be based on an analysis about the best use that can be made of potential funds, so as to reap utmost value added. This evaluation should take into consideration:
 - cost sub-classifications and estimated amounts payable;
 - reasons why such costs are being incurred; and
 - time when amounts will be due and payable.

Decisions taken and MF approvals should be in writing.

Inadequate Storage of Communication Documentation by Treasury

All correspondence regarding prospective loan issues should be adequately documented and stored systematically for quick future reference. Separate files should be opened for every new MGS issue and should enclose all relevant documentation.

Inadequate Means of Disaster Recovery at Treasury

Treasury should guarantee that all data is methodically stored and backed-up to warrant rapid and absolute retrieval if a disaster occurs.

Control Issues

Evidence supporting Debt Related Decisions and Communication not provided by MF

- All public debt decisions are to be documented together with reasons explaining revised estimates and justifying decisions taken in this regard. These documents should be endorsed by the decision making team and kept with other evidence used in arriving at conclusions.
- It is not enough to maintain templates which indicate amended data. The templates, related adjustments and the rationale behind such modifications should be adequately documented, approved, stored and made readily available for future reference.
- MF should inform Treasury, in writing, about public debt decisions made. This communication should be well-timed to warrant consideration of all pertinent criteria in public debt projections, prepared by Treasury.

Insufficient Reasons provided in the 'Variances in Revenue for Financial Year' Statement in Part I of the Annual Financial Report

- In order to enhance the value added reaped by users of the Variances Statement:

- variances should be further sub-classified to better ascertain their nature; and
- reasonable justifications for variations identified should be provided to Annual Financial Report users.
- Detailed variance explanations should be prepared and maintained by MF for internal use. Such information would help identify potential problematic areas as well as aid performance management.

Continuous Public Debt Budgeting Approach

A continuous public debt budgeting approach, through co-ordination and communication between MF and Treasury, should be applied. Government's public debt targets need to be assessed regularly in view of changes in Government's financial performance and position. This will ensure effective cash flow management and the attainment of long term public debt objectives.

Inadequate Treasury Bill Authorisation and Communication Documentation at Treasury

- Reasons indicating recommendations made, and justification of decisions taken, should be documented.
- All approvals should be in writing and be adequately stored for future retrieval.

Treasury Bill Tender Forms received by Treasury not stamped

Treasury Bill tender forms should start being stamped upon receipt to indicate the date of receipt.

Market Intervention through Sinking Fund Investments

- Sinking Funds should not be used for underwriting Government securities.
- The Local Loans (Registered Stock and Securities) Ordinance should be amended to avoid any market intervention by Government.

Sinking Funds not accounted for separately

A distinction should start being made between capital and profit and loss items. All funds should have individual capital and profit and loss accounts. This accounting structure will be of particular importance following the introduction of Government accrual accounting.

Incomplete Sinking Fund Transaction Records at Treasury

All account transactions should be recorded real time by Treasury. This will guarantee a satisfactory audit trail of all realised transactions.

All accrued interest on Sinking Fund Deposit amounts should be accounted for once amounts are re-transferred back from the Public Account to the Sinking Fund Deposit Account.

Lack of Evidence showing that Treasury makes reference to Previous Years' Variances in Public Debt Planning

Where appropriate, prior year public debt variances should be taken into consideration when preparing new forecasts.

Compliance Issue

Non-enforcement of Cash Flow Projection Circulars 10/2001 and 6/2003 by Treasury

Even though major revenue generating Departments might have the most significant impact on Treasury Department's weekly cash flow projections, yet since Circulars are to be complied with by other Ministries/ Departments, Treasury should ensure that all involved comply, otherwise action is to be taken accordingly.

Management Comments

No comments regarding this report were received from the Permanent Secretary, MF. Comments forwarded by BOD excluded any

points with regards to those areas falling outside their direct competence.

Key Issues

Inadequate Formal Public Debt Planning Organisational Structure

Ministry of Finance

BOD explained the overall planning structure applied within MF and with Treasury and stated that *"The existence of a planning organisational structure is now evident from the explanation.....which also refers to the procedures being followed and responsibilities of each sector..... Action will be taken in order that, where applicable, communications made between the parties concerned will be formalised through the necessary additional documentation."*

Treasury Department

"The organisational structure for debt planning is embedded within the Administrative organisational structure itself. All players contribute towards the debt planning exercise resulting in the determination of the optimal strategy to be adopted. Both communication channels and responsibilities are dictated by the above mentioned administrative arrangements."

No written documentation supporting this formal structure was provided and no indication regarding action to be taken, was forthcoming.

No Formal Debt Management Strategic Plan

Ministry of Finance

BOD did not comment about having a written debt management strategic plan. Instead, a description of procedures adopted was provided. No documentation to support statements made was provided to NAO.

Treasury Department

- *"The outcome of the debt management strategic plan is incorporated within Malta's*

Convergence Programme. Maintaining debt at sustainable levels over time remains the key factor within the macro-economic scenario.

- *In terms of the recommended contents of the debt management strategy mentioned by the Auditor General, one has to point out that all these are currently pursued, in some form or another, although, of course, the allocation of resources to these specific areas would finally enhance the overall management of Public Debt.”*

Public Debt Mix lacking Policy Guidelines

Ministry of Finance

BOD did not comment about action to be taken regarding observations noted and recommendations forwarded. It was commented that communication channels amongst the parties concerned exist and that projections made are not subjective. It was also pointed out that:

“With the exception of foreign loans (no new foreign loans are currently being resorted to), which are project linked, the dynamics of the PSBR do not necessitate that the remaining part of the PSBR needs to be broken down according to ‘pre-specified expenses’”.

Treasury Department

- *“The fact that decisions on Public Debt issues are taken by different players does not necessarily imply that there is no balanced mix according to financial, legal and risk factors. All these factors are given due consideration by all parties concerned through consultation and discussions. Admittedly not all meetings are minuted. The macro consolidated perspective is inevitably discussed on an ongoing basis given that Malta is bound by legislation to report on the macro-level to institutions such as the EU (through the Convergence Programme and Fiscal Notification of Debt and Deficit), IMF and other local and foreign institutions.*

- *Although there may not always be formal minuted documentation of meetings held, one cannot conclude that “there is no interaction between the parties involved in the planning process”. In fact various discussions take place during the year in different fora.the Treasury also taps on the resources of other entities which have the necessary experience in the relative fields.*

- *In the case of local loans servicing projections, these cannot be “subjective” in view of the fact that amounts and rates are known in advance. On the other hand Treasury Bills interests are determined by the market and are therefore subject to variations.*

In terms of projected stock positions, these may indeed vary during the year depending on the prevailing market conditions and/or other factors such as the timing or absence of privatisation proceeds.

This notwithstanding explanations on variations may be found in various correspondence exchanged between the Treasury and the Ministry of Finance during the year.”

Evidence of the above, through systematic complete filed correspondence exchanged between Treasury and MF, was not provided to NAO. Treasury failed to indicate whether action, to have organised public debt decision documents, will be taken in future.

Non-functionality of the PDMAC

Treasury Department

The Accountant General commented that although from Treasury files provided to NAO during the audit, “.....the topic relating to the maturity profile of debt would appear ‘to have been curtailed’, actual correspondence between the Accountant General, the Ministry of Finance, the Central Bank of Malta and the Malta Stock Exchange prior to each and every stock issue would show otherwise. In fact, the maturity profile of existing stocks as well as projections on

ceilings and future maturities features prominently in almost every such correspondence. Although the PDMAC may not have tackled this issue during a formal meeting this topic is frequently debated amongst the entities concerned.....

With the resources available, best use is being made for the purpose of undertaking risk analysis and mid-office functions. However, of course, should the Treasury be provided with qualified staff it would be in a much better position in this regard."

Inadequate Formal Authorisation Procedures for the Publication of MGS Annual Issuance Calendar and for New Government Stock Issues

Ministry of Finance

BOD feels that it should not be involved in the MGS Annual Issuance Calendar since this is being treated by Treasury, together with Financial Administration within MF. Any public debt servicing cost variances arising during the year "are catered for through the exchange of 'ad hoc' correspondence between the Treasury and the Budgetary Operations Division."

Treasury Department

- The Accountant General pointed out that draft calendar approvals from the Director General, Financial Administration/ Permanent Secretary, MF, are electronically stored. He further noted that:

"The involvement of Budgetary Operations Division in the approval of the calendar is questionable given that it would have already factored in the debt servicing when deriving the PSBR.

The recommendation on the selection of the optimal strategy for government borrowing falls within the remit of the Treasury in consultation with other bodies with the necessary expertise in the field."

- "Although in this particular instance the Permanent Secretary's decision may "prima facie" appear to have prevailed over

the Parliamentary Secretary's, one should note that the relative Legal Notices were in fact, subsequently passed through the normal channels and hence approved by the Parliamentary Secretary's office.

.....approvals given and/or changes suggested by the Hon. Parliamentary Secretary are invariably carried out by written procedure (usually by e-mail)."

However, no internal documentation indicating the final decision, reasons thereof and final endorsement of the Parliamentary Secretary and Minister of Finance, was provided to NAO. It was not indicated whether action will be taken to ensure that all decisions and related justifications are documented and easily accessible for quick future reference.

Lack of Communication between MF and Treasury Department

Ministry of Finance

"It is not the case that there is 'lack of information from the Ministry and subjectivity which surrounds the availability of foreign loan finance'.Action will be taken in order that, where applicable and as pointed out by the NAO, communications made between the parties concerned will be formalised through the necessary additional documentation."

Inadequate Storage of Communication Documentation by Treasury

Treasury Department

This recommendation has been taken on board and all communication documentation will start being filed in its respective Treasury file.

Inadequate Means of Disaster Recovery at Treasury

Treasury Department

"All Treasury PCs may now be backed up on the server".

Control Issues

Evidence supporting Debt Related Decisions and Communication not provided by MF

Ministry of Finance

“Action will be taken in order that, where applicable and as pointed out by the NAO, the documents.....will be retained in the relevant files.”

Treasury Department

The Accountant General confirmed that revised estimates regarding public debt are officially submitted to BOD, twice a year. Occasionally, BOD queries Treasury's plans in respect of short term borrowing. *“.....revised estimates as a whole are continually discussed between Treasury and MF within the context of other reporting requirements such as the Fiscal Debt and Deficit Notification (April/September) and The Convergence Programme which are submitted to the EU Commissions, as well as other occasions where reporting is requested.”*

Lack of Evidence showing that Treasury makes reference to Previous Years' Variances in Public Debt Planning

Treasury Department

“Variances are indeed analysed as they take place. In this regard the Treasury would enquire with the MF regarding perceived shortfalls in revenue, and also with the privatisation Unit with regards to proceeds from privatisation. Apart from the above, the Treasury monitors PSBR on an ongoing basis.”

Continuous Public Debt Budgeting Approach

Ministry of Finance

BOD stated that a continuous budgetary process is carried out and that financial performance is regularly assessed through monthly meetings on the revised estimates held within MF for the purpose of attaining

the predetermined deficit targets by the end of the year. Meetings with revenue earning Departments and Ministries/entities are held as necessary.

Inadequate Treasury Bill Authorisation and Communication Documentation at Treasury

Treasury Department

- The Accountant General pointed out that the Public Account is monitored daily to take immediate action in case of liquidity shortfalls. He further added:

“Although it is acknowledged that it would be ideal to have decisions documented, in practical terms this would stifle operations. Decisions need to be taken on the spot, of course, after having taken consideration of all known parameters.

- *With regards to the short-term borrowing process, the Treasury issues Treasury Bills on a weekly basis.Given the substantial amounts involved and also the fact that stakeholders would require urgent replies as to whether they were successful or not, the Treasury normally informs participants of the outcome of the auction within 45 minutes following the closing time. By the closing time the Treasury would have drawn up the weekly Swing Operation Report identifying the amount needed for that particular week. However, in terms of assessment of the bids offered, rates, alternative action in case of lack of participation and other scenarios, all these decisions would need to be taken within 45 minutes and hence it would be very difficult to document the scenarios and decision taken within that restricted time bracket.*

Having said this, the Treasury had, in 2002, taken measures to introduce a mechanical way on how the weekly borrowing could be ascertained, with the introduction of the Weekly Swing Operation. This could, of course, be further improved should modern electronic methods be introduced to aid management in this area. On the other

hand certain parameters such as market sentiment, probable bid prices and scenarios still remain issues which no one other than management would have to gauge, assess and take action upon.

- Although it is correct to state that in most instances the Accountant General gives verbal consent for the issue of the calendar, one must point out that this is supported by data produced by the Public Debt Section of the department as well as discussions which take place prior to the issuance of the calendar.

The Accountant General takes note of the recommendation of the Auditor General to endorse the final version of the calendar and file same in the relative Treasury file.”

Treasury Bill Tender Forms received by Treasury not stamped

Treasury Department

This recommendation was agreed to and taken on board by Treasury.

Market Intervention through Sinking Fund Investments

Treasury Department

“The case mentioned by the Auditor General was a one-off. The sinking fund had indeed underwritten the stock at the cut-off rate. Therefore it did not influence the market in any way. During the past three years, this was the only instance when the sinking fund invested in Treasury Stocks.”

Compliance Issue

Non-Enforcement of Cash Flow Projection Circulars 10/2001 and 6/2003 by Treasury

Treasury Department

“The Treasury does resort to such measures but only in cases of repeated default. The Department has very limited sanctions through which it can enforce

compliance and hence it seeks to take action where it is mostly warranted and likely to be most effective.”

No comments were received from Ministry of Finance regarding:

- market intervention through Sinking Fund investments;
- insufficient reasons provided in the ‘Variances in Revenue for Financial Year’ Statement in Part I of the Annual Financial Report;
- the non-functionality of the PDMAC; and
- failure to set up the DMO.

No comments were given because “.....in the opinion of this Division, these recommendations do not remain applicable following the explanations given”.

No comments were received from Treasury Department regarding the:

- necessity of having a written debt management strategic plan and procedure guidelines and timeframes within which these would be formulated;
- lack of communication between MF and Treasury Department;
- failure to set up the DMO;
- Sinking Funds not accounted for separately;
- incomplete Sinking Fund transaction records at Treasury; and
- recommendation to consider prior years’ variances when preparing new public debt forecasts.

Appendix

During the audit, reference was made to several documents comprising the following:

- IT System Report on Treasury Public Debt Management prepared by MITTS, 2004.

- Report prepared by Crown Agents and the Commonwealth Secretariat about the 'Setting up of a Public Debt Management Office and Implementation of CS-DRMS 2000+', 2003.
- Report commissioned by the MF Permanent Secretary and prepared by the MEU regarding 'Treasury Department Operations Review', 2004.
- Report prepared by the now Accountant General regarding his visit to the UK DMO and HM Treasury, 2001.
- UK DMO Annual Review Report.
- Public Debt Presentations prepared by the Treasury.
- The Local Public Debt Legislative Framework.
- Treasury files dealing with Public Debt Management.
- Presentation to the International Consortium on Government Financial Management prepared by Jean-Jacques Dethier, The World Bank about the 'Institutional Arrangements for Public Debt Management – Recent Trends in OECD and EU Accession Countries', June 2002.
- Questionnaire prepared by Storkey & Co Management Consultants on 'Public Debt Management Assessment Tool', 2003.

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INTOSAI Public Debt Committee Reports

- Guidance for Planning and Conducting an Audit of Internal Controls of Public Debt – Final Report, May 2000.
- Guidance on the Reporting of Public Debt – Final Report, May 2000.
- Guidance on Definition and Disclosure of Public Debt, 1995.
- Survey on Public Debt, 1992.
- Interim Report on Public Debt Survey, December 1993.
- International Monetary Fund Definition, December 1993.
- Public Debt Performance Auditing – A Summary of Practices as of August 1993.
- Guidelines on Best Practice for the Audit of Public/Private Finance and Concessions, October 2001.

Ministry for Rural Affairs and the Environment

European Agricultural and Guarantee Fund – Paying Agency

Background

The Paying Agency (PA) is responsible for the management, on behalf of the European Union, of assistance derived from the Common Agricultural Policy and/or any market intervention as well as on the structuring of the agricultural sector that is financed by the European Agricultural Guidance and Guarantee Fund (EAGGF). It is also responsible for effecting payments to beneficiaries in relation to this Fund.

The Agency is situated within the Office of the Permanent Secretary, Ministry of Rural Affairs and the Environment (MRAE).

Key Issues

No Financing Plan

The PA has no cash flow management programmes in place. Payments to beneficiaries were made subject to availability of funds and EU Commission deadlines.

Recording of Funds

The Paying Agency Management System (PAMS) is a stand-alone electronic package. Information on cash outflows and inflows is not integrated with the current Government's accounting system (DAS).

Furthermore, funds received from the EU Commission are not being accounted for in any accounting system. Neither the Treasury, nor the MRAE are being notified by the PA when such funds are received. Expenditure is not being reconciled with respective amounts actually refunded.

Deadlines for Expenditure

Instances were encountered where deadlines for expenditure were not being respected.

Staff Turnover and no PA Manager

The position of PA Manager has remained vacant since the middle of 2005 and resigning/retiring officers are not being replaced, with tasks being shifted to other employees.

Dependency on MITTS

PA was still dependant on the MITTS Project Team for the electronic processing of payments of subsidies and other system-related transactions.

Control Issues

Opportunities for improvement were identified in the following areas:

Checks and Internal Controls

- Lack of segregation of duties in the payments process.
- No verification is carried out to ensure that effective controls are in place by the Integrated Administration and Control System Department (IACS), to which it has delegated its authorisation function.
- Discrepancies in checklists and inconsistent information presented to the PA by IACS are not being queried and acted upon. Furthermore, no checks are being carried out to ensure compliance with financial forecasts.

- Parameters set for data sampling verification do not cover whole population, increasing the risk of ineligible transactions being intentionally excluded. Moreover, the level of confidence is unsatisfactory due to a small sample size taken. Verification is not being made against an independent source.
- A list of payments rejected by the bank, due to incorrect bank account number, etc., and records of when actual payment was eventually made were not being kept. Discrepancies were noted when tested.
- The system and data were possibly put at high risk, with administration rights to the PAMS being given to a relatively junior employee.
- Passwords to the PAMS have no expiry date.

Communication

- Informal and unstructured communication between the PA and IACS.
- No involvement by the Accountant General (Treasury Department), neither in the receipt of funds, nor in the payment process to the beneficiaries.

Banking Transactions and Bank-Related Issues

- Bank charges were not charged to the proper account.
- Bank statements were not available for most of the accounts held by one of the commercial banks as at 31 December 2004, and no proper bank reconciliation statements were being drawn up.
- Control by the bank has been by-passed as in the absence of proper authorisation, batch payments should have been rejected but were actually processed.
- A letter authorising the bank to issue payment to beneficiaries was submitted twice with different value dates increasing the risk of double payments.

Documentation

- One of the Memoranda of Understanding was not endorsed by the parties.
- The list of the authorised signatories and any discretionary limits as regards bank matters was not made available, and neither were Circulars issued by the Ministry to provide guidelines to the PA.
- The transfer of over Lm160,000 from the Central Bank of Malta (CBM) account to the PA's account held by one of the commercial banks was authorised without a formal request for such transfer being made. Funds transferred remained unutilised for seven (7) weeks.
- Manual of Procedures not updated.
- The signing of documents very often appears to be considered as a formality rather than assuming responsibility by the officer endorsing them.
- The letter of engagement does not stipulate minimum monthly hours and what is covered by the monthly fee paid to the internal auditors.
- Quarterly internal auditors' reports are not being drawn up as agreed, with the result that any deficiencies in the internal control systems are not being identified or acted upon.
- The return submitted to the Treasury overstated a balance of Lm434,430 as at 31 December 2004.
- Original bank documents are not kept in a safe and secure storage.
- No user manual is available for the PAMS. Moreover, no guidance and regular training were given by the system provider.

Compliance Issues

Updating of EU Regulations

No designated person at the PA is responsible for keeping abreast with EU regulations.

No Reports or Certificates drawn up by IACS

The Agency is not being kept regularly informed on the results of activities carried out by the IACS Department to confirm that the latter are fulfilling their responsibilities.

Recommendations

No Financing Plan

A financing plan for a financial year should be drawn, including refunds received from the Commission, and reviewed monthly for any possible variations.

Recording of Funds

The PAMS is to be improved and integrated with corporate data (DAS). It should also incorporate features which allow for the recording of funds received, so as to enable the PA to keep better track of funds spent and reimbursed. Furthermore, reconciliations of all cash transactions are to be carried out.

Reporting to the EU Commission

Reporting deadlines should be strictly adhered to.

Staff Turnover and no PA Manager

Human Resources function should assess the cause of high staff turnover and take remedial action. In addition, the position of PA Manager should be filled without delay, with the new appointee assuming exclusive management responsibilities of the Agency on a full time basis.

Dependency on MITTS

The PA is to take full ownership of the PAMS, especially at operational level.

Segregation of Duties

The function of the payment process should be segregated from the actual payments. A clear separation is to be made between these two tasks.

Delegated Authorisation Function

To ensure that adequate controls are in place by IACS, the PA should carry out a walk-through test on a sample of applications received by IACS.

Controls by-passed by the PA

PA officers should be fully aware of all the required checks. Any discrepancies noted are to be queried and, unless solved, the batch payment should not be processed.

Data Sampling and Verification Check

Testing is to be performed on the system so as to ascertain its proper functioning and that access is restricted to authorised personnel. A threshold percentage of verification should be pre-established to give an acceptable level of accuracy. Furthermore, in order for this check to be valid, the sample data is to be checked against the original applications.

Rejected Payments

The PA is to keep track of all the rejected payments from the point of rejection up to when the beneficiary is ultimately paid. All the relevant details for each reject are to be duly documented and a reconciliation prepared after each batch payment.

System Security

Employees having administrator rights are to be limited possibly only to section heads.

Changing Passwords

Passwords are to be changed regularly to enhance the system's security.

Communication between the PA and IACS

More formal meetings are to be held between the PA and IACS, to enable the PA to keep up-to-date with IACS' affairs and give the latter the opportunity to put forward any problems or observations.

Lack of Involvement by Treasury

More co-ordination with the Treasury is recommended. The Treasury is also to be copied with all the necessary information to keep abreast with cash flow movements of EU funds.

Bank Charges

The bank is to be immediately directed to deduct any charges from the correct account.

Bank Reconciliations

Regular monthly statements of all bank accounts are to be obtained. A reconciliation statement is to be prepared for all the bank accounts, as required by the General Financial Regulations.

Letters authorising Bank to issue Payments

The terms set out with the bank regarding letters giving authorisation should be clear. It is in the PA's interest that such controls are not by-passed by the bank, who should be advised accordingly.

Authorisation Letter submitted Twice

Any amended authorisation letter is to state that it supersedes the previous one sent, including the reasons for the re-issue and the value date clearly indicated.

Unofficial Documentation

All agreements and reports of concern to the PA are to be duly signed and dated.

No Retention of Important Documentation

Documents relevant to the PA's operations are to be appropriately filed and made available when requested.

Transfer not substantiated

The setting up of a financing plan is being recommended in order to avoid unnecessary transfers.

Manual of Procedures

The Manual of Procedures is to be amended and thereafter kept updated to be in line with the current organisational structure of the PA.

Signing of Documents

It needs to be emphasised that an officer is assuming responsibility when endorsing documents.

Shortcomings in the Letter of Engagement

The letter of engagement is to be reviewed, with reference being made to the expected number of hours together with the work to be performed, and the terms made more favourable to the PA.

Another alternative which ensures continuous internal audit service is to deploy a full time internal auditor within the PA, with a monthly work schedule/plan being prepared.

No Quarterly Reports by Internal Auditors

Reports are to be drawn up by the internal auditors as established in the letter of engagement.

Incomplete and Unreliable Return

Details are to be submitted in an accurate and responsible manner so as to enable Treasury to process the information correctly.

Security of Bank Documents

Important documentation is to be stored in the PA's safe deposit, with access being given only to the Manager or head of section.

No User Manuals or Proper Guidance from MITTS

A user manual is to be requested from MITTS. Furthermore, the PA is to ensure that the terms of the agreement entered into with the service provider are honoured and that proper training is given to employees.

Updating of EU Regulations

There should be an employee specifically delegated with the tasks of keeping up-to-date with any new regulations issued by the EU and to ensure their inclusion in the Manual of Procedures.

No Reports or Certificates drawn up by IACS

IACS is to be requested to report to the PA on the activities it carries out, describing also the means employed, as required by the pertinent guidelines. Both parties are to agree on the frequency, timing and structure of such reports.

Management Comments

Management has generally agreed to the recommendations and corrective action is being taken.

However, reservation was made on recommendations stating that although the position of the PA Manager is currently vacant, such responsibility has been temporarily assigned to the Director Corporate Services. Various attempts have

been made with the competent authorities to strengthen the PA's administration.

According to management, unless two signatures are present in the authorisation forwarded to the bank, the batch payment will be rejected. However, a number of authorisation letters reviewed by the examiners held only one signature, and payment was still processed by the bank, therefore the reply submitted was not satisfactory to the NAO.

In their response, management did not properly address the issues presented by this Office as regards:

- Bank transfer of over Lm160,000 not substantiated and funds remaining unutilized for a number of weeks. Management replied that since this was the Delegated Service's first experience, the delay in issuing payments was acceptable.
- No quarterly reports are being drawn up by the internal auditors (though these were agreed upon in the letter of engagement).
- System security with respect to attribution of administrator rights to employees, stating that this is up to the MRAE to set.

European Agricultural and Guarantee Fund – Integrated Administration and Control System

Background

The Integrated Administration and Control System (IACS) Department within the Ministry for Rural Affairs and the Environment (MRAE) is the body responsible for the management of all data of applicants and their holdings incorporated in the IACS system in relation to the assistance by the EU, from its initiation up to the stage when claims for payment are passed to the Paying Agency (PA) for payment, as directed by Council Regulation.

Key Issues

High Level of Dependency on One Officer

An IACS officer (in a relatively minor grade) is responsible for a vast array of tasks. Apart from placing segregation of duties at risk, this high dependence on one officer impinges upon the smooth running of the Department.

Total Reliance on the IACS System

IACS is placing heavy reliance on the inbuilt mechanisms of the system. Furthermore, hard copies of generated reports, checks performed and other important information could not be evidenced. IACS experienced difficulty in extracting the required reports from the system.

Staff Allocation

There is a short-fall of employees in grades engaged in certain processes, when compared to the list of staff identified in the Department's organizational chart. On the other hand, employees in low grades are not being utilised efficiently.

Control Issues

Opportunities for improvement were identified in the following areas:

Location Spot Checks and Inspectors' Training

- Location spot checks for aid in respect of fields under specific cultivation are being carried out long after the crops are harvested. Moreover, inspectors did not always check for the crop residues while conducting location spot checks.
- In the majority of cases, no measurements were being taken by the inspectors in cases of discrepancies from applications, only approximations were noted.
- Good Agricultural and Environmental Conditions (GAECs) checklists were not being filled on location.
- In five (5) out of eleven (11) parcels of land reviewed, discrepancies were not noted down on the control reports by the inspector, even though these were evident from the orthophotos.
- Sufficient information was not given to inspectors by the Department to carry out location spot checks.
- An inconsistent number of inspectors carried out verification on land for the 2004 campaign. This varied from one to four.
- Quality control checks subsequent to verifications on location did not cover a sample of the work carried out by each inspector.

Application Forms

- Fourteen percent (14%) of the declaration forms reviewed were not signed by the applicant or his legal representative, five percent (5%) were not signed by an IACS officer while thirty-eight percent (38%) carried no date.
- Original applications were not being maintained by IACS for the 2004 campaign in the case of Gozo submissions. When declaration forms are revised (final), these are not always endorsed by the applicants.
- When applying for subsidies, farmers provide no evidence that they are actually working the land.

Anomalies and Convocations

- A hard copy of the letters notifying farmers to attend a meeting at IACS, in order to sort out irregularities arising from their application, is not being filed. Moreover, no letters were sent to farmers whose irregularity could not be resolved in time. As a result, farmers were not informed of any withholding or reduction in payment.
- During the 2004 campaign, applicants were called too close to payment deadlines in order to clear anomalies. This created unnecessary pressure resulting in inaccuracies.

Shortcomings in the IACS System

- On various occasions aggregate total area of parcels was overstated. This could have possibly led to overpayments being made to beneficiaries.
- Lack of audit trail in the IACS system with respect to parcels incurring penalties.
- Inadequate control over the large number of users putting the system's security at higher risk.
- Farmers are not informing IACS of any modifications in the parcel size.

Documentation

- No responsibility is being assumed by officers endorsing the respective

documentations for which they are not directly accountable.

Rubble Walls Scheme

- Restoration work on rubble walls that should have commenced in 2004 was not evident in twenty-three percent (23%) of the plans reviewed.

Compliance Issues

Manual of Procedures

According to the Manual of Procedures, the late submission of an application incurs a penalty in the form of four percent (4%) reduction in subsidy per working day, as against the one percent (1%) established by EU Regulations.

No Reports or Certificates drawn up by IACS

Although required by the Memorandum of Understanding between the PA and IACS, the Agency is not being kept informed on the results of activities carried out by the IACS Department on a regular and timely basis in order to confirm that the latter are fulfilling their responsibilities.

Recommendations

High Level of Dependency on One Officer

The IACS function could be delegated to a number of employees, each responsible for part of the process. Furthermore, the tasks of all IACS officials are to be supervised by a senior member of staff so as to enhance internal controls and avoid complete dependency on one officer.

Total Reliance on the IACS System

Continuous testing needs to be carried out on the system to ensure that deficiencies are identified and dealt with in due time.

Staff Allocation

If redeployment of employees to short-staffed areas is possible, recruitment of additional personnel is to be considered.

Timing of Location Spot Checks

Location spot checks are to be carried out closer to harvest time. When this is not possible, crop residues from different parts of the parcel are to be physically checked for evidence of the last crops sown on the land.

Measuring of Land

Land qualifying for subsidy is to be accurately measured by inspectors during physical location inspections, as required by EU regulations. Any exclusions from the area eligible for payment are to be clearly marked on the orthophotos.

Compilation of the Good Agricultural and Environmental Conditions

Inspectors are to be made more aware of the importance of the information required in the GAEC forms, which are to be filled in accurately on location and attached to each control report.

Discrepancies on Control Reports

The number of quality control checks is to be increased to obtain further confidence that inspectors are diligently carrying out verifications on land and duly recording findings in the control reports.

Information forwarded to Inspectors and Identification

Mapping sheets forwarded to the inspectors are to clearly indicate the parcels within the same area selected for location spot checks.

Number of Inspectors carrying out Location Spot Checks

Each team for location spot checks is to consist of at least two inspectors in order to obtain more reliable results.

Quality Control Checks

When selecting the sample for the quality control check, consideration should be given both to the location of the parcels and to the officers carrying out the inspections, whilst

increasing the percentage to ensure that a sample of verification performed by each inspector is covered.

Declaration Forms

IACS officers are to ensure that each declaration form is duly signed both by the applicant and a Department official. All declarations are to be automatically dated by the system.

Filing of Applications

Filing of the original application forms, endorsed by the applicants, should be centralized.

Farmers applying for Subsidies

IACS is to ensure that payments are made to the correct beneficiaries by performing location spot checks close to harvest time. Moreover, the Department is to make a summarized Maltese version of the relevant regulations available to all applicants and stress their importance.

Anomaly Letters

Each anomaly letter sent to the beneficiaries is to be printed and filed in the respective personal folder. Where anomalies cannot be resolved, farmers are to be informed of any withholding or reduction in payment.

Convocations

For the 2005 campaign, farmers are to be called at an earlier stage, allowing ample time for queries on the irregularities encountered to be resolved before the first aid payment is made.

Overstated Total Area of Parcels

Testing is to be carried out on the system to rectify such discrepancies. The subsidies are to be calculated on the exact measurement of the parcel.

Lack of Audit Trail

An amendment to the system is recommended to enable tracking of parcels on which penalties were incurred and the applicable tolerance limit.

Users Creating and Registering Applications

The number of users creating applications is to be reduced after giving careful consideration to the expected number of applications in each location. Access to the system should only be given to authorised personnel.

Changes in Parcels

Farmers are to be instructed to notify the Department of any relevant changes in their holdings, in order to update records accordingly.

Signing of Documents

The officer is assuming the required responsibility when endorsing documents.

Rubble Walls Scheme

Monitoring of the work performed on rubble walls by farmers should be carried out by the Department to ensure that restoration work had actually started in 2004.

Manual of Procedures

The Manual of Procedures is to be updated on a regular basis.

Reports or Certificates drawn up by IACS

IACS is to report to the PA on the activities it carries out, describing also the means employed, as required by the pertinent guidelines. Both parties are to agree on the frequency, timing and structure of such reports.

Management Comments

Reservations made by the Department on recommendations were not found acceptable. Management pleaded that:

- No further delegation of tasks is possible due to limited number of officers at managerial grades.
- The Department is using a remote sensing technique whereby measurement is done on screen.
- There is no need for the final declaration to be endorsed by the farmer.
- In cases of doubtful applications as to whether the beneficiary is the person actually working the land, unscheduled location spot checks are carried out.
- IACS will be keeping the PA updated by means of a yearly report.

The following observations were also rebutted:

- Location spot checks being carried out long after crops are harvested.
- Application dates not evidenced on the actual forms.
- Inadequate control over the large number of IACS system users.
- Farmers not informing IACS of any changes in their parcels or holdings.
- Restoration of rubble walls not evidenced in the plans reviewed.

The reply submitted by management was not satisfactory as regards:

- Shortcomings noted in the control reports.
- The overstated aggregate total parcel areas.
- No responsibility assumed by officers when endorsing documents.

A number of recommendations have been accepted, most of which have already been adopted.

Ministry of Health, the Elderly and Community Care

Bio Medical Engineering Stores

Karen Grech Hospital

Background

The Bio Medical Engineering Store is responsible for the receipt and issuing of various parts relating to medical equipment located within Karen Grech Hospital, St Luke's Hospital, St Vincent de Paule's Residence and various Health Centres. There are approximately 5,200 items at the stores.

Key Issues

Stock Control System

Details such as the unit cost and supplier details of various items are either incorrectly recorded or have not been inputted in the stock control system. Requisition numbers relating to items issued from the stores are also not being recorded.

The creation of stock codes and accounts in the stock control system for dental equipment has not yet been implemented in the system. As a consequence receipts and issues relating to this equipment are not being recorded in the system.

Discrepancies between Physical Quantities and Stock Control System

Excesses or shortages of items were encountered when comparing the stock balances with the stock control system against quantities physically in stock.

Control Issues

Opportunities for improvement were identified in the following areas:

- In the absence of the store officer,

workshop technical officers have access to the stores accompanied by a security guard. Related documentation is only prepared when the store officer returns on duty.

- Receipts and issues effected in the stock control system were not posted at the end of the current week but were left pending for weeks on various occasions.
- Manual requisition forms in loose sheets and not pre-numbered are used. Stock codes are only quoted occasionally on requisition forms.

Compliance Issues

Physical Stock Take

No physical stock take is being carried out at the stores and consequently no stocktaking list was forwarded to NAO for both years 2004 and 2005.

Recommendations

Key Issues

Stock Control System

The unit cost of each item is to be recorded in the stock control system, whilst supplier details and requisition numbers should also be inputted. It is also essential that proper records of all receipts and issues of dental equipment are maintained.

Discrepancies between Physical Quantities and Stock Control System

Proper control should be exercised on the receipt and issue of store items, such that

any discrepancies identified through random checks are acted upon immediately as required by the General Financial Regulations.

Control Issues

- Relevant documentation should be effected upon delivery of items from stores, in order that the physical balance at the stores agrees with the balance on the system after all issues.
- Transactions are to be posted once or twice a week in the stock control system so that it is always up-to-date with reliable information, portraying the actual balances in stock.
- Requisition forms are to be pre-numbered consecutively in duplicate form. Stock codes should always be quoted during the filling in of the requisition form to facilitate processing.

Compliance Issues

Physical Stock Take

Regular stock taking exercises should be carried out as stipulated by the General Financial Regulations so that items are counted at least once every year. Any discrepancies noted should be identified and resolved immediately. A report on each stock taking exercise is to be drawn up.

Management Comments

Management concurred with some of the observations made. However comments received were deemed inadequate since management did not commit itself to implement any of the recommendations presented and failed to state what other alternative action will be taken to rectify the limitations mentioned by the audit.

Furthermore, unsatisfactory comments were received in relation to the following issues:

- Recording of supplier details and requisition numbers;
- Access to the stores when stores personnel are not present;
- Current format requisition forms.

Management also commented on problems encountered with the computer hardware and the stock control system. Since this software is no longer supported by its agent, the store has ceased utilising this software and shifted to a manual system. Management is proposing that alternative software should be used and that a network is set up between the computer at the store and the technical officer's computers with read only access to stock concerning their section.

The Elderly and Community Care Expenditure

Background

The audit covered expenditure incurred during 2004 in the following six (6) Cost Centres within the ministry's portfolio:

- Permanent Secretary's Office
- Director General's Office
- Institutional Health Care Sir Paul Boffa Hospital
- Public Health
- Institute of Health Care
- Nursing Services

Key Issues

Transport

- The vehicle database is not comprehensive and excludes important information for control purposes. Vehicles on long term hire and ex impressed vehicles are not included and no distinction is made between fully expensed and general use vehicles.
- Considerable hiring costs were incurred in respect of three (3) fully expensed vehicles in use by secretariat officers, and two (2) vehicles in use by the Public Health Department.
- No call for tenders was issued for the hiring of the three (3) fully expensed vehicles used by secretariat officers.
- Log books were not being used by a number of departmental vehicles whilst various details were incomplete in the

vehicle's log book. Furthermore, journey details recorded indicate that some vehicles were not being left on departmental premises after office hours.

- Various fuel requisition and issue notes are not properly and completely filled in. The maximum allowable fuel consumption ceiling was exceeded by three (3) officers during a sample month.
- Three (3) government owned vehicles do not display the name of the Department.

Director Pharmaceutical Services

The post of Director Pharmaceutical Services is occupied by two officers. One of these officers was seconded with the University of Malta whilst retaining the same benefits, including a fully expensed car, and the other was temporarily appointed in this post as a replacement. The Health Division failed to request reimbursement of the salary, including any benefits paid as a result of this secondment to the University of Malta.

Control Issues

Opportunities for improvement were identified in the following areas:

- VAT receipts which are not received upon payment are rarely attached to the original payment vouchers, making it difficult to ascertain whether the supplier gave a proper receipt. The VAT department is not being notified of suppliers who fail to produce a fiscal receipt.
- Goods/Services Purchase Orders were drawn up after the purchase had been

effected in twenty seven percent (27%) of the purchase orders.

- Payment vouchers were not posted to the proper account in twenty eight percent (28%) of payments. Furthermore, purchases of two (2) fully expensed vehicles and a PA system were disbursed from inappropriate Cost Centres.
- A ten percent (10%) bank guarantee pertaining to a contract worth Lm5,500 was not renewed for the second year of the contract, removing the possibility of redress in the case of failure by the contractor to fulfill any of his obligations.
- Documents relating to two payments of Lm9,840 and Lm1,202 respectively were not traced.
- Inventory items bought during the year were not marked with an asset identification number whilst various shortcomings were encountered in the Ministry's inventory database with respect to these items.
- Three (3) computers purchased by the Institute of Health Care could not be physically traced as the location on the database was incorrect.

Compliance Issues

Hospitality Expenses

Hospitality expenditure incurred was not approved by the Permanent Secretary.

Recommendations

Key Issues

Transport

- A comprehensive vehicle database is to be prepared by the Transport Section to aid monitoring of vehicles in use.
- Transport requirements are to be reviewed and alternative methods of obtaining vehicles needed for long term should be considered with a target to maximize cost

effectiveness. In particular, the possibility of acquiring vehicles through a 'finance lease' (where the lessee assumes ownership of the asset by the end of the lease term) or the option of purchasing vehicles (upon approval of the Ministry of Finance) are to be explored.

- Procurement regulations are to be adhered to and a call for tenders issued if total estimated expenditure exceeds Lm2,500.
- Procedures specified in the Public Service Management Code should be adhered to. All vehicles, other than fully expensed cars, should have a log book, duly and legibly filled in and endorsed. It should also be ensured that government owned vehicles are left on departmental premises after office hours.
- Fuel Requisition and Issue notes are also to be properly filled in as required by the Public Service Management Code, whilst fuel consumption limits set out in MF 5/98 are to be adhered to.
- The department's name should be displayed on all government owned vehicles, with the exception of fully expensed cars, in accordance with MEAF 2/97.

Director Pharmaceutical Services

The Health Division should seek to recover the value of the benefits being paid to the seconded officer from the University of Malta.

Control Issues

- VAT receipts are to be attached to the original payment vouchers on all occasions. The procurement of any good or service from suppliers failing to produce a fiscal receipt should be discontinued until the matter has been rectified. The VAT department is also to be notified of defaulting vendors in accordance with Treasury Circular 9/99.
- Procurements should always be covered with a Goods/Services Purchase Order to ensure that funds are available and

authorisation has been sought prior to placing an order.

- Expenditure must be appropriately allocated in the correct account and cost centre, as stipulated in MF circular 3/2000.
- A bank guarantee should be renewed prior to its expiry to remain valid for the whole contract duration.
- The missing documents are to be traced and accounted for. The proper filing of documents is to be given more importance in the future.
- Inventory items are to be marked with an identification number. Information on the inventory database should be accurate and complete as guided by MF circular 14/99 whilst including any additional details that may be relevant in enhancing control. The database is to be kept updated at all times with any additions and/or movements.

Compliance Issues

Hospitality Expenses

Disbursement of public funds in connection with Government hospitality is to be authorised by the Permanent Secretary in accordance with the Public Service Management Code.

Management Comments

Management concurred with some of the observations made and has committed itself to implement the recommendations presented and/or any other additional or alternative measures to rectify limitations mentioned. Moreover it was also pointed out that:

- Even though it is a better option to purchase vehicles rather than hire them, management stated that specific funds were not provided by the Ministry of Finance.
- Vehicles pertaining to the Public Health Department are not being left on departmental premises as the area is not considered safe since private vehicles have already sustained damages. Moreover, vehicles are occasionally required by the Health Inspectorate Services after office hours.
- Documents relating to the two payments could not be traced.

Furthermore, unsatisfactory comments were also received in relation to other issues raised in our report:

- Departmental vehicles not using vehicle log books.
- Location of three computers purchased by the Institute of Health Care.

Ministry for Resources and Infrastructure

Ta' Robba Quarry

Background

Ta' Robba Quarry (Ta' Robba or Quarry), located on a site officially known as Il-Bur ta' Dingli at the limits of Kirkop, had its operation reactivated in the 1970s when an estimated eighty five per cent of its soft (*franka*) stone resource had been already exhausted by hand tools over the years.

On the site plan, the Quarry is divided into approximately four equal blocks. Quarrying of the fourth block has already started. Permit by the Malta Environment and Planning Authority (MEPA) for full development of the Quarry has been served on Director General (DG) Works, within the Ministry for Resources and Infrastructure (Ministry, MRI), early in the current year.

The Quarry falls under the direct responsibility of the Construction and Maintenance Department (CMD). This is headed by a Director reporting to DG Works.

A principal technical officer in charge of the Support Services Unit reports on Quarry matters (hereinafter Quarry OIC) to the CMD Director.

Key Issues

Below-the-Line Account

- The warrant for the opening of a below-the-line account (BLA) for the Quarry issued by the Ministry of Finance was not made available. This account is at the core of controls that could be exercised over Quarry's operation. As a result it was not possible to assess the extent to which disbursements were compliant with the

official terms and conditions under which the BLA should be operable.

- Unrelated expenses brought to charge in 2005 to Quarry BLA included the cost of 11 pick-up vans, mostly for the Cleansing Services Department's use, amounting to Lm58,569.
- Not all expenses directly related to Ta' Robba could be traced to Quarry BLA or Departmental Accounting System (DAS) accounts linked thereto. Two examples are electricity bills and the cost of a newly acquired pick-up in addition to the abovementioned 11 vans. Finance approval was granted in respect of intended call for tenders for only 7 vehicles against the rationale behind the Quarry BLA, considering the unusual nature of the disbursements from the BLA. Moreover the Contracts Department did not press for prior Finance approval for the additional 4 vehicles.
- It could not be determined whether Quarry's electricity bills had actually been paid and in what year.

Stock Records

- No records are kept of any of the resource material being used up at the Quarry, or sold or issued therefrom. This is regarded to be in violation of standing regulations governing the maintenance of stock records.
- The records that are being kept for Ta' Robba sales are both inadequate and inaccurate. Entries in DAS income accounts linked to Quarry BLA could not thus be completely verified.

- Since 2003 Request Forms for stone cut from Ta' Robba directly issued to sites ceased being copied to Mriehel Stores, where MRI's main record system of stocks of operating materials and supplies is installed.
- The practice of internal charging for services has also been nonexistent between intra-departmental subdivisions of the Ministry, Ta' Robba being one such subdivision.

Control Issues

Opportunities for improvement were also identified in the following areas:

- DAS records for Quarry transactions are classified under a cost centre unrelated to Ta' Robba, namely under the Manufacturing and Services Department.
- Finance as well as the Treasury are unaware as to under which cost centre(s) in Financial Estimates, and to what extent, should Quarry's operations be financed when these could not possibly be sufficiently funded from revenue from the sale of stone.
- Account keeper allocating Quarry's expenses had often exercised arbitrary judgement as to which account was to be debited, including whether the expense should be brought to charge to Quarry BLA in the first place.
- Expenses of the same type had been allocated in different accounts.
- Besides the operating expenses not brought to charge in Quarry BLA highlighted under Key Issues, the major part of disbursements allocated in Recurrent Vote accounts were estimated to exceed Lm80,000 in labour and vehicle running expenses.
- Certain costly extra-ministerial services are being availed of for free by the MRI. As an example it can be said that a team of nine officers paid by the Ministry for Gozo processes payroll amendments for MRI. Quarry is not charged its share of this cost. Full accountability on the part of MRI with regard to its running costs, and those of any of its subdivisions (including Ta' Robba), is not possible.
- After unearthing a long-buried water reading meter, a dispute over amount billed by Water Services Corporation (WSC) for period 8 July to 31 October 2005 amounting to Lm3,229 led to suspension of the service.
- Stone supplies, even to other government institutions, had eluded Quarry's billing system.
- A 'business case' could not be established to justify running of own quarry or government's need for self-sufficiency in the supply of soft stone.
- Running Period Contracts (RPCs) are being awarded for stone supplies and for services ancillary to the Quarry's operation, such as fair facing and delivery of orders to customers. On the other hand, sales of stone from government-owned Ta' Robba Quarry to non-government institutions imply that stone to government is not in short supply.
- The quantity of resource available up to exhaustion of Quarry is not known to management, though the indications are that it could last for another 25 to 85 years.

Compliance Issues

Inventory

- Omissions had been noted in Quarry's inventory records.
- Copies of suppliers' invoices, in support of Quarry inventory items on record, are not held by inventory officer.

Stone pricing

- The Building Industry Consultative Council (BICC) did not meet the request of the NAO to be furnished with a retail price list of soft stone used in construction, claimed to be available at their end.

- Diverse stone products were charged out to customers at one unit price, irrespective of variation in thickness, etc.
- Individually distinct prices for stone block units sold from Ta' Robba, arbitrarily fixed by Quarry OIC, are not evidenced, neither on the records that are being kept, nor on bills issued to Quarry customers.

Quarry Sales to Outside Customer

- Contrary to the applicable standard operating procedure, not all Quarry sales to an outside customer had the prior approval of DG Works. Sales that had never been backed up by such authority were not even recorded in the daily register in such a way that these could be added.
- It could not be established what transportation expense government could have incurred by way of returns from the foregoing unauthorised sales. Such expense could well have comprised the cost of crane hire considering the extraordinary size of the stone block units sold (4x3x2).

VAT Accounts

- Not all output VAT element collected from an outside customer was credited to an Output VAT Account.
- Notwithstanding its direct relationship to Quarry sales (taxable goods) none of the input VAT element for the contracted transportation of orders from Ta' Robba had been debited to a VAT Account in 2005.
- DAS accounts under MRI's Recurrent Vote in use for output and input VAT are not in line with MFC 4/95, 'Accounting of VAT by Departments'.
- Clerks issuing manual fiscal receipts related to VAT-rated sales at the Revenue Section of the Finance and Administration Department (FAD) allocate the output VAT element in DAS accounts only against minuted instructions accompanying each individual receipt. The same could be said

of allocations in DAS accounts of input VAT element by FAD account keepers in charge of payments to suppliers.

Quarry Staff Attendance

- No attendance records, individually signed by staff engaged at the Quarry, are being kept.
- No formal routine daily tasks or daily production quotas (minima) expected of each Quarry worker engaged on a 'task and finish' basis could be evidenced, not even in the log books kept for work performed. On the morning the NAO visited site, only two of 11 quarry floor workers could be witnessed.
- Source authorising abovementioned flexibility scheme could not be determined. Payments to employees at overtime rates are also being made under the scheme.

Waste Cleanup

- 'Stop and enforcement' orders by MEPA regarding waste-deposit **works** 'in and around' Quarry remained unexecuted. Prevention of unauthorised waste disposal, and removal within 24 hours of any such dumping by MRI as Quarry operator, is a condition of the aforementioned MEPA permit to full development.
- Cleanup of rubble adjacent to the first entrance gate had to start immediately on issuance of the second of two such enforcement orders.

Restoration Plan

- As another condition of the permit for full development, MEPA were expecting Quarry restoration plan, not necessarily restricted to exhausted parts, by 7 May 2006.
- MEPA Minerals Board's report, in a preamble to the conditions made to Works on granting this permit, regards Quarry Blocks 'A' and 'B' as exhausted. During their site visit, however, it was noted that stone was still being cut from Block B.

Impressed Vehicle

- Lead replacement petrol (LRP) to the impressed car at the service of the Quarry is not being reimbursed on the basis of recorded milometer readings. This goes against the relative provisions in the Public Service Management Code (PSMC) regarding reimbursement of fuel expenses for this category of vehicle.
- In June 2005 this vehicle was issued diesel in excess of the maximum (unauthorised) allowance of 205 litres of LRP for the month.

Recommendations

Below-the-Line Account

- Ministry of Finance should seriously consider closing BLA in question, replacing it with separate revenue and expenditure accounts under the pertinent revenue budget lines and Expenditure Votes as necessary. In the interim, in order to ensure compliancy with conditions under which this account had been initially opened, regular mutual monitoring by MRI and Finance is recommended.
- Suppliers' invoices for goods and services procured for Ta' Robba should be cross-referred to payment voucher when paid.
- MRI should seek to regularise procurement of vehicles in question.

Stock Records

- Bin cards (and store ledger sheets) for the various sizes of stone block units cut from Quarry should be kept as per Treasury Circular 6/2004, 'Stock Control Procedures'. Recorded store movements are to be supported by Goods Received Note of cut blocks transferred to store on quarry site and Store Issue Form for every quantity leaving Ta' Robba in delivery to customers. Main store records at Mriehel cannot be bypassed when implementing these recommendations.

- A write-off procedure is required for quarry waste and rejects (defective stone block units cut) being discarded as waste. Insofar as it is possible, this should be in line with General Financial Regulation (GFR) 108.
- Reconciliations are recommended at the end of a reporting period between records of quantities sold, quantities billed and subsequent revenue from customers.
- Once records of cut stone in hand (in store on quarry site) are available, official declaration of their validation in accordance with section 106 of GFR is recommended. A hundred per cent physical check at least once a year is mandatory. Complete stocktaking at the year end is advisable and declaration thereof is to be submitted to the NAO in the first month of the following year.

Cost/Budget Centre

- Quarry's DAS records should be maintained under the cost/budget centre of the directorships responsible for Ta' Robba's operation.
- Officer(s) accountable for the cost/budget centre comprising Ta' Robba could be more accountable for the Quarry's operation if a subdivision in DAS records is created specifically for the purpose, i.e. treating Ta' Robba as a distinct responsibility centre with a separate budget drawn up.

Allocation in DAS Accounts

- Allocation in main ledger accounts should be the responsibility of the officer(s) responsible of the Quarry's budget, who ought to guide the account keeper in this regard.
- Official information backing the standard chart of accounts should be complemented by premeditated allocations covering all types of revenue and expenditure in the Quarry's budget. Reference to such budget allocations should be made when raising Request Forms for the procurement of goods or services for the Quarry.

Reported Net Expenditure and Internal Charging

- FAD within MRI could correct misallocations of expenditure, and any known error in Quarry BLA, where still in time to do so.
- Interdepartmental charging for services rendered to MRI by other line Ministries could only become government policy with the initiative/intervention of Finance.
- Though in coordination with Finance, the internal transfer of funds and adjustments between cost centres (charging intra-departmental services) is completely within the control of MRI, and could be independently introduced any time.
- If no water supply had been extended specifically to feed Ta' Robba, a request for the removal of Quarry's name from the pertinent account in the records of WSC is recommended. In this way consumption by other departments when the service is reinstated would not be charged to Quarry.

Billing

- Drivers engaged in the delivery of Quarry sales should be held personally liable for amounts Quarry is unable to charge out and collect as a result of their failing to retrieve evidence of satisfactory delivery to customers.
- One billing system has been recommended for both intra-departmental Quarry sales and sales to outside customers.

Business Case for Own Quarry

- Sale of stone to third parties is to cease, unless deemed as justifiable.
- Quarry's resource capacity to exhaustion is to be determined to a degree of reasonable accuracy. This would enable one to assess fairly the commercial viability of the present autonomous set-up and the various other business forms that Ta' Robba's undertaking could take. The officer(s) responsible for the Quarry could

be asked to present 'business case(s)' to this effect.

Inventory

- Quarry inventory is to be updated regularly to reflect complete and accurate records in compliance with standing inventory regulations. Quarry's administrative staff are to undertake more frequent verification of inventory listings with physical checks.
- As soon as they become available at the Ministry, loose copies of documentation (such as suppliers' invoices signed in evidence of satisfactory delivery) could be distributed to inventory officers to update their records and retain.
- Quarry's inventory records should be adequately supported with cross-reference to source documents maintained in sequentially filed, readily available copies of suppliers' invoices or other pertinent documents.
- All relevant items owned by third-parties are to be noted in official inventory records in accordance with PSMC regulations, and identified by an ad hoc sub-class.

Stone Pricing

- No discriminatory internal transfer prices are to be applied to any government entity procuring stone from Ta' Robba unless otherwise justified/authorised.
- Individually distinct stone prices should be charged, reflecting every variation in size, quality and mode of delivery to customers.
- If it is decided that sales to outside customers are not to be discontinued, only current prices as established in the local building stone market should be charged rather than internal transfer prices.
- Quarry OIC is to be guided by an official regularly updated comprehensive price list. Until the Malta Resources Authority come up with guidelines and/or the BICC make their prices known to the NAO, reference could be made to prices charged out to government under current RPCs for the supply and delivery of *franka* stone.

Quarry Sales to Outside Customer

- If requests for Quarry sales to non-government entities could not be declined, as they would relate to government's business, orders should still be conceded strictly in compliance with established procedure, i.e., after DG Works approval is granted and against payment prior to delivery.
- Explanations from Quarry OIC are to be sought for deviation from established procedures concerning sales to outside customers and sales of this type for which DG's approval was never obtained. Explanations are also to be sought for any transportation costs incurred by government that were not covered by the payment customer was asked to make.

VAT Accounts

- Strict compliance with MFC 4/95 is recommended insofar as VAT accounting is concerned.
- DAS users at the Revenue Section could be officially informed to allocate amount excluding VAT to appropriate income account and, at the same time, VAT element to output VAT account. This is to be done as soon as a manual fiscal receipt is issued.
- Any improperly reported VAT should be corrected in the subsequent VAT return(s).
- Independent reconciliation is to be performed of records of quantities sold kept at the Quarry, quantities billed at the Revenue Section, and subsequent receipts from customers recorded in DAS accounts.

Quarry Staff Attendance

- Full attendance records are to be maintained at the Quarry in accordance with PSMC regulations.
- Any flexibility scheme applied to workers at Ta' Robba is to be regularised with the direct involvement of the Management and Personnel Office, OPM.

- A minimum of daily tasks required of each worker participating in a 'task and finish' scheme is to be drawn up and monitored to ensure a fair return for a day's pay.

Waste Cleanup

- MRI, as a government entity, should be at the forefront in executing MEPA enforcement orders.
- To step up security at Ta' Robba, in order to prevent unauthorized dumping at the Quarry site, MRI need exercise better control over duty watchmen employed outside office/operating hours.

Restoration Plan

- MRI should consider discontinuing quarrying activities in Block B.
- Timely action on a restoration plan covering the entire Quarry is recommended, especially if cleanup of rubble outside the first gate is envisaged as part of the plan. This would mitigate the risk of prejudicing the bank guarantee issued by Works in favour of MEPA in this regard. The risk of suspension of the operating/full-development permit would also be reduced.

Impressed Vehicle

- Fuel issues to impressed cars should be strictly on the basis of milometer readings logged during official business in line with standing regulations.
- Management are to determine the correctness of fuel issues made to the impressed driver in 2005, who may need to remedy his position with regard to any unauthorised fuel allowances he might have benefited from.

Management Comments

MRI stated that:

- 'Operation of the below the line account for Ta' Robba Quarry is being reviewed';
- A second tender was issued for the purchase of two pick-up vans further to the

- 11 questioned vans, but did not substantiate this;
 - It is not practicable to account for Quarry rejects and natural wastage;
 - As regards internal charging, no charge is even made for Quarry supplies to Departments within the Ministry simply because the expense could not be met;
 - WSC were paid the full amount disputed up to time of audit. Quarry will now be fed water from a supply from District 4 Offices nearby (but no mention was made as to how consumption cost would be reflected in BLA);
 - Sales to outside customer were all approved by DG Works, but did not substantiate such approval in respect of sales partly returned, allegedly at customer's own cost;
 - Clean-up works in the area adjacent to the entry gate is currently in progress, as well as the cleaning of 'minor dumping' over quarry surplus material.
 - Any procurement of stone from Quarry by interdepartmental customers would be preceded by approval of Director responsible of Ta' Robba on a standard Request Form;
 - Sales from Ta' Robba to outside customers will be discontinued with immediate effect;
 - Disciplinary steps would be taken against those failing to retrieve evidence of satisfactory delivery of sales from Ta' Robba on the basis of which customers are billed;
 - Measures are being taken to update Quarry inventory.
- Certain initiatives, not mentioned in our report but that MRI would be taking to enhance internal controls at the Quarry, include two additional employees to assist in the technical operation as well as administrative work.
- However, other points directly concerning MRI were not fully addressed in their response.

On NAO's recommendations:

- As from 2006 Quarry's DAS records would be maintained under an ad hoc cost centre;

Ministry for Justice and Home Affairs

Courts of Justice - Wages and Salaries

Background

The Law Courts' mission is to provide case management support to the Judiciary for the benefit of the general public. The administration of the Courts of Justice is the responsibility of the Director General while the legal responsibility for the implementation of judicial orders rests with the Registrar of Courts.

During financial year 2005 the actual amount spent on Personal Emoluments including that of the judiciary was Lm2,733,252 (Approved Estimates – Lm2,863,000), covering three hundred and ninety five (395) employees on the payroll for 2005.

Key Issues

Budget

The budgeted amount to cover salaries of the members serving on the Board of Local Tribunals was exceeded by nearly twice as much since the actual expenditure for 2005 amounted to Lm86,925. Additional funds made up of virements totalling to Lm42,000 as well as a supplementary warrant of Lm20,000 were allocated to cover the deficit. Moreover, the amount of Lm2,000 provided to cover salaries of Board Members for Reletting Urban Property (Regulations) Ordinance did not cover the actual expense of Lm15,939. An additional amount of Lm14,000 was provided by means of a supplementary warrant.

Transcription Fees

- The task of transcriptions of court hearings both for Civil and Criminal cases should be performed after office hours at an extra remuneration. However, it was noted that some officers were carrying out this job during office hours while still receiving this allowance. The total amount of Lm30,706 was paid for this service in 2005.
- Though claims for payment of transcriptions are being certified correct, no list of sittings that need to be transcribed is available to verify status of each tape in order to ensure that payment is claimed only once.
- The source of authority supporting the rate payable to transcribers was not presented for verification.

Hours worked by Mediator

A mediator working for the Family Courts, who in terms of the contract of service should perform 10 hours a week, only reported for work on 16 days during 2005. However, a payment of Lm154.15 every 4 weeks is being made by the courts.

Control Issues

Opportunities for improvement were identified in the following areas:

Attendance Sheets and Leave Record Cards

- There was no record of the hours worked by three (3) officers examined in the audit sample, as they are not signing the

Attendance Sheets. As a result, accuracy and validity of remuneration paid could not be verified.

- The majority of employees who were marked as reporting late for work still signed in as if they arrived on time.
- No official authorisation was evident for officers working within the Courts of Justice and temporarily leaving the office during normal working hours. Moreover, no temporary absence sheets were kept.
- Medical certificates could not always be traced to cover the days marked as sick leave on the attendance sheets.
- Vacation Leave and the Sick Leave Record Cards were either not updated or were recorded with the incorrect number of days taken.
- No checking of source documents was performed before payment to verify that the amounts claimed as 'vetturi' fees¹ were correct.
- No written approval was traced or presented in support of the two Court marshals to share in the allowances paid to their colleagues in respect of serving court notifications.
- Reports reflecting the 'mandati' fees¹ due to the Court marshals were either not presented to the Accounts Section or were incomplete. This resulted in understated payment of allowance to the foregoing officers.

Overtime and Time Off in Lieu (TOIL)

- No supporting documentation was found in respect of overtime payment claimed by one officer out of the ten (10) employees chosen in the audit sample who worked overtime.
- There is no liaison between the Salaries and the Human Resources Sections to verify that employees are not requesting both payment and TOIL for the same hours worked as overtime.
- Lack of control over time off taken in lieu of overtime performed was noted. Furthermore, compensation for overtime has also been granted by time off in lieu to an officer within the audit sample working on a reduced time table.

Lack of Staff

The total hours worked by the Human Resources section were inadequate to meet the needs of the three hundred and ninety five (395) government employees and twenty six (26) Ex-Dockyard employees working at the Courts of Justice.

Allowances

- Funds budgeted for "Allowances" in the Financial Estimates for the year 2005

under Salaries and Wages of the Courts of Justice were exceeded by Lm7,572 representing 2.8% of the budgeted figure.

Payment of Honorarium

- The honorarium to Commissioners of Justice in respect of Local Tribunals giving service to the Local Councils Department were paid and borne by the Law Courts as no budget allocation by the Department has ever been made for these services.
- The Administration Section of the Law Courts were not in a position to confirm the accuracy of this expenditure claimed by the Department which amounted to Lm86,925 for the year 2005.

Errors by the Treasury Salaries Section

- Details of employees inputted in Treasury database were not being verified. A case in point is the adjustment in salary from Scale 16 to 15 that was due to an officer, within the audit sample, which was only given three years later.
- Double checking of manual calculations has not been performed by the Treasury Department when calculating the arrears due to the foregoing officer as the said adjustment was understated.

¹ Fees paid to marshals/ushers for the delivery of notifications to parties requested to appear before the Courts.

Compliance Issues

Selection Process for Officers Acting as Transcribers

Authority to select transcribers at the Courts is by law vested in the Registrar. However, it is the custom for employees willing to carry out this task to approach the Deputy Registrars who then pass on any tapes for transcription.

Return of Allowances

The two annual returns, providing updated information on allowances paid to entitled personnel at the Law Courts, are not being prepared and sent to the Ministry of Finance as stipulated by the Public Service Management Code (PSMC). Neither is a certificate being issued by the Administration Section to certify that the conditions pertaining to the allowances received by each officer still apply.

Recommendations

Key Issues

Budget

Estimates of funds to cover the salaries for Board Members can be calculated on an average number of sittings each member can possibly attend during a calendar year.

Transcription Fees

- A special section could be set up at the Courts of Justice made up of a pool of full time transcribers approved by the Registrar. Information could thereby be better controlled to eliminate the risk of employees claiming payment for transcriptions carried out during office hours.
- Status of all tapes for transcription is to be recorded on a computerized database for better monitoring of their progress.
- Any disbursement of public funds should without fail be supported by official rulings from the right level of authority.

Hours worked by Mediator

The number of weekly hours performed by each mediator are to be certified by a responsible officer and information passed to the Accounts Section. A refund is to be requested for any amounts overpaid.

Control Issues

Attendance Sheets and Leave Record Cards

- The Legal Officer, the Part-Time Judicial Assistant and the Consultant should start keeping attendance records. The number of weekly hours performed by these officers is to be certified by a responsible officer.
- Attendance Sheets are to be supervised on a daily basis to ensure correctness and duly signed by the officer in charge.
- A medical certificate should be produced within the period stipulated in the Public Service Management Code (PSMC). Days of absence on sick leave are not to be paid for unless supported by a valid medical certificate timely submitted to the Human Resources section.
- Regular reconciliations between attendance sheets and vacation leave as well as sick leave records are to be carried out by the officer in charge of Human Resources. Furthermore, the list prepared by the Human Resources Section should be accurate and reliable.
- Any absences from work are to be authorised and documented in the temporary absence sheets as stipulated in the PSMC.

Overtime and Time Off in Lieu

- Overtime hours are to be evidenced as having been performed and certified correct before payment for overtime is approved.
- A single application is to be formulated in respect of compensation for overtime work

showing the preference of payment or time off opted for by the officer concerned.

- Officers working on a reduced timetable are not to be compensated for overtime as stipulated in the Management Code.

Lack of Staff

Management is to consider increasing the number of employees in the Human Resources Section by the re-deployment of staff. The introduction of additional members of staff will help to reduce any backlog that may exist.

Allowances

- Budgeted expenditure is to be sufficiently monitored and controlled by those responsible of the respective cost centres.
- The officers in charge of the manual registers recording allowances to be paid to the court marshals are to be given access to the LECAM² electronic system to eliminate the manual register. This would avoid duplication of work and reduce any manual errors in summation.
- Any agreement regarding fees for serving court notifications reached between the Court marshals and Ushers involved is to be made in writing.
- The officer in charge is to ensure that complete records are submitted for the entire month. It is also suggested that any understated 'mandati' fees be confirmed and paid to the Court marshals concerned.

Payment of Honorarium

An agreement is to be reached with the Ministry of Finance so that the allowance for such honorarium is included in the pertinent budget line of the Local Councils Department.

² Legal Case Management System - an integrated computerized system that covers the functionality and provides the latest technology tools for the efficient functioning and control of the Civil and Criminal Courts. (LECAM 2000 User Console)

Errors by the Treasury Salaries Section

Calculations are to be checked by an independent officer in a senior grade at the Treasury and duly endorsed for evidence.

Compliance Issues

Selection Process for Officers Acting as Transcribers

The Registrar is to establish guidelines as to the qualifications transcribers should possess and only officers meeting these requirements are to be offered the job. In addition, these employees are to be advised as to what is expected of them as well as to how their work is to be presented.

Return of Allowances

Allowances which are authorized are to be reviewed periodically. At the beginning of each calendar year DCS is to obtain a certificate from the relevant directors in respect of each officer receiving an allowance, confirming that the conditions pertaining to the allowances still apply. This certificate is to be forwarded to the Director, Finance and Administration and also submitted to the Ministry of Finance. Any changes in entitlement of allowances are to be immediately identified and reflected in the officer's salary.

Management Comments

Management has accepted and adopted a few of NAO's recommendations. However, the following issues were not adequately addressed in their response:

- The selection process of transcribers and claims for payment of transcription work;
- The low number of hours worked by a Mediator;
- Keeping of attendance and leave records;
- Honorarium paid to Commissioners of Justice.

Management failed to comment on NAO's observation regarding Incomplete Records and understated 'Mandati' fees.

Non-Central Government Organisations/Public Entities

Malta Stock Exchange

Background

Established by virtue of ACT XXXIII of 1990, the Malta Stock Exchange (MSE) provides facilities for the purchase and sale of quoted securities, a place for the trading, facilities for the maintenance of a central securities depository and performs all tasks required for its proper functioning.

Control Issues

Fixed Assets' Inventory

The MSE did not maintain an inventory of property, plant and equipment while the inventory of electronic equipment lacked essential details and links to the physical assets.

Business Continuity Plan

The Business Continuity Plan (BCP) was not finalised. The MSE Council was awaiting information on the costs involved for the implementation of the recommendations put forward by the BCP Committee report.

Trading System

The maintenance agreement of the current trading system was due for renewal by end March 2006. The Exchange was not in a position to negotiate a new Trading system to be introduced by April 2006. Eventually the MSE was compelled to either renew the maintenance agreement incurring the attached cost, over which management highlighted concern, or continue using the current trading system without supplier's support exposing itself to the attached risks.

Travel Abroad

Officers travelling abroad were not submitting the 'Overseas Travel Return Form' and the relevant receipts backing the contingency moneys utilised as required by the MSE procedures manual. Reimbursements to or by the MSE were also not effected.

Petty Cash

No standard petty cash float was being maintained by the MSE, thereby reducing control over petty cash expenditure and in conflict with the provisions of its procedures manual.

Leased Motor Vehicles

Lease agreements were not formalised with respect to five motor vehicles in use by the MSE for which an average annual cost of circa Lm 16,000 was being incurred. In view of the lack of formalised agreements proper accounting classification of the motor vehicle leases could not be ascertained. Furthermore, the MSE was not in a position to ensure, and enforce if necessary, that the actual service provided was in accordance with the terms and conditions agreed upon.

Recommendations

Control Issues

Fixed Assets' Inventory

It is recommended that:

- an inventory of all property, plant and equipment be compiled and maintained;

- the inventory of electronic equipment be updated to include details ensuring adequate control; and
- periodic physical inventory checks be performed and checks' results logged in compliance with the MSE's procedures manual.

Business Continuity Plan

The BCP be finalised and adequately tested on a regular basis.

Trading System

The MSE should carefully evaluate all options available giving due consideration to the continuity of operations and the timing of new business needs from the trading system.

Travel Abroad

The MSE procedures manual should be strictly adhered to.

Petty Cash

An imprest system in line with the MSE procedures manual should be introduced.

Leased Motor Vehicles

It is recommended that all lease agreements entered into by the MSE be formalised.

Management Comments

Management has already adopted most of the recommendations and remarked that:

- Both inventories were being updated and physical checks were to be performed shortly.
- Developments opened new strategic and technological avenues for the MSE in relation to the Trading System. The market technology arm of the current software was bought by another company and new discussions are currently underway with this company. Meanwhile the current maintenance agreement would be renewed.
- Petty cash was being maintained on an imprest system.
- The situation with respect to the leased motor vehicles' agreements was rectified.

Mediterranean Conference Centre

Background

The Mediterranean Conference Centre is a government entity falling under the Ministry for Tourism and Culture. The Centre consists of various halls that are regularly rented out for conferences, exhibitions, fairs, seminars and other similar events.

Key Issues

Tangible Fixed Assets

Tangible fixed assets were written off to the profit and loss account in the year of purchase as opposed to normal accounting practice requiring write off over the expected useful life of the asset. This accounting practice is not in line with International Financial Reporting Standards.

Tangible Fixed Assets' Inventory

The following observations concerning the safeguarding of the assets of the Centre were noted:

- Values of listed inventory items were generally unavailable.
- The inventory did not include all the Centre's tangible fixed assets.
- Physical inventory checks were not performed.

Control Issues

Water and Electricity

Operators, providing catering services through the use of the Centre's facilities, disputed amounts charged for the consumption of water and electricity since

meters in place did not enable direct quantification of usage.

Debtors Provision

An evaluation of aged debtors, performed at time of audit, revealed doubtful debts amounting to circa Lm 12,000, which were not provided for in the financial statements.

Compliance Issues

Procurement

Procurement regulations were generally adhered to except for one particular case in respect of printing services amounting to Lm 10,500. Only one quote was obtained instead of a departmental call for tenders, as required by the then applicable Public Service (Procurement) Regulations 1996.

Recommendations

Key Issues

Tangible Fixed Assets

The Centre is to carry out an exercise so as to identify its tangible fixed assets. Fixed assets already recorded in the Centre's accounting system should be disclosed in the financial statements immediately.

Tangible Fixed Assets' Inventory

The tangible fixed assets' inventory is to be updated with all the Centre's tangible fixed assets and a value is to be allocated to all items of inventory. Valuation could be spread over a period so as not to disrupt the Centre's operations. Periodic physical

inventory checks should be performed and evidenced.

Control Issues

Water and Electricity

A meter enabling direct quantification of the water and electricity consumption is to be installed in order to invoice operators on a timely basis, enable complete disclosure of income and ensure money due to the Centre is recouped.

Debtors Provision

The provision for bad debts should be revised and any balances not yet settled should be fully provided for.

Compliance Issues

Procurement

The Centre is to strictly comply with the applicable procurement framework.

Management Comments

Management has already adopted most of the recommendations and remarked that:

- The cost of items purchased during 1995 and onwards, net of their cumulative depreciation will be restated from reserves and disclosed in the financial statements as from the year ended 31 December 2005.
- Appropriate meters have been installed and all water and electricity bills have been recharged to operators.
- Debtor balances highlighted have been followed up and the provision for bad debts will be adjusted where applicable.
- The supplier selected for the procurement of the printing services possessed the sole right to utilise photographs from previous assignments depicting the Centre.

Conservatorio Vincenzo Bugeja Programmes

Background

The Fejda and Jeanne Antide Programmes, established in 1997, aim to provide services and education to girls with behavioural problems while the Dar Is-Sliem Programme, established in 2003, is a residential facility for the accommodation of refugee unaccompanied minors who are under 'Care Order'.

Control Issues

Opportunities for improvement were identified in the following areas:

Books of Accounts

The accounting of the Programmes was maintained on a computerised spreadsheet. The financial statements were not prepared in accordance with International Financial Reporting Standards (IFRSs) and a modified cash based system was adopted, adversely affecting the true and fair view of the accounts.

Accounting Procedures and Practices

Mispostings were observed resulting in misclassifications and overstatement of proceeds from the sale of fixed assets and other expenses. Expenses refunded by the Conservatorio Vincenzo Bugeja Fund, actually representing donations, were not disclosed in the accounts.

Fixed Assets' Inventory

No Fixed assets' inventories were kept by the Programmes.

Contracts of Employment

Contracts of employment were not drawn up for all employees of the Programmes.

Back Ups

The Programmes lacked adequate and formalised back up procedures. Only payroll information was backed up and no offsite copies were kept.

Compliance Issues

Fiscal Documentation

Instances were observed whereby documentation supporting expenditure incurred by the Programmes was not available or respective invoice was not fiscal.

Recommendations

Control Issues

Books of Accounts

The financial statements and accounting system should shift from the current modified cash based system to an accrual accounting system in line with International Financial Reporting Standards. An accounting package should also be introduced.

Accounting Procedures and Practices

Detailed monitoring and review of the accounts of the Programmes is to be performed in order to avoid, detect and correct misclassifications, omissions and erroneous entries.

Fixed Assets' Inventory

Fixed assets' inventories are to be compiled and maintained by the Programmes in line with MF Circular No. 14 / 1999. Periodic physical inventory checks should be performed and relevant results logged.

Contracts of Employment

The Board should make the issuance of contracts of employment to existing employees a priority and ensure that future employment relationships be formalised.

Back Ups

Adequate back up procedures are to be formalised and adhered to.

Compliance Issues

Fiscal Documentation

Proper documentation is to be obtained so as to support the Programmes' expenditure and ensure adherence to tax laws.

Management Comments

Management concurred with all observations and has already taken corrective action on the issues relating to the contracts of employment, fixed assets' inventory, back ups and the procedures over the accounting function. In connection with the introduction of an accounting package management remarked that it was not recommended from a cost effective point of view.

Malta Standards Authority

Background

The Malta Standards Authority (MSA) is an autonomous institution established by virtue of the Malta Standards Authority Act of 2000. The Authority is entrusted with the co-ordination, monitoring and promotion of standardisation and related activities while ensuring the existence of supporting related services.

Key Issues

The Authority's Accounting Function and the Statutory Audit

A lack of adequate communication between the accounting staff and the external auditors performing the statutory audit of the financial statements was observed.

The Authority's workings and schedules, in respect of fixed assets, did not incorporate prior years' audit adjustments. As a result fixed assets' additions were accounted for on a calendar year basis instead of the applicable financial year basis reducing the accuracy of the Authority's quarterly management accounts.

Tangible Fixed Assets' Disposal

Fixed assets amounting to Lm 279,090 were transferred to the Malta National Laboratory. Though the disposed assets were fully covered by a European Union grant, the accumulated depreciation released was about Lm 20,000 in excess of the accumulated amortisation. The discrepancy resulted from errors originated in prior years when accounting for the depreciation of the tangible fixed assets. The over depreciation identified was credited to the profit and loss account for the year under

review in conflict with the requirements of International Accounting Standard (IAS) 8 "Accounting Policies, Changes in Accounting Estimates and Errors"

Control Issues

Opportunities for improvement were identified in the following areas:

Accounting Procedures and Practices

- Discrepancies between the debtors' and creditors' ledgers and the respective control accounts were noted. Bank reconciliation discrepancies were also observed and journal entries were not documented.
- The MSA was not in a position to provide a breakdown of debtors provided for in the financial statements.
- Items of a capital nature were expensed within IT development services.
- A shortfall within the cost of the intangible asset, which had a contracted cost of Stg 51,500, was observed after using the applicable date of payment exchange rates.
- Income from seminars, travelling and seminar costs were not fully recorded in the respective financial year.

Fixed Assets' Inventory

- The Authority's fixed assets' inventory was not up-to-date and did not incorporate asset values. The reconciliation of inventory to book totals was therefore not possible. Furthermore, evidence of physical inventory checks was not kept and full access to the inventory was granted to all accounting staff.

Information System

- Users on the internal network had unrestricted internet access and no protection / security technologies were in place between the internal network and the internet.

Compliance Issues

Procurement

The Authority's procedures manual only required quotes from different suppliers for the procurement of products and/or services costing over Lm 100.

Recommendations

Key Issues

The Authority's Accounting Function and the Statutory Audit

The Authority is to evaluate and review audit adjustments prior to inclusion in the final audited financial statements. Furthermore, all adjustments should be included within the relative books of accounts' workings and schedules so as to align and enhance the reliability of the management accounts prepared by the Authority.

Tangible Fixed Assets' Disposal

The Authority is to account for all transactions in accordance with International Financial Reporting Standards.

Control Issues

Accounting Procedures and Practices

The Authority should endeavour to avoid such discrepancies. Procedures for the raising, documentation and approval of journal entries should be set up and strictly adhered to.

The Authority should always be in a position to explain all figures and disclosures in the financial statements.

Items of a capital nature should be capitalised and depreciated over their estimated useful lives.

Intangible assets should be properly valued.

Income and expenditure should be recorded in the year to which they relate, in accordance with the accruals basis for accounting and revenue recognition criteria adopted by the Authority.

Fixed Assets' Inventory

The fixed assets' inventory should be maintained up-to-date, asset values be included within the inventory and evidence of physical inventory checks be kept. Access to the inventory should be on a "need to have" basis.

Information System

The Authority is to implement protection / security technologies between the internal network and the internet.

Compliance Issues

Procurement

It is recommended that the purchasing procedures manual be aligned to the provisions of the Public Contracts Regulations, 2005.

Management Comments

Management concurred with most of the recommendations relating to accounting procedures and practices, the fixed assets' inventory and the procurement procedures manual.

The Authority is still studying the best way how to implement the recommendations in respect of the information system.

Management also remarked that all audit adjustments were explained and discussed and that 'for some reason depreciation charged in the past years on the assets transferred was not fully compensated by amounts released from the grant'.

Appendix

Guidelines for Internal Control Standards for the Public Sector

The International Organisation for Supreme Audit Institutions (INTOSAI) is composed of 185 National Audit Offices and Courts of Audits/Accounts from around the world. Each of these institutions represents the Supreme Audit Institution (SAI) of its country. The National Audit Office (Malta) is one of these institutions.

These institutions meet in a Congress on a triennial basis and last met in October 2004 in Budapest (Hungary). The Congress, apart from discussing a number of themes of common interest, also approves a number of reports and studies that are prepared by different INTOSAI Working Groups or Committees.

One of these is the Internal Control Standards Committee, which had prepared updated Guidelines for Internal Control Standards for the Public Sector. These were based on the COSO¹ model, which is considered as one of the world's leading models on internal control standards.

These INTOSAI Guidelines are being referred to briefly here as it is felt that they should serve as a strong basis on which Government Ministries, Departments and even public entities may design or revise their internal controls. Proper internal controls are crucial in helping to ensure that public sector activities are carried out economically, efficiently and effectively with due regard to legality, accountability and transparency.

These Guidelines are considered to be of great importance by the Contact Committee – a network of SAI Presidents of EU Member State SAIs, of which the NAO is a member. A Resolution approved by all EU Member State SAI Presidents during the Contact Committee Meeting held in Stockholm in December 2005):-

“calls on its members to encourage the effective application of common professional and INTOSAI standards by administrative authorities at both national and Community [EU] level, in particular the Guidelines for Internal Control Standards for the Public Sector.” (full text of Resolution at Annex 1)

According to the Guidelines, Internal Control is defined as “an integral process that is affected by an entity's management and personnel and is designed to address risks and to provide reasonable assurance that in pursuit of the entity's mission the following objectives are being achieved:

- executing orderly, ethical, economical, efficient and effective operations;
- fulfilling accountability operations;
- complying with applicable laws and regulations;
- safeguarding resources against loss, misuse and damage.”

¹ Committee on Sponsoring Organisations of the Treadway's Commission integrated framework for Internal Control

In terms of the Guidelines and the COSO model on which they are based, Internal Controls consist of five interrelated components:

- control environment
- risk assessment
- control activities
- information and communication
- monitoring

Ministries, Departments and public entities are strongly encouraged to make use of these INTOSAI Guidelines on Internal Controls (http://www.intosai.org/Level1a/1a_IntContrSC.html) in reviewing and strengthening their internal control system.

MEETING OF THE CONTACT COMMITTEE OF THE HEADS OF THE SUPREME AUDIT INSTITUTIONS (SAIs) OF THE EUROPEAN UNION, WITH THE PARTICIPATION OF THE HEADS OF THE SAIs OF THE EU CANDIDATE COUNTRIES

Stockholm, 5-6 December 2005

Statement on the role of external audit within the framework of accountability for Community funds

Adopted at the meeting of the Contact Committee of the Heads of the Supreme Audit institutions of the European Union in Stockholm on 5-6 December 2005

The Treaty establishing the European Community (EC Treaty, art 248 (1)) stipulates that “the Court of Auditors shall provide the European Parliament and the Council with a Statement of Assurance (*déclaration d’assurance – DAS*) as to the reliability of the accounts and the legality and regularity of the underlying transactions”. For the past eleven years the European Court of Auditors (ECA) has given a negative Statement of Assurance on the majority of payment appropriations.

In April 2004, the ECA published its opinion on a Community Internal Control Framework. The European Parliament’s resolution discharging the European Commission for the 2003 budget included recommendations for implementing this framework and moving towards a positive Statement of Assurance. In June 2005, the Commission subsequently published its *Roadmap to an integrated control framework*. In November ECOFIN published its conclusions on the Roadmap. These conclusions will be considered by the European Council in December 2005.

The Contact Committee consists of the Heads of the Supreme Audit Institutions (SAIs) in the EU Member States and the ECA. It is autonomous, independent and non-political and works to enhance co-operation among its members in order to improve external audit and accountability in the EU field.

The Contact Committee welcomes the desire expressed to introduce greater rigour into the management of Community finances and to encourage more effective audit. It notes that the EU institutions intend to continue to monitor and respond, as appropriate, to future developments within their respective remits and professional competence.

Independence of external audit

The Contact Committee emphasizes the clear distinction between internal controls and external audit. The responsibility for the design and administration of the internal control framework, including internal audit, lies with management - the European Commission and the governments of the Member States. The SAIs of the Member States and the ECA, as bodies independent of management, plan and carry out their audits after giving due consideration to the internal control environment implemented by management. SAIs and the ECA may, following the completion of the audit, report on the operation of the internal controls and may make recommendations to management for improvements. The Contact Committee considers that the external audit work of its members gives an impetus for improving financial control and management systems at both national and European level.

Reporting

European funds are accounted for by national governments in a variety of ways. To a varying degree these funds become part of the national budgets. The national audit institutions audit Community funds received by Member States under their respective mandates derived from national law. The Contact Committee notes that SAIs are independent institutions which report under their respective legislative framework. The Treaty does not require a national audit institution to audit the use of European funds or European institutions to determine the nature, form or content of reports that the SAI produces and submits under its national legislation.

Co-operation

The relationship between the ECA and the national SAIs is defined by Article 248 (3) of the Treaty. It calls for other members of the Contact Committee to co-operate with the ECA *“in a spirit of trust while maintaining their independence”*. In practice this means that, the ECA may look to rely on the work of the national audit institutions. The level and extent of this co-operation in each case is at the discretion of the independent partners.

Simplification

Many of the European Community programmes of expenditure are subject to complex rules and regulations. The Contact Committee considers that the simplification of the rules and regulations could help reduce the risks inherent to transactions under shared management.

The Contact Committee will maintain and seek to increase the impact of external audit work in the drive for greater financial accountability within the EU field. To that end the Contact Committee

- calls on its members to encourage the effective application of common professional and INTOSAI standards by administrative authorities at both the national and Community level, in particular the INTOSAI Guidelines for Internal Control Standards for the Public Sector;
- will continue to enhance the bilateral and multilateral co-operation between its members, including the planning of activities, as a way to ensure that Community funds are audited in all Member States under sound methodologies in accordance with international auditing standards;
- will in this context welcome pilot projects which identify possible areas of co-operation between the ECA and SAIs involved;
- will identify scope for further improvement in the systems of management, internal control and accountability for the efficient and effective use of Community funds in the Member States, and notes the efforts by national SAIs' audits to further contribute to the improvement of those systems – and most importantly to the effective use of Community funds in the Member States; and
- will continue to enhance and encourage the existing network and co-operation between the ECA and national SAIs as an element of widening European integration.

The Contact Committee will continue to contribute towards improving the framework for and the terms and conditions applying to the audit of Community finances, and therefore will follow up this work at the Contact Committee meeting in Warsaw 2006.