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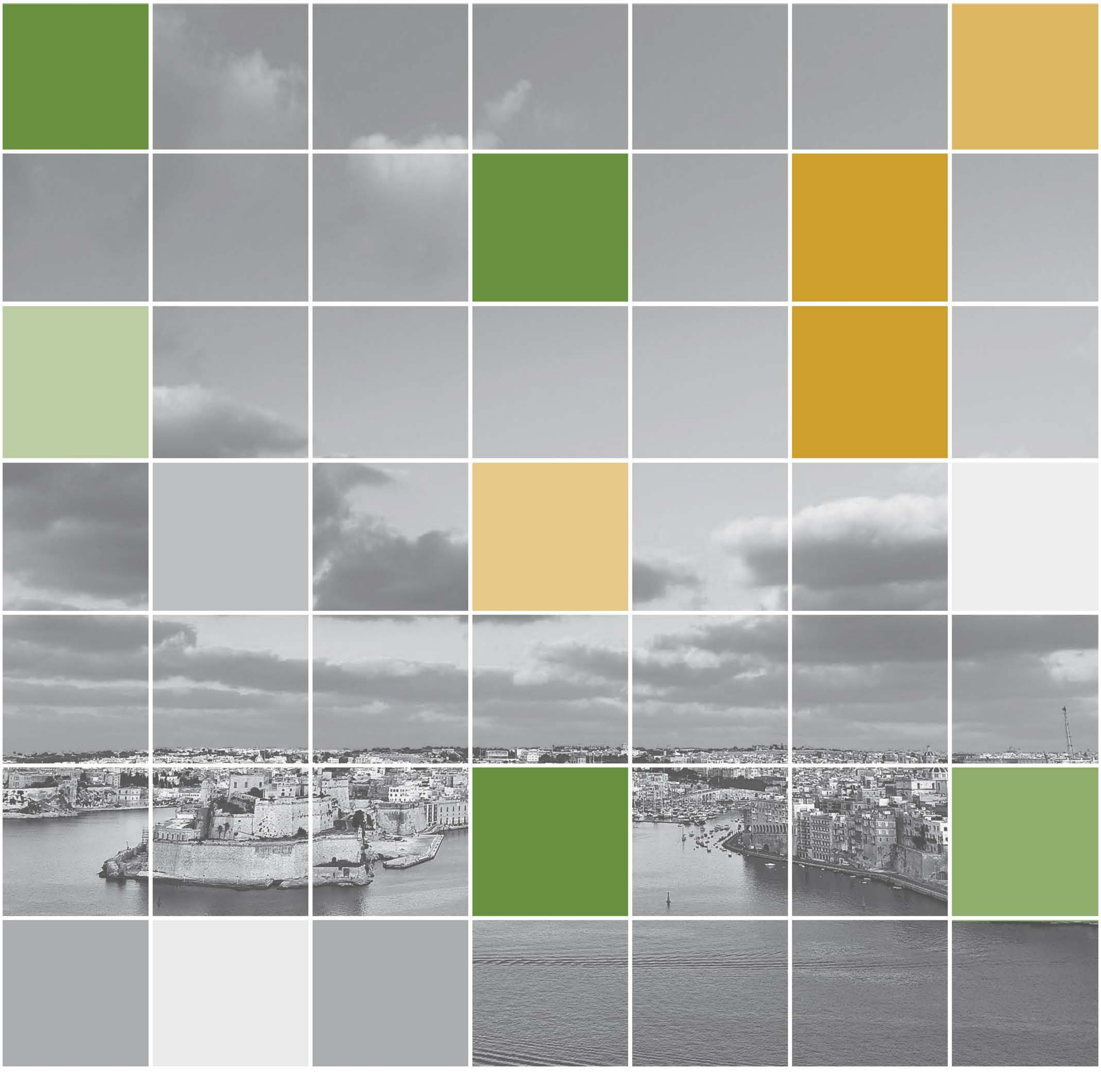
National Audit Office
MALTA

Follow-up Reports by the National Audit Office 2020

Volume I



National Audit Office

Follow-up Reports 2020

Volume I

Report by the Auditor General
June 2020

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Foreword

Like all other Supreme Audit Institutions (SAIs), the National Audit Office serves as the Maltese public sector's external auditor. As such, we are essentially mandated to provide the necessary assurance to our Parliament, and ultimately to our citizens, that public resources are being used in the best manner possible and in line with prevailing rules and regulations. Amongst other duties, this necessitates that in our Reports we invariably provide doable recommendations to duly address any shortcomings identified throughout our audit assignments. This reflects our primary objective to continue acting as catalyst for enhanced good governance across the public sector.

While performing our auditing work, we follow the International Standards of Supreme Audit Institutions (ISSAI) framework. This ensures that all our audit assignments are credible, competent and professional; only thus can we aspire to continue enjoying the trust of our citizens.

In this regard, ISSAI 12 – 'The Value and Benefits of Supreme Audit Institutions – making a difference to the lives of citizens', clearly highlights the way SAIs should carry out their auditing mandate, based on the fundamental values of transparency, integrity and accountability. This is a sine qua non condition throughout the whole audit process, from the initial identification of audit subjects up till the final phase of audit follow-up. Indeed, Principle 3 of this same ISSAI clearly states that "*SAIs should report, as appropriate, on the follow-up measures taken with respect to their recommendations*".

Hence the need of this publication which, in this first volume for this year, includes various follow-up reports undertaken by our Financial and Compliance Audit Section. The second volume will feature follow-up reports undertaken by the Performance Audit and Information Technology Audit Sections respectively.

We are pleased to note that once again the level of compliance of our recommendations is overall very positive with 84% of recommendations implemented or partly implemented. At the same time, we sincerely hope that more effort will be undertaken by our auditees to ensure an enhanced service delivery to our citizens, as they surely deserve.

Charles Deguara
Auditor General

June 2020

List of Abbreviations

AAR	Annual Audit Report
AFM	Armed Forces of Malta
AVS	Attendance Verification System
CD	Commerce Department
CfR	Commissioner for Revenue
CPSU	Central Procurement and Supplies Unit
DAS	Departmental Accounting System
FES	Foundation for Educational Services
HR	Human Resources
IRD	Inland Revenue Department
LMS	Licence Management System
MCA	Malta Communications Authority
MEDE	Ministry for Education and Employment
MFC	Malta Film Commission
MFIN	Ministry for Finance
NAO	National Audit Office
PPR	Public Procurement Regulations
PSMC	Public Service Management Code
SFCE	Secretariat for Catholic Education
SL	Sick Leave
VAT	Value Added Tax
VL	Vacation Leave

Armed Forces of Malta

Background

In its Annual Audit Report for 2015, the National Audit Office (NAO) published a write-up entitled 'Armed Forces of Malta'. The main scope of the audit was to verify that operational and maintenance expenses incurred during the financial year 2015 were duly authorised and properly accounted for, as well as to ensure that such expenditure was in line with the Public Procurement Regulations (PPR) and other relevant circulars. The objectives were also to assess the reliability and adequacy of information recorded in the Fleet Management System, compliance with the relevant sections of the Public Service Management Code regulating transport, and that inventory records were properly maintained.

Audit Scope and Methodology

The scope of the follow-up audit was to enquire on the developments following the initial audit and check the extent to which the Armed Forces of Malta (AFM) has acted upon the recommendations made by NAO. Management comments submitted in respect of the aforementioned assignment were also referred to during this follow-up.

An initial meeting with the respective officers was held and subsequently a set of questions to AFM was prepared. The respective replies were analysed and supporting evidence, together with any additional information, was requested to substantiate any assertions made by AFM.

Followed-up findings and respective recommendations as featured in the 2015 Report, are reproduced in grey text below. Developments pertaining to each issue follow.

Key Issue

Reimbursements of Medical Receipts

In 2015, as per Departmental Accounting System, at least an amount of €42,159[1] was paid to various members of the Force as refund for medical services. It was confirmed that AFM officials are given the option to procure the required medicines directly from a pharmacy of their choice and then present the receipt for reimbursement. However, the foregoing procedure has never been supported by an official documented policy.

[1] *The amount in question may not be exhaustive as similar expenses were also recorded in other accounts.*

Furthermore, notwithstanding that the said receipts were endorsed by the Principal Medical Officer, NAO encountered instances where these were not itemised and so did not specify what was actually purchased. Hence, no verification could be carried out.

Reimbursement of medical expenses are to be adequately verified and covered by an official policy approved by the respective Ministry.

Developments: *Fully Implemented*

A Medicine Refund Policy was issued by AFM on 4 May 2016, clarifying the eligibility conditions for refund of medicines and what supporting documentation is to be provided in this regard. From the three payment vouchers tested, in aggregate amounting to €2,984, it was noted that the respective receipts and invoices were itemised.

Control Issues

Lack of Verification

Audit testing revealed that adequate verification was not performed before invoices were approved for payment.

All invoices are to be invariably verified and certified as correct by the officers in charge, in order to confirm their accuracy before being processed for payment. Furthermore, to ensure that amounts claimed are correct, each payment is to be adequately substantiated with source documentation, which is to be properly filed for future reference.

Developments: *Fully Implemented*

From the 10 transactions randomly selected for testing, it was confirmed that the respective invoices were endorsed accordingly prior to effecting payment and, where applicable, casting was correct and supporting documentation, such as agreements, were available.

Water and Electricity Bills charged by Gozo Channel Co Ltd

Gozo Channel Co Ltd charges AFM for consumption of water and electricity used by AFM Gozo Command on a periodical basis, in accordance with sub-meter readings. However, no formal agreement was in place between the respective parties.

A bilateral agreement is to be in place to regulate the provision of the respective service.

Developments: *Fully Implemented*

In the Management comments following the original audit, it was stated that it was the intention of Management to initiate discussions with the company in question to formulate a formal agreement. However, during the follow-up audit, an agreement made with the Government Property Department way back in June 2012, was provided in this regard. This 15-year lease agreement of premises at Mġarr Harbour, Gozo, mentions that "*all electricity, water and other service charges shall be borne by the lessee* …", i.e. AFM.

Shortcomings in the Fleet Management System

Whilst scrutinising the Fleet Management System report, covering 217 vehicles, as well as 144 other fuel operating machines, such as generators, grass cutters and mowers, lack of details that hinder inventory control management were noted.

AFM is to ascertain completeness and accuracy in the recording of data in the system.

Developments: *Partly Implemented*

In 381 out of the 420 entries (91%), the Section name was not indicated in the respective column but broadly recorded as All Sections. In addition, in 26 instances, details were left blank. Following audit queries, it was stated that these refer to vehicles that were no longer in use and will be deleted accordingly.

Compliance Issues

Procurement without Appropriate Approval

Certain purchases falling within the audit sample, to the tune of €828,000 were not procured in line with PPR. AFM staff was unaware that when specialised goods and services are required and these can be provided only by a particular economic operator, approvals for direct orders were still to be sought from the Ministry for Finance (MFIN) or the Department of Contracts, as applicable.

AFM is to obtain the most advantageous prices within the market. Procurement by direct order is only to be made as a last resort after the necessary approvals are acquired.

Developments: *Fully Implemented*

In light of the revised PPR, communication highlighting the salient provisions of public procurement was issued by AFM in January 2017. During the year under review, it was confirmed that the goods and services in question were procured in line with standing regulations and direct order approvals were obtained, where applicable.

Other Competitive Suppliers not considered

MFEI Circular No. 9/2009 – 'Procurement of Liquid Fuels' stipulates that "the market for inland liquid fuel was liberalised in 2007", whilst marine bunkering services have been subject to liberalisation since 1995. This implies that such goods and services can be obtained from suppliers other than Enemalta Corporation, which was up to that time enjoying a monopoly of the market. However, both inland liquid fuel and marine bunkering services were still procured by AFM directly from Enemed Co Ltd. During the year under review, payments for inland liquid fuel and marine bunkering service totalled €204,930 and €778,436 respectively.

Fuel procurement is to be made in accordance with PPR, which also includes the option of adopting a framework agreement, with the possible 'call offs' on a regular basis according to AFM's requirements. If need be, further guidance may be sought from the Department of Contracts in this regard.

Developments: *Fully Implemented*

A two-year contract, with the possibility of an extension of one year, was signed in May 2018, between two economic operators, covering six lots, for supply of different types of fuel.

Bunkering Services extended perpetually

On 25 August 2011, approval was obtained from the Department of Contracts to proceed with a direct order for fuel. On the same date of approval, a supplier was selected to provide bunkering services for a maximum period of two months, in line with quotation sent on 11 August 2011. However, up to March 2015, i.e. until such fuel was required, this service was extended perpetually with the supplier in question. These extensions resulted in an aggregate payment of €2,228,738, covering the period November 2011 to March 2015.

Although the majority of extensions were duly approved, extending agreements for subsequent periods still hinders competition between other potential suppliers. Furthermore, there were extensions that were approved retrospectively, indicating that services continued to be procured without the necessary authorisation.

In order to guarantee that the best rates and conditions are obtained within a framework of a transparent and fair selection process, a fresh call for tenders or quotations is encouraged for future similar instances. Furthermore, Management must strive to ascertain that procurement is invariably backed up by adequate and timely approvals.

Developments: *Fully Implemented*

As per Management comments, no bunkering service was further required following March 2015, since a fuel farm was commissioned at the Maritime Squadron. During the follow-up audit it transpired that, for specific reasons, the two vessels stationed at Mġarr Harbour, Gozo still required this service. The abovementioned contract covered such service; however, the respective supplier was not operating in line with the tender conditions and consequently the related two lots were terminated. As a result, AFM obtained direct order approvals from MFIN to acquire the service from the only licensed bunkering fuel supplier in Gozo, until expiry of the contract in question.

Prior Approvals not obtained for Direct Orders

a. *In four instances, relating to the procurement of services and spare parts for motor vessels, amounting collectively to €84,084, both the request for direct order and the respective approval were sought and obtained retrospectively, i.e. after the commitment was entered into.*

b. *As per PPR and MFIN Circular No. 3/2013 – 'Public Procurement Regulations – Direct Orders', each request for direct order must be endorsed by the Permanent Secretary of the responsible Ministry. However, the audit revealed that prior written approval from the latter was not obtained in five sampled cases, collectively amounting to €157,656. On the other hand, in another 11 instances, totalling €347,872, procurement direct from the open market was endorsed by the Permanent Secretary subsequent to the relevant approval obtained from the Direct Orders Section within MFIN.*

Management is to refrain from entering into commitments, unless all the necessary approvals have been duly obtained. Moreover, requests for direct order authorisation are to be resorted to only in exceptional circumstances and supported by proper justification.

Developments: *Fully Implemented*

From documentation provided for five direct orders for services of a proprietary nature, it was confirmed that approvals were obtained in a timely manner.

List of Awarded Tenders and Direct Orders published late

According to standing regulations, heads of departments are obliged to publish every six months in the Government gazette a full list of departmental contracts awarded, including procurement effected through the direct orders procedure. This requirement was also stipulated in the letters of approval for direct orders.

However, the latest published list by AFM was issued on 17 January 2014. Nearly two years later and following NAO's queries, eventually on 15 December 2015 AFM issued another list, which included 37 departmental tenders and 70 direct orders awarded from January 2014 to December 2015. Another similar list was published on 15 January 2016, in order to include two direct orders which were omitted from the publication of the previous month.

Officers in charge are to be fully aware of the relevant regulations, as the necessary publications are to be made in the Government gazette in a timely manner, every six months. The respective amounts are also to be indicated.

Developments: *Partly Implemented*

The list of direct orders for the period January to June 2019, submitted to the Ministry for Home Affairs and National Security in October to publish on AFM's behalf, was incomplete. At the beginning of December 2019, a complete list was still being compiled.

No Designated Officers in charge of VAT Issues

As per pertinent circulars, one or more officers are to be designated with the responsibility to ensure compliance with the respective directives concerning the Value Added Tax (VAT) receipts. However, AFM confirmed that no particular person was responsible for such duties during 2015.

In line with the applicable circulars, specific officers are to be officially designated to ensure that the directives on VAT matters are duly followed.

Developments: *Fully Implemented*

AFM nominated a responsible officer in charge of VAT matters in January 2019.

List of Defaulters not compiled

AFM confirmed that defaulters were not being reported to VAT Department, in line with applicable circulars.

Quarterly returns with details of defaulters are to be submitted to the Audit and Assurance Section of VAT Department on a quarterly basis, as required by the pertinent circulars.

Developments: *Insignificant Progress*

AFM confirmed that the backlog was still being addressed.

Inventory Returns not submitted to the Auditor General

As per MF Circular No. 14/99 – 'Government Accrual Accounting: Revised Inventory Control Regulations', a certified hard copy of the inventory database is to be provided to the Auditor General once a year, as a minimum. However, it was established that at least since year 2004, including the year under review, such return was not submitted.

The Auditor General is also to be notified on a half-yearly basis of any additional items of inventory acquired. Notwithstanding that as per AFM's inventory database 245 items, amounting collectively to €843,410, were recorded as acquired during the first half of 2015, this Office was also not informed accordingly.

Statutory information is to be forwarded to NAO, in order to ensure compliance with the established provisions and enable control over inventory items.

Developments: *Significant Progress*

AFM duly submitted the inventory returns twice a year, from 2016 to 2018. However, the return for January to June 2019 was only submitted end October, following the introductory meeting for this follow-up audit.

Furthermore, the Auditor General was not in receipt of a mid-year list showing any additional items of inventory acquired during 2019. According to the inventory database provided during the audit, additions recorded during the year amounted to €134,675.

Shortcomings in the Inventory Database

Following an analysis of the inventory database provided by AFM as at end December 2015, a number of shortcomings were noted. Amongst others, these included fields with negative quantities, same asset identification number featuring more than once, coding not in line with the applicable circular, as well as acquisition of two particular assets wrongly recorded as purchased in November 2016.

Besides hindering the preparations for accrual accounting, such inaccurate information also impinges on the necessary monitoring over Government-owned assets and results in lack of control thereof.

The inventory database is to be updated without undue delay, in order to reflect precise and reliable data as required by MF Circular No. 14/99.

Developments: *Not Implemented*

NAO noted that the observations related to inventory management included in the 2015 Report still apply. For instance, certain items had no cost associated with them, others had a negative value while some information was still left blank.

Conclusion

NAO satisfactorily noted that the methods of procurement were enhanced, whereby procedures are now in line with standing regulations and relevant authorisations are obtained as deemed necessary. With regard to VAT issues, defaulting suppliers are to be reported timely. Being one of the pilot sites for accrual accounting, AFM is to ensure that inventory records are complete and accurate.

Church Schools

Background

The National Audit Office (NAO) published a report entitled 'Church Schools', in the Report by the Auditor General – Public Accounts 2016[1]. The audit covered expenditure on Church Schools incurred by the Ministry for Education and Employment (MEDE). This audit revealed that sound internal controls were lacking, thus their establishment together with a complete audit trail was imperative and urgent.

MEDE was assessing the possibility of using 'envelope funding' to meet Church Schools' financial requirements. However, this was not deemed feasible as statemented children would have to remain without a learning support educator until the respective school finds the necessary financing.

In 2016, disbursements from public funds over a 10-year period were found to have almost doubled, from €32 million to €63 million, whilst the student population increased by just 3% during the same period. In calendar year 2019, this amount again increased to €85.4 million, which contrasted with the fact that the student population decreased slightly from 17,120 in scholastic year 2016/2017, to 17,058 in 2018/2019.

According to the Ministry, this phenomenon can be explained by the fact that:

- class sizes were reduced in line with the latest collective agreement, which led to more teachers as from scholastic year 2018/2019;
- the introduction of new initiatives, such as Subject Proficiency Assessment and Core Curriculum Programme, as well as the adoption of specific limits effecting the individual teaching load; and
- the increase of the individual staff salaries in line with the new collective agreement.

Actual findings and recommendations proposed by this Office as they featured in the 2016 Annual Audit Report are reproduced in grey text.

Audit Scope and Methodology

The scope of this follow-up was to enquire on the developments following the abovementioned audit and to assess the extent to which MEDE has acted upon the recommendations made by NAO. Management comments submitted by the former were also referred to during this follow-up exercise.

[1] Hereafter referred to as the Annual Audit Report.

Following an initial meeting with MEDE officers, a set of questions relating to the shortcomings encountered and the respective recommendations were prepared. Management replies thereto were analysed and supporting evidence, together with any additional information, was requested to substantiate Management assertions.

Key Issues

Lack of Documentation to support the Budget Allocation

In order to determine the financial contribution made by the State, the Secretariat for Catholic Education (SFCE) was required to submit to MEDE the staff complement required by Church Schools for the following scholastic year together with an indication of the relative salaries, by the end of August annually. In this regard, the following transpired:

- *The budget requirement for financial year 2016 was only made available for audit purposes four weeks following NAO's request.*
- *Workings provided showed a budgeted expenditure of €62,285,152. No consideration was given to the annual interest derived from the Foundation for Church Schools, which amounted to €3.65 million, intended to set off part of this expenditure. As a result, these figures could not be reconciled with the €63 million allocated.*
- *Although NAO requested further documentation relating to the 2016 budgetary allocation from MEDE, no such records were made available. NAO could not therefore review the budgeting process.*

Developments: *Fully Implemented*

- The annual budget requirement for the years 2019 to 2021 was forwarded to MEDE in August 2018, well before the established deadline and forwarded to NAO in a timely manner.
- Interest from the Foundation for Church Schools was listed as €2 million in the 2019 projections and as €500,000 in the budget calculations for the following three years, i.e. 2020 to 2022. This interest was correctly deducted from the budgeted projections.
- Signed annual projections for Funding of Church Schools for the years 2019 to 2022, together with a thorough analysis showing the information used for these calculations, were forwarded to NAO, evidencing that a detailed exercise was undertaken by SFCE to derive the budgeted figures.

Reconciliation not performed

MEDE confirmed that no reconciliation was ever performed in order to ascertain whether the total funds transferred to cover staff salaries actually tallied with the approved expenditure.

Developments: ***Fully Implemented***

Adequate reconciliations are being performed to ensure that financial assistance tally with the approved staff expenditure. The following relate:

- Reconciliations in relation to paid salaries were carried out on a monthly and annual basis by MEDE. A standard operating procedure in this regard was also forwarded to NAO.

- In January 2018, MEDE reconciled the staff lists and the corresponding salary scales held by the Education Department against the information provided by SFCE with respect to a sample of four schools chosen at random.

- Following a request for quotations, in October 2019, a local accounting firm was awarded a contract to reconcile reimbursements to all Church Schools on an annual basis.

Monthly Claims not substantiated

Individual salary costs approved for payment by MEDE could not be reconciled against claims made by SFCE as the latter did not keep a detailed breakdown of the actual monthly staff expenditure financed by the State. In 2001, NAO had already brought this matter to the attention of the relevant authorities.

Developments: ***Fully Implemented***

A comprehensive list of monthly salaries paid to all Church Schools in 2018 was compiled by SFCE. This information allows for the appropriate reconciliations to be carried out.

Entitlement to Resources

According to MEDE, each school's entitlement was always computed in accordance with the Guidelines to Church Schools' Entitlement of Resources. However, this could not be confirmed by NAO as relevant official records were not made available for audit purposes.

Developments: ***Fully Implemented***

A capacity building exercise for the scholastic year starting September 2019 was forwarded to NAO. This was based on a set of Classification Guidelines (non-state schools) which was issued to assist in identifying these requirements.

Conclusion

NAO satisfactorily noted that considerable effort was made by the Ministry to address the shortcomings highlighted in the 2016 Report in order to strengthen its controls and ensure compliance.

Commerce Department

Background

The National Audit Office (NAO) published a Report entitled 'Commerce Department – Trading Licences Revenue' in the Report by the Auditor General – Public Accounts[1] 2015. The main objective of this audit was to ensure completeness of revenue from trade licences during the year under review and to evaluate the level of existing controls and procedures in place by the Commerce Department (CD) in its collection process.

The audit had revealed a number of issues, including insufficient verification of application detail requirements. Other shortcomings had been noted in the collection of arrears of revenue.

Audit Scope and Methodology

The scope of this follow-up was to enquire on the developments made following the abovementioned audit, and to assess the extent to which the Department has acted upon the recommendations put forward by NAO. Related Management comments submitted by CD in response to the audit findings were also referred to.

Meetings were held with the respective officials, whereby this Office was informed of the progress made by the Department since the initial audit. A set of questions was then prepared, seeking clarifications and supporting evidence. Management's feedback to our queries was analysed and incorporated in this Report accordingly.

Findings and recommendations proposed by NAO, as featured in the 2015 Annual Audit Report, are reproduced in grey text. Developments pertaining to each issue follow.

Key Issue

Insufficient Verification of Application Detail Requirements

Although CD checked that each application form was filled in appropriately and that all required documents were submitted, NAO did not trace any evidence in file that information listed in the application form was verified for correctness. Furthermore, no evidence was provided that CD confirmed that, the applicant(s) would have not commenced operations prior to date of application.

NAO recommends that CD liaises with other entities to verify that trading activity commenced as declared in the application form, besides that all information was correctly submitted. It is also suggested that in the case of new applications, on-site spot checks are carried out by the Department to obtain further assurance prior to respective trade licence issuance.

The Department is also to enforce penalties, as stipulated in Trading Licences Act, 2002 (Cap. 441), to avoid situations where businesses trade without the proper authorisation.

[1] Hereafter referred to as the Annual Audit Report.

Developments: ***No Longer Applicable***

In view of the legal amendments made to the trading licensing regulations in 2017, individuals opening a premises-based commercial activity, are no longer obliged to register with CD. In effect, the Department started issuing only licenses to the following categories, namely street hawkers, market hawkers, marketing agents, auctioneers, pedlars and credit reference agencies. Enforcement powers, including charges of penalties shall, until new legislation is introduced, remain the responsibility of the Malta Police Force.

Control Issues

Discrepancies between the Department's Reporting Systems

The Department records all transactions in relation to trade licences using the Licence Management System (LMS), which captures all information on such licences administered by the Department. On the other hand, its Accounts Section makes use of the Departmental Accounting System (DAS) to record all related monetary transactions.

Whilst examining the reports provided from the respective systems by CD, pertaining to revenue from trade licences for the year ended 31 December 2015, a discrepancy of €119,642 in the closing figure (DAS - €1,752,734, LMS - €1,633,092) was noted.

Reconciliations are to be performed on a regular basis to detect any material misstatements that may have an impact on the closing revenue figure, as reported by the two systems. This would ensure the reliability of any information extracted from both LMS and DAS for control or reporting purposes.

Developments: ***Fully Implemented***

The processing officers are now reconciling revenue received daily. For better control, cash and cheques are deposited to the Central Bank of Malta and remittance is sent to the Treasury Department on a weekly basis. At the end of the month, total cash and cheque payments received are further reconciled with the monthly totals as per LMS and reconciled manually with DAS monthly report. NAO viewed the whole process as described by CD, obtained the necessary evidence and noted no exceptions.

Accumulation of Arrears due to Delayed Action by the Department

Revenue in arrears was accumulated to significant high amounts over a considerable period, due to untimely or insufficient action taken by the Department.

In a number of instances, a judicial letter or notification was issued to the respective defaulters, followed by an annual reminder generated automatically by LMS. However, no further evidence was traced to control the increasing levels of uncollectable licences. Total arrears of revenue pertaining to sampled cases amounted to €240,252.

The Department is to increase its efforts to control arrears of revenue and reduce such amounts to an acceptable level. Timely and effective action is to be taken to safeguard the interests of the Department and collect what is due to Government.

In cases where no payments are effected within the timeframe stipulated by the renewal notice, CD is expected to take note of the defaulters and proceed with immediate action to recoup the outstanding amounts. Corrective action taken in a timely manner in cases of late payments, will avoid situations of legal prescription.

Developments: *Partly Implemented*

Arrears of revenue in relation to licences issued after 2017 are minimal, both due to the legal amendments and since the licence is issued every three years. Balances relating to arrears preceding 2017, which are mostly premises-based, are not easily recoverable. Thus, in 2019, 585 legal letters were sent to the licensees in order to effect payment, out of which a total of 65 responses were received; 41 effected some form of payment, whilst the remaining 24 provided evidence that fees were not due.

According to CD, during the first quarter of 2020, it shall initiate action to follow up the cases where no response was received.

Compliance Issue

Remittances to Public Account not effected in a Timely Manner

In view of the limited human resources, bank remittances and reconciliations were not being performed daily. Deposits to the Central Bank of Malta were being effected at long intervals. Moreover, all stages of collection, recording and depositing of monies were done by the same designate.

The strengthening of the Accounts Section will enable the Department to improve the internal control setup, as well as assist in reducing inherent risks. Cash and cheques are to be deposited on a regular basis, to ensure that the handling of public funds is done with utmost care and diligence.

Developments: *Fully Implemented*

Although the Department has one Accounting Support Officer who caters for cash receipts, cash and cheques are now deposited in a timely manner. This is also due to the fact that revenue from licencing fees is minimal, following changes in regulations.

Conclusion

NAO satisfactorily noted that adequate action by CD has been taken on the shortcomings reported in the 2015 Annual Audit Report.

Foundation for Educational Services

Background

The Annual Audit Report of 2015 published by the National Audit Office (NAO) included a write-up on the expenditure incurred by the Foundation for Educational Services (FES). The main focus was on personal emoluments and the procurement of contractual and professional services. The objectives of the audit were:

a. to verify that the level of internal controls in the payroll process was adequate; and

b. to ensure that the procurement of services was duly authorised, within the approved limits and in line with the provisions of standing public procurement regulations. Testing was also aimed to obtain reasonable assurance that payments effected were accurate, duly covered by supporting documentation enabling verification, and in line with applicable agreements.

The audit revealed that due to the lack of internal controls, attendance records maintained could not be considered as reliable. Moreover, no evidence was obtained to confirm that payroll is adequately verified prior to processing and that overtime was approved before it was performed. Shortcomings were also encountered in the procurement of cleaning services which was covered by three separate concurrent contracts, awarded restrospectively.

Audit Scope and Methodology

The scope of the follow-up was to determine the extent to which Management has acted upon the recommendations put forward by NAO with respect to the abovementioned audit.

An introductory meeting was held with Management in order to obtain a general insight of the actions taken to address the highlighted shortcomings. The exercise also included an analysis of the supporting documentation provided, assessing the extent of the implementation progress, as well as the effectiveness of the said actions. For reference purposes, a summary of the followed-up findings and respective recommendations which featured in the 2015 Report are reproduced in grey text below.

The developments pertaining to each issue are indicated according to a set scale outlining the stage of the process leading to the resolution of the issue.

Key Issues

Shortcomings in the Financial System

A financial governance review exercise carried out in 2015 identified various weaknesses in the financial management at FES, amongst which was the fact that the then Chief Executive Officer was not being provided with any management information and was thus oblivious to the financial situation of FES and the other subsidiary services provided by the Foundation. In addition, only the bare minimum of financial documentation was retained by the Foundation and this was mostly scattered in unfiled piles of paper.

It was also noted that the Foundation did not account for social security contributions as well as final settlement tax, covering a six-month period and amounting in excess of €600,000, which were collected on behalf of FES employees. These were then settled directly by the Ministry for Education and Employment (MEDE) in January 2015.

Though various internal control measures were implemented following the conclusion of the abovementioned financial governance review exercise, NAO still highlighted various observations including:

a. inadequate attendance records and verification;

b. shortcomings in overtime approval; and

c. inadequate filing of documents leading to a lack of audit trail.

Financial and human resources management are of critical importance within every entity. In this regard, Management was encouraged to implement and maintain adequate procedures to attain a robust internal control environment.

Developments: *Significant Progress*

Through restructuring and engagement of new employees, the Foundation's administration function was strengthened, improving the internal control set up and reducing the inherent risks.

Management accounts are now being prepared regularly on a quarterly basis. A reply to the Management letter, drawn up by external auditors following the conclusion of the audit, is also being compiled accordingly.

The statutory dues payable to the Inland Revenue Department were all settled in November 2018. Since then, applicable deductions were being remitted to the foregoing on a timely basis, i.e. by the end of each payroll period.

Yet, room for improvement was noted with respect to overtime approval and the weekly endorsement of attendance records, as detailed further down in the Report.

Inadequate Attendance Records and Payroll Verification

During 2015, FES relied solely on manual records for registering the attendance of its employees as automated devices were not yet installed. Only the timesheets prepared by part-timers were endorsed; attendance registers for full-time employees were not. Additionally, during fieldwork, NAO did not obtain evidence to confirm that payroll within FES is adequately verified prior to processing.

Given the substantial amount paid on salaries, NAO recommended the implementation of attendance verification devices, to facilitate the payroll and make it less prone to error whilst reducing the possibility of abuse. On the other hand, effective verification measures were to be incorporated within the payroll process where the introduction of such devices was not considered feasible by FES.

Developments: *Significant Progress*

An automated attendance verification system was installed at Head Office in 2017; however, to-date attendance was still recorded manually at the various centres managed by the Foundation. Notwithstanding that attendance sheets were checked at each centre by the respective coordinator, it was noted that these were endorsed by the latter at the end of the four-week pay period, implying that certification was not carried out on a weekly basis as stated in the Public Service Management Code. These records were then passed over to the Head Office, mainly to take note of vacation leave and sick leave, as well as for arithmetical verification prior to inputting the related data in the payroll system.

Control Issues

Prior Approvals to perform Overtime not official

Section 15 of FES collective agreement[1] *requires that, except in emergency situations, overtime work is to be officially approved in writing prior to its performance. However, from documentation relating to the three officials in the audit sample who were paid overtime, NAO could not confirm that this requirement was met, as the date when overtime was approved was not indicated.*

In order to be processed for payment, overtime is to be approved prior to the commencement of the respective tasks in line with FES collective agreement. Supporting documentation is to be filed for ease of reference and audit purposes.

[1] *Collective agreement covered from 31 July 2015 to 31 December 2018.*

Developments: *Partly Implemented*

According to Management, unless formal approval is obtained prior to the carrying out of overtime work, claims for the respective payment are not honoured. However, testing carried out on documentation in relation to overtime worked in the sampled month of June 2019 revealed that out of 51 instances:

- in six occasions, the date when approval was granted was not disclosed; and
- in another two cases approval was solicited after the work was performed.

Shortcomings in Personal Files

In a number of instances, documents in the personal files reviewed were loosely inserted instead of orderly filed; as a result, the foregoing were not being properly updated. Additionally, the personal files did not contain a record of the officers' basic pay since their employment with FES. Thus, in the case of promotions, the correctness of their salary pay could not be confirmed with accuracy.

Personal files are to be kept updated with all the necessary documents, especially those relating to emoluments. Besides enabling ease of reference, as well as verification by third parties, this ensures a smoother transition in the event of a change in human resources personnel.

Developments: *Fully Implemented*

From verifications carried out on a sample of eight personal files, it was noted that these were updated with all relevant documentation, including a signed employment contract, which records were numbered for ease of reference and filed accordingly in a timely manner.

Cleaning Services

Following calls for tenders, three separate contracts were awarded concurrently and at the same rate to a private company for the provision of cleaning services at the Childcare Centres, Klabb 3-16 Centres and FES Head Office respectively. The one-year agreements, which were awarded on the basis of the cheapest rate[2] per hour, were signed retrospectively on 16 February 2015 with effect from 1 January 2015. The collective value of these contracts amounted to €201,587. The following shortcomings were noted in this respect:

a. *In five cases pertaining to two of the sampled invoices, NAO was not able to tally the hours claimed on the invoices with the timesheets presented, since supporting documents were either missing or illegible.*

b. *Several variances were noted between the hours charged and the hours logged on the timesheets in three invoices from the five verified.*

[2] *Tender rate per hour was €5.80 amended to €6.29, both exclusive of VAT, in accordance with Contracts Circular No. 4/2015 – 'New Regulations regarding the Award of Services Contracts within the Public Administration'.*

c. *In six instances, covering 297 hours, the relative timesheets were not countersigned by the area coordinator, yet the documents were still processed for payment.*

d. *As per contracts dated 16 February 2015, the service provider agreed to submit a performance guarantee, amounting to €10,800 each, in respect of two tenders awarded. However, the performance guarantees submitted, both valid for one year each, in aggregate amounted to €6,600 less than the required amount.*

Claims for payment should only be settled following a thorough reconciliation with duly endorsed supporting documents, in order to ensure correctness. It is also to be ascertained that contractors submit the required performance guarantee in full for the respective contracts to avoid undue exposure to the related risks.

Developments: *Partly Implemented*

In 2017, an agreement was made with MEDE so that the provision of cleaning services at the centres falling within the Foundation's remit will be carried out under the same contract that the former has in place for state schools. Claims for reimbursement of expenses were then forwarded to MEDE every quarter, based on an estimated number of utilised hours[3], multiplied by the service charge rate. This information was obtained from spreadsheets created by the then Head of Business.

However, FES did not have in its possession a copy of the related contract and the respective timesheets to verify the applicable rate and the actual number of hours performed at the individual centers. Hence, the correctness of payments effected could still not be ascertained.

At the Head Office, cleaning services were procured in line with a call for quotation, whereby on 17 June 2019, a request for a quote was sent to three specific service providers. The cheapest bidder was awarded a six-month contract for cleaning services starting 22 July 2019, up to a threshold of €5,000 excluding Value Added Tax (VAT).

Central Filing System not in place

The Foundation did not have a central registry system in place to keep track of official files and their movements.

FES was encouraged to set up a centralised filing system as soon as possible. This will ensure ease of reference as well as an adequate audit trail and business continuity in the event of a change in roles and responsibilities within the organisation.

Developments: *Not Implemented*

A central registry system maintaining an official record of existent files and their movement was not yet developed. According to FES, files are opened for specific purposes and thus these are located in the respective section and rarely transferred to other departments. Management maintained that a registry system was therefore not required.

[3] During 2018 and 2019 these remained fixed.

Compliance Issues

Lists of Direct Orders and Departmental Contracts not published

FES confirmed that in breach of pertinent regulations, lists of departmental contracts awarded, including purchases effected through direct orders procedures, as well as cases involving variations of more than 5%, were not published in the Government gazette.

Officers in charge are to be fully aware of the relevant regulations and are to ensure that the required publications in the Government gazette feature accordingly in a timely manner.

Developments: *Fully Implemented*

In compliance with Article 111(2) of the public procurement regulations, where applicable, the Foundation published in the Government gazette a list of awarded direct orders and tenders.

VAT Receipts not submitted

VAT receipts were not attached to the relative original invoice for ease of reference but were kept in a separate file. Additionally, two service providers failed to supply VAT receipts, in aggregate amounting to €35,554, against the respective payments made.

FES confirmed that it never reported VAT defaulters to the pertinent authority up till the time of audit, as Management was not aware of the requirements stipulated in the relevant circulars.

Effort is to be made to enforce the principle that VAT receipts are invariably obtained for every purchase of goods and/or service, in line with VAT regulations. These are to be kept in the same file to support the respective payments.

Developments: *Partly Implemented*

Whilst it was noted that VAT receipts were now attached to the respective payment voucher, defaulter lists were still not being compiled and reported accordingly. Following this follow-up audit, the Foundation took the necessary action to comply.

Financial Accountability

The stipulated deadlines, established by the statute attached to the Foundation's deed, for the submission of statutory documentation[4] to the Minister responsible for Education, were not adhered with.

Management is to ensure that the audited financial statements and other information, as required by the statute of FES, are submitted by the established deadlines.

[4] *Audit report and financial statements of the previous year are to be submitted by not later than the end of March each year, whilst the business plan for the following three financial years, together with an estimated budget of income and expenditure for the following year are to be forwarded by end of May each year.*

Developments: ***Fully Implemented***

NAO satisfactorily noted that the Foundation complied with the reporting requirements, both as regards auditing timeframe, as well as the submission of the business plan and the estimated budget of income and expenditure within the established deadline.

Conclusion

NAO acknowledges that significant efforts were made by Management to take on board recommendations put forward in the 2015 Audit Report. However, stricter controls are still to be implemented, especially for the procurement of cleaning services at the centres falling within the Foundation's remit.

Malta Communications Authority

Background

The Annual Audit Report (AAR) for 2016, published by the National Audit Office (NAO), included a write-up on the revenue collected by the Malta Communications Authority (MCA). The main objective of the audit was to evaluate the adequacy of the procedures in place for the collection of revenue, as well as to ensure that the income received was duly recorded by the Authority and forwarded to Government in a timely manner.

Audit Scope and Methodology

The scope of this follow-up, which was carried out through various meetings held with MCA officers, was to enquire on the developments registered following the foregoing audit. Management's feedback to NAO queries were analysed, and supporting evidence was requested to substantiate any assertions made and to establish the extent of the progress made.

A summary of the findings and recommendations proposed by this Office, as featured in the 2016 AAR, are reproduced hereunder in grey text, followed by the developments pertaining to each issue.

Key Issues

Untimely Transfer of collected Fees to Government

During 2016, MCA issued several invoices for postal fees and other fees of office. However, although all these invoices were settled throughout the same year, the Authority only forwarded the fees collected to Government[1] in one tranche on 31 January 2017. NAO noted other instances whereby fees relating to Scarce Resources, with some of the individual amounts approaching half a million Euro, were transferred to Government with a delay of up to three months.

Fees collected from operators on behalf of Government are to be remitted to the respective Ministry without undue delay, thus ensuring diligent handling of public funds. This would also enhance cash management by Central Government.

Developments: *Fully Implemented*

During 2019, invoices for Scarce Resources and postal fees were issued to major operators on a quarterly basis, while the small postal operators were invoiced annually. From the bank documents made available for

[1] *Net of deductions.*

audit purposes, it was noted that MCA effected quarterly transfers to Government, thus income collected was remitted within reasonable timeframes.

Reliance placed on Information provided by Operators

Invoicing of Fees for Rights of Use was based on information submitted by the respective operators, without MCA carrying out any independent verifications on the correctness of such information.

In the case of licences for operation of radiocommunications in the Private Mobile Radio, the location of any equipment comprising a fixed installation would be known to MCA, as the respective details are included in the licence application; however, the same cannot be said for mobile and portable equipment. Therefore, the risk that such equipment is not duly registered with the Authority, possibly leading to undercharges, could not be adequately addressed through on-site verifications.

MCA was recommended to propose more effective methods of verification leading to levying of fees to licensees. The Authority was also encouraged to increase the number of inspections it carries out on different operators and also to keep abreast with the latest technological developments, which could be beneficial for the detection and identify any unlicensed use of links and/or equipment.

Developments: *Fully Implemented*

In 2017 and 2018, MCA adopted an inspection methodology in line with a report issued by the International Telecommunication Union[2]. Based on the results obtained through scrutiny in the foregoing two years, the Private Mobile Radio was considered as a low risk area. Hence, as from 1 January 2019, inspections on these licences were carried out solely in particular instances, such as the issuance of a new licence. With the aim of ensuring constant compliance of already inspected licences, the Authority also carried out 30 inspections during the year under review.

Furthermore, to reduce the risk of abuse, S.L. 399.40 – 'General Authorisations (Radiocommunications Apparatus) Regulations' were amended, now requiring dealers[3] to programme only equipment whose radio frequencies or channels were assigned in writing by MCA. The latter held one-to-one discussions with dealers to explain their legal obligations.

In January 2019, MCA also submitted proposals to Government to simplify the radiocommunications licensing regime for the amateur radio service. As at time of audit fieldwork during the first quarter of 2020, these proposals were still being considered. Moreover, in May 2019, the Authority issued a call for tenders through the Department of Contracts for the 'Supply, installation and commissioning of a state-of-the-art radio spectrum monitoring system', in an attempt to detect any unlicensed use of links and/or equipment.

To ascertain the effectiveness of monitoring carried out by MCA, NAO obtained the list of inspections performed by the Authority during 2019 and corroborated information with the respective reports. Five inspection

[2] The union is the United Nations specialised agency for information and communication technologies.
[3] Any person engaged in commercial activity to sell, programme or configure apparatus.

reports, selected randomly, were reviewed and the details of the quantity and models of the apparatus found on site were verified against the information on the respective licences. The accuracy of amounts charged by MCA was also confirmed against S.L. 35.01 – 'Fees Leviable By Government Departments Regulations'. No shortcomings were noted by NAO.

Control Issue

Weaknesses in Radiocommunications Licensing and Invoices

Different computer programs were utilised by MCA for issuing radiocommunications licences and the corresponding invoices to operators. The Authority first obtained details through a manual application form that is compiled and submitted by the prospective licensee. The relevant details were subsequently inputted in a computer program and, after the required checks were carried out, MCA invoiced the operator. Once payment was effected, the licence was then issued from a word-processing software.

All invoicing was carried out through one computer application; however, the method for calculating the respective fee depended on the type of licence in question. The use of different programs, as well as the manual inputting of information at various stages, increased the possibility of errors in the chargeable fee. In fact, during the audit, two such errors were encountered from the sample tested.

The Authority was encouraged to explore feasible ways of integrating the computer programs currently in use, thus reducing the likelihood of errors. Manual processing of data was also to be kept at a minimum.

Developments: *Fully Implemented*

Following the audit carried out for financial year 2016, the information technology accounting system used for radiocommunications was integrated to that used for the issuance of invoices; thus reducing the manual input.

Conclusion

NAO satisfactorily noted that shortcomings identified in the 2016 AAR were addressed by the Authority. Management is encouraged to maintain its current efforts with regard to the simplification of the radiocommunications licensing regime.

Malta Film Commission

Background

In its Annual Audit Report (AAR) for 2016, the National Audit Office (NAO) published the outcome of an audit carried out at the Malta Film Commission (MFC), which mainly focused on the adequacy of internal controls prevailing with respect to the provision of cash rebates to qualifying film producers, and to determine whether operations reflected efficient administration of public funds, in line with standing terms, conditions and regulations.

Audit Scope and Methodology

The scope of this follow-up was to assess Management's actions following the recommendations presented by NAO in the 2016 AAR.

Meetings and reviews of supporting documentation were carried out to identify the developments made.

For reference purpose, followed-up findings and respective recommendations as featured in the previous Report, are reproduced in grey text below. Developments pertaining to each issue follow.

Key Issue

Potential Loss of Revenue to Government

While the Government paid significant amounts of money to film production companies by way of cash rebates, audit findings showed that no effective controls were in place in this respect, especially with regard to income attributable to Government in the form of tax payable.

It was recommended for MFC to extend the remit of its auditors to verify the eligibility of the cash rebates, confirm their validity, and ensure that revenue due to Government is duly paid and any irregularities reported accordingly in a timely manner.

Developments: *Partly Implemented*

According to Management, the revision of the cash rebate guidelines, which came into force on 1 January 2019 adopts a stricter stance with respect to the necessary verifications ahead of issuing the respective cash rebates. In fact, a full audit of the expenses is now required, except for reimbursements of amounts less than €100.

To substantiate Management's claim of these verifications, a production from 2018 and for which the respective rebate was paid in 2019, was selected for testing. However, it transpired that the new guidelines were not yet being applied for rebates relating to 2018 productions. Details highlighting the results of such testing are reported upon under each pertinent observation in this follow-up Report.

Control Issues

No Formal Approvals and Divergences from the indicated Salary Packages

Controls with respect to allowances paid to officers were completely lacking. It also transpired that the organisational structure indicating the respective salary packages consisted of an undated spreadsheet which did not cover all positions. Instances were also noted whereby salaries paid to employees exceeded the amounts stipulated in the said organisational structure, with certain individuals being in receipt of allowances for which they were not entitled to.

The organisational structure and respective salary packages are to be formally approved, clearly indicating the date of such approvals and when the related provisions come into force. Moreover, rather than maintained on a spreadsheet, these records were expected to be in a document which cannot be manipulated. Adequate control over the payment of allowances was also encouraged.

Developments: *Insignificant Progress*

The Commission's organisation structure, which was valid up till year 2018, was not updated by the time this follow-up audit was concluded, i.e. end January 2020. Negotiations were still underway between MFC and the pertinent Unit to update the former's grading salary structure for the four-year period 2019 to 2022.

Instances of divergencies between salaries and allowances paid to officers as per payslips and those stipulated in the employment contracts and salary structure were again noted. Following queries raised during this follow-up, in November 2019, MFC carried out an exercise to align salaries and allowances paid to its staff with the employment contracts.

Lack of Records substantiating Payroll

No attendance records were available for MFC staff and several of the employees working at the Malta Film Studios. Furthermore, those made available with respect to the remaining staff employed by the latter did not cover the full year under review and were not certified correct.

Management was encouraged to maintain certified records, in line with the provisions of the Public Service Management Code, thus ensuring that all employees were duly accounted for at all times.

Developments: ***Fully Implemented***

As from October 2019 an access control system, entailing an electronic finger-print reader was installed at the Commission's premises. The system started being used to maintain the attendance of all staff working at MFC as well as the Malta Film Studios.

Film Incentives

Tax on Income not paid in its entirety

The amount of income tax paid by actors could not always be verified due to lack of and/or incomplete documentation.

Moreover, testing performed on the list of extras, whose Payee Statement of Earnings forms (FS3s) were forwarded to the Inland Revenue Department (IRD) by the local production company also revealed that details of over 5% of the extras in the sampled production were not included therein[1].

Management was recommended to carry out thorough checks, confirming that income considered to be earned in Malta has been declared in full. Moreover, all documentation required to perform the necessary verification were to be maintained. Complete and accurate information is also to be filed with IRD together with the respective payments and verified prior to providing the cash rebates.

Developments: ***Partly Implemented***

During 2019, measures were introduced with regard to tax payments, whereby production companies were required to present the following documentation upon applying for financial incentives:

- copies of Value Added Tax (VAT) returns as submitted to the respective department together with a detailed report of the VAT return and relevant receipts, showing that tax was duly paid to the Government;
- tax[2] compliance certificates; and
- payslips, proof of payment of the withholding tax, as well as returns submitted to IRD and related receipts.

From testing carried out on the sampled production it was noted that income of €44,499 earned in Malta by 22 foreign actors was supported by the necessary documentation. However, receipts to confirm that the relative tax portion of 10% was remitted to IRD, were only traced for two individuals. Management claimed that the tax portion for the remaining 20 actors was paid in the respective employing country.

[1] *Such records were provided to NAO by IRD.*
[2] Including VAT, final settlement system and social security contributions compliance certificates.

Expenditure incurred on payroll costs pertaining to employees engaged by the local production company was properly backed up by sufficient documentation[3]. Moreover, no discrepancies were noted between the related employee records as maintained by IRD and those provided by MFC for the purpose of this exercise.

Expenses claimed not duly substantiated

In their majority, expenses claimed for rebate purposes were not supported by an agreement, with the only documentation available consisting of invoices and purchase orders, thereby hindering verification of correctness of amounts being claimed.

Services over an established threshold are to be, as far as possible, backed up by an agreement, clearly setting out the terms and conditions, period covered and rates applicable.

Developments: *Partly Implemented*

As from 2019, invoices claimed for rebate purposes by qualifying companies were to be supported by a valid proof of payment, being either a copy of the bank transaction, copy of cashed cheque or a supplier receipt. In addition, costs exceeding €50,000 for which a benefit is being claimed are to be supported by agreements.

Starting from 2019, as an additional level of control, during the filming of productions, the funding unit within MFC has carried out spot checks to ascertain that items presented in budgets were actually used on set and any doubts were highlighted to the respective private auditors.

The sample of expenditure reviewed for the purpose of this follow-up, amounting to 30% of the total eligible costs[4] claimed for rebate by the qualifying company, was supported by proper invoices. However, no valid evidence of payment was provided for 39% of the sampled expenses. As a result, no comfort could be obtained on whether the respective expenditure was actually paid. Moreover, agreements outlining the terms and conditions of the service being acquired, especially in the case of substantial amounts, were generally missing.

Conclusion

This Office acknowledges the Commission's efforts in taking the first steps in an attempt to address the shortcomings highlighted in the 2016 AAR. However, the need for more thorough checks is to be emphasised, especially in the light of the requirements of the updated cash rebate guidelines. Management is also encouraged to direct attention towards the remaining unaddressed matters, to enhance the efficiency and effectiveness of its operations.

[3] This entailed a detailed payroll analysis together with copies of the relevant payslips, Payee Statement of Earnings forms (FS3s) and Payee Status Declarations (FS4s).
[4] Total eligible expenditure (excluding payroll costs) aggregated to €1.7 million.

Medicines and Surgical Materials

Background

The National Audit Office (NAO) published a report entitled 'Medicines and Surgical Materials' in the Report by the Auditor General – Public Accounts[1] 2016. The audit covered expenditure incurred by the then Ministry for Energy and Health on medicines and surgical materials in 2016.

The audit had revealed shortcomings, including issues related to the management of the allocated funds, security controls and others relating to stock records.

Audit Scope and Methodology

The scope of this follow-up was to enquire on the developments following the abovementioned audit and assess the extent to which the recommendations put forward by NAO were acted upon. Related Management comments submitted by the Ministry were also referred to.

Meetings were held with the respective officials to discuss progress registered since the last audit. Further comments, clarifications and supporting evidence were also requested. Following verification of documentation obtained, Management replies were analysed and incorporated in this Report accordingly.

Findings and recommendations proposed by NAO, as featured in the 2016 Annual Audit Report, are reproduced in grey text. Developments pertaining to each issue follow. However, in view of the specific technical and medical factors, NAO was not in a position to verify the validity of particular explanations given by the Central Procurement and Supplies Unit (CPSU) Management.

Limitations on Scope of Audit

Physical Counting of Stock

A private audit firm was primarily responsible for carrying out the stocktake undertaken during January 2017. According to Management, a report showing discrepancies between physical counts and stock records, together with the relative explanations, was still in the process of being compiled by end May, when the audit was in its final stages. Although a report showing discrepancies was submitted in July 2017, the relative explanations remained pending by end September, when the Annual Audit Report was concluded.

[1] Thereafter referred to as the Annual Audit Report.

Developments: *Significant Progress*

Instead of the annual stocktake, CPSU had planned quarterly stock counts for the year 2019 together with regular weekly cyclic counting. However, according to Management, the occurrence of a series of events that necessitated the re-opening of the ex-general stores and medical stores in Gwardamanġa to cope with an increase in stockpiling due to Brexit as per Government direction, as well as the Falsified Medicines Directive and the robotics project, brought a strain on the human and financial resources.

As a result, only two such counts, each covering approximately 66%[2] of total stock value, were executed. The analysis of the resulting discrepancies was made available to NAO.

Expired Stock not marked accordingly

Enquiries concerning expired stock that was not identified as such by Management remained pending by the end of the audit. The aggregate value at cost of these items was €861,860.

Developments: *Fully Implemented*

The stock report as at end October 2019 provided for audit purposes did not contain any expired items.

Key Issue

Management of the Allocated Funds

a. *Although CPSU could take cost efficient measures in procurement and stock management, actual consumption depended entirely on generated requests by the respective health entities. Moreover, the entities concerned were not allocated a budget to manage and for which they would be held accountable for any variations arising thereto.*

b. *CPSU started invoicing St Vincent de Paul Residence for supplies as from January 2015, since the latter was no longer under the responsibility of the same Ministry. However, no reimbursements were received for supplies issued since then. Pending reimbursements had since reached €2,432,429.*

It was recommended that Management's intention to ring-fence such budget on the entities, so that each is accountable for the respective allocation, was to be implemented as soon as possible.

[2] The average value of stock counted during these two exercises amounted to €16,641,213. On the other hand, records made available at the beginning of the audit indicated a total stock value of €25,267,245 as at end October 2019. If one assumes that this is the average stock value held throughout the year, stock checked would be equivalent to 66% of the stock value. Throughout these quarterly counts, CPSU intended to check each item in stock at least once annually, whereas others would be checked more frequently.

Developments: ***Insignificant Progress***

The same situation prevailed in 2019 whereby entities were still not being allocated a budget to be held accountable for any resultant variations. Management claimed that previous plans to allocate budgets onto different entities had changed. In line with the Ministry for Finance's direction, it was decided that total budgetary control should rest within CPSU to ensure proper financial and administrative management and adherence with the applicable regulations, amongst others. It was stated that consumption within entities is monitored and spikes in demand require justification.

Moreover, NAO noted a substantial increase in outstanding reimbursements compared to the €2,432,429 as at end 2016 since, beginning December 2019, pending dues to CPSU from the Active Ageing and Community Care Department and Steward Health Care Malta amounted to €7,434,346[3] and €16,652,405 respectively.

Control Issues

Security Controls

Strict access control only applied in the room assigned for the storage of dangerous drugs, but not throughout the remaining area of the main stores in San Ġwann, where no restrictions were in place to limit the right of entry to staff. Moreover, access to both the receiving and dispatch areas was available through front and back entries, even to outsiders. Additionally, closed circuit television cameras did not cover all areas. These weaknesses increase the risk of intrusion and theft.

Whilst acknowledging that plans were underway for the enhancement of security controls, remedial action was not to be unduly prolonged. CPSU officers were to be assigned physical accessibility only to designated areas, as required, to enhance accountability, while entry by outsiders was to be forbidden.

Developments: ***Fully Implemented***

Closed circuit television cameras covered all areas within the main stores in San Ġwann, whilst access controls were being installed during the course of this review. In order to enhance controls and limit the risks identified, the Unit has set up a structure of four teams of security personnel. These officers were assigned within the stores, at the receiving and dispatch areas, in the guard room and occasionally within the reception area. Notwithstanding this, CPSU claimed that the staff complement needed to be supplemented.

[3] Of this amount, €6,896,599 relates to St Vincent de Paul Residence.

Computer Stock Records

The following issues were noted from an analysis of the report[4] containing stock costing €18,031,558, which was issued by Management on 16 January 2017 for stocktake purposes:

Expired Items

a. *The final stocktake report included a list of 29 entries marked as expired and valued at €325,846, some of which had been expired since January 2014.*

b. *A considerable number of expired stock items recorded at an aggregate cost of €861,860, some of which were expired for over five years, were not marked as such. According to Management, not all expired stock was disposed of following a board of survey as some items could be returned to supplier for replacement or credit.*

Management was to endeavour to limit the amount of expired stock as much as possible in order to avoid the waste of resources. When such expiry was inevitable, action to write off the respective stock, in line with the General Financial Regulations and Treasury Circular No. 6/2004 – 'Stock Control Procedures', was to be taken within a reasonable time. Input of information was to be accurate and complete.

Items without Expiry Date

Expiry date was not recorded for a number of items[5], such as nutritional formula, medicinals and sunblock cream, which became ineffective after the lapse of specific intervals.

Negative Balances

The stocktake report also contained six items with a negative balance.

Stock Items marked at a Zero Cost

The stock report made available to NAO contained no less than 67 entries with a zero value, hampering the accuracy of the information. As a result, the stock value of just one of the items in question was understated by €210,000.

Developments: *Partly Implemented*

According to Management, following NAO's audit, modification of the stock control system was requested. This enabled expired stock to be removed from stock lists by an inbuilt routine. Responsible officers were to

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[4] Besides medicines and surgical materials, this report contained also stationery and cleaning materials held at the Gwardamanġa stores, as well as hardware items kept at the electrical and mechanical stores within Mater Dei Hospital.

[5] NAO did not deem it necessary to quantify such stock as it would have required an analysis of each of the numerous items listed to determine which should have an expiry date and which not.

verify the items earmarked as expired by the system periodically and segregate them to a designated area. These items are then examined by the board of survey and the necessary approvals for write-off are obtained. Thus, records for expired stock are now being kept separately by CPSU. However, expired stock reports and write-off approvals were not provided for audit purposes.

An expiry date was recorded for all items in the stock report. Furthermore, the list did not contain negative balances.

NAO still identified a number of items at zero cost within the stock records. Management stated that these items were supplied in tandem or in conjunction with other items and such costs could not be split. Thus, the full cost is absorbed by the other product.

Accountability Concerns

Corroboration of details obtained from the invoices sampled revealed discrepancies in quantities recorded on the computer system and bin cards, besides other accounting errors.

Enhanced accountability is expected, especially in view of the sensitivity and value of certain stock items. Although NAO acknowledges that discrepancies can never be eliminated in their entirety, more needed to be done to find a reasonable and practical operational solution in order to minimise such differences.

Developments: *Not Implemented*

Similar accountability issues were again noted during the course of this review. CPSU was monitoring progress registered with respect to each procurement through the use of spreadsheets. It was noted that confirmation of orders drawn up by the procurement section and forwarded to the respective suppliers lacked a unique identification number, thus, the receiving section was not always in a position to pair the goods received note with a specific order. Moreover, although CPSU maintained separate files for each stock item, relevant documents were not always filed and/or minuted accordingly.

Anomalies noted by NAO in the procurement process of a particular item remained unanswered notwithstanding reminders. This Office also noted limitations on the management and control of the same item as it was being ordered by various sites and locations directly from the supplier, under the same contract without the cognisance of CPSU. NAO was not informed of the official arrangements in place, if any.

Compliance Issue

Statutory Stock Return not submitted to NAO

In accordance with General Financial Regulations Article 105, CPSU is required to furnish the Auditor General with a stocktaking report outlining the results obtained. Although Treasury Circular No. 6/2004 also spells out this requirement, this return was not submitted to NAO.

The necessary information was to be duly submitted to NAO in line with statutory requirements.

Developments: ***Insignificant Progress***

Management claimed that when the report was in the process of being compiled, all effort was suddenly focused on dealing with the pandemic. As a result, CPSU did not provide such information to NAO, citing insufficient resources.

Conclusion

NAO appreciates that over the last months CPSU's operations had to adjust to abnormal market conditions, due to the pandemic crisis situation, which impacted directly the supply of medicines and surgical materials. Within this context, NAO acknowledges the progress registered in certain areas, such as security and the management of stocks through computer records. On the other hand, there is much room for improvement within the CPSU's overall operations. CPSU Management affirmed that this is subject to a reasonable injection of financial recurrent expenditure and human resources.

VAT Department

Background

The National Audit Office (NAO) published a write-up entitled 'VAT Department – Expenditure and Personal Emoluments' in its Report by the Auditor General – Public Accounts 2015. The objectives of this audit were to verify that, during financial year 2015, there were adequate internal controls on the operational and maintenance expenditure incurred by this Department, as well as that personal emoluments were appropriately processed and recorded.

The main areas of concern following the initial audit included lack of internal controls within the Human Resources (HR) and payroll function. Other shortcomings, particularly but not limited to non-compliance with procurement regulations in the provision of legal services, were also noted.

In July 2019, the Value Added Tax (VAT) Department was integrated with the Inland Revenue Department and, as a result, the administration and HR, including the payroll function of both Departments was merged.

Audit Scope and Methodology

The implementation or otherwise of the recommendations made by this Office in its 2015 Report was the primary focus of this follow-up audit. Management comments submitted thereto by the VAT Department were also referred to.

Following an introductory meeting with Management, the exercise proceeded with an analysis of the supporting documentation provided to back up the extent of the implementation progress by end 2019. For reference purposes, the followed-up findings and respective recommendations, which featured in the previous NAO Report, are shown in grey text below. The developments pertaining to each issue follow.

Control Issues

Personal Emoluments

Discrepancies between Vacation Leave and Time Records

Several inconsistencies were noted between the Vacation Leave (VL) records and that recorded in the Attendance Verification System (AVS).

Management is to ensure that the record keeping of VL is reliable, as well as complete, by carrying out regular reconciliations between the documentation and the applicable system.

Developments: *Fully Implemented*

A daily reconciliation of the attendance records is now being performed by an HR official. This was confirmed from the four randomly selected dates that were checked.

Lack of Authorisation of Vacation Leave

Written approval for VL was not always traced and a number of authorisations were not dated.

In order to maintain an adequate control environment, it is recommended that all VL hours are adequately authorised prior to utilisation, specifying authorisation date.

Furthermore, in order to facilitate VL management, including the application, authorisation and eventual updating of leave records, Management is to consider introducing an electronic system for recording the full VL process. This would ensure that authorising officers are immediately notified of any requests for leave and HR Section is timely informed of the respective approvals.

Developments: *Fully Implemented*

The VL of the five sampled officials for the tested month was duly authorised prior to utilisation. Up to mid-year 2019, VL was authorised through an attachment by electronic mail. Subsequently, the VL system was automated and monitored by the Ministry for Finance (MFIN).

Discrepancies between Sick Leave Documentation and Time Records

Inconsistencies were noted between sickness absences recorded in the payroll system when compared to Sick Leave (SL) hours listed in AVS.

Documentation related to sickness absences is to be checked regularly against time records. Furthermore, the Department may also consider integrating the SL function within the payroll system with AVS, in order to ensure the accuracy and completeness of records.

Developments: *Fully Implemented*

The SL function was not integrated within the payroll system; however, an HR official was tasked to list all officers who reported sick and these were subsequently inputted in the payroll system. NAO observed that SL was adequately reported.

Weaknesses in Recording of Attendance

Sample testing revealed that time records were not being checked for correctness on a regular basis. The following shortcomings were encountered:

a. *Officers failing to clock out at end of working day.*

b. *Telework hours not recorded on time records.*

c. *SL and VL recorded in time records not in line with telework arrangement.*

All VAT officers are to clock out whenever they leave the premises for whatever reason. It is imperative that regular inspections of attendance records are carried out to ensure a sound system of internal control over personal emoluments. Moreover, Management needs to be duly informed of all personnel who are actually on the premises in case of any emergency, such as an office fire.

In addition, all sections within the Department are expected to inform HR in writing whenever officers carry out duties outside premises during office hours.

Developments: *Partly Implemented*

Although a number of reconciliations were performed on attendance records, some shortcomings related to missing time outs were still noted.

Temporary Absences Records not maintained

In line with the Public Service Management Code (PSMC), temporary absences are to be recorded in a temporary absences record sheet. However, the VAT Department was not always in a position to provide justification for temporary absences since the respective template was not filled in.

Management is to ensure that absenteeism is appropriately recorded and authorised by the senior officer in charge, which is important for a reliable audit trail. Disciplinary action is to be taken in case of unauthorised absence.

Developments: *Insignificant Progress*

Office Circular No. 2/2017 – 'Recording of Attendances and Absences', dealing with temporary absence procedure was issued on 4 January 2017, wherein VAT inspectors, apart from filling in the temporary absences record sheet were also required to record their outdoor duties on a logbook. However, a copy of this logbook for the sampled period[1] was not provided for audit purposes.

[1] Sampled period between 23 April and 17 June 2019.

From a review of documentation relating to two of the sampled inspectors, it also transpired that information relating to temporary absence could not always be corroborated with other documents, either due to missing or different information.

Following NAO's queries, another circular was issued on 22 January 2020, reminding employees to make use of temporary absences record sheet.

Inadequate Control on Overtime performed

Overtime records did not portray sufficient evidence of an officer's overtime hours. Moreover, overtime was not duly authorised by Management and the Permanent Secretary. Inaccurate overtime payments were also noted.

The maintenance of accurate and reliable records is a fundamental element of a sound system of internal control over personal emoluments, including overtime. The VAT Department was recommended to review the recordkeeping process in order to enhance the present manual system for the authorisation of overtime and respective calculations.

In view of the Department's constant requirement for overtime, authorisation from the Permanent Secretary is to be requested in line with the PSMC. Management must adequately approve all overtime in advance in order to ensure control over this expenditure.

Prior to settlement of overtime payments, verification is to be made by HR as to whether overtime hours claimed have been actually carried out and that the applicable approvals were not exceeded.

Developments: *Significant Progress*

The Commissioner for Revenue (CfR) officials confirmed that the Department engaged a Manager to take up HR responsibilities. In 2018, the incumbent was transferred to the Revenue Section and the overtime request forms were discontinued for some time. According to the Department, the overtime request forms as per PSMC requirements resumed as from 1 January 2020.

From testing of one payroll period (from 2019) of three randomly selected officers, NAO confirmed that managerial approvals for overtime were obtained. Calculation of overtime payments was also found accurate. However, although the VAT Department has a constant requirement for overtime, authorisation from the Permanent Secretary for the year 2019 was not obtained in line with PSMC requirements.

Employees' Personal Files not safeguarded against Unauthorised Access

The employees' personal files were located in HR office, which office was being shared with other officers from different sections. It was noticed that any officer could easily access the personal files of all employees within the VAT Department.

All personal files should be adequately safeguarded and kept in a secured location, to deter unauthorised access, as well as to reduce the risk of any manipulation of personal information to a bare minimum.

Developments: *Fully Implemented*

Personal files are now adequately safeguarded under lock and key.

Personal Files not properly maintained

In a number of instances relevant documentation was not filed in the employees' personal files.

HR Section is to maintain all relevant documentation in the respective personal file, to ensure a sound system of internal control, as well as a reliable audit trail.

Developments: *Fully Implemented*

The three personal files reviewed included relevant documentation, such as telework agreements, qualification certificates and related correspondence.

Inaccurate Calculation of Allowance

The additional non-pensionable allowance payable to eligible VAT inspectors was not always paid to one of the employees in the audit sample. This resulted in an aggregate underpayment of around €1,719.

To achieve a reasonable level of accuracy, where possible, independent checking is recommended.

Developments: *Fully Implemented*

No shortcomings were identified when verifying the allowances paid to two sampled officials.

Telework Practices not according to Standing Policies

A review of the personal files of the four employees selected in the sample who were working on a telework arrangement, revealed the following observations:

a. *requests for the renewal of telework agreement not properly authorised;*

b. *renewal of telework agreement even though such arrangement was previously terminated;*

c. *clauses in the agreement to control teleworking not adhered to; and*

d. *no evidence that telework was appropriately monitored.*

Irregularities noted are to be rectified without delay. Moreover, telework arrangements are expected to be revisited on an ongoing basis. Hours worked from home, as well as relative output, are to be duly monitored so as to avoid possible abuse and irregularities.

In the event that telework arrangements need to be changed due to work exigencies, such amendments are to be authorised and recorded in the respective officer's personal file.

Developments: *Fully Implemented*

From a review of two sampled officials working on a telework agreement, NAO observed that requests for the renewal of telework were adequately authorised and tasks performed duly monitored by Management.

Expenditure

Non-compliance with Public Procurement Regulations

Provision of legal services from three different lawyers was procured directly from the open market, without a public call for applications being issued or relevant approval from MFIN sought, even though these exceeded the applicable threshold of €6,000 (VAT excl.) allowing procurement direct from the open market. The entries of the Departmental Accounting System show that total payments made to these three service providers from VAT Department's Vote throughout 2015, amounted to €68,062, €16,522 and €7,618 respectively.

NAO could not determine the date when these legal advisors commenced providing their services with the VAT Department since contract agreements were not drawn up. Moreover, in such absence, the invoiced hourly fee could not be corroborated. A maximum amount payable to these service providers was also not established.

Local procurement regulations are to be followed in order to ensure transparency, accountability and to provide equal opportunity to all interested parties. It is also recommended that projections of total costs are made prior to engagement of any service provider.

In exceptional cases, where procurement above the established thresholds is acquired direct from the open market, the Department is to obtain the necessary approval from MFIN.

It is also important that procurement of services is invariably supported with a formal agreement.

Developments: *Insignificant Progress*

Before the issue of a tender to strengthen its own Legal Unit on 23 May 2018, CfR had been granted approval from MFIN to extend the service rendered by four lawyers for an additional 12 months. Their services were supported by formal agreements valid for a period of one year, entered into on 14 June 2018. Both direct order approval and the respective contracts included a fixed rate per hour and the maximum total possible outlay.

However, at the end of these contracts, the Department continued using the services of the same lawyers. Evidence of a further direct order approval from MFIN and extension agreements with the service providers was not provided for audit purposes.

Compliance Issue

Expenditure

Ongoing update on Inventory List

The inventory database forwarded to this Office for audit purposes was dated June 2012, thus indicating that such register was not updated since. Moreover, related room inventory lists were not provided for review.

As a result, this Office could not carry out proper testing of inventory, including a planned physical inspection of selected inventory items held at the VAT Department, in order to ascertain whether proper internal controls were exercised over inventory items.

All assets are to be accurately recorded in an inventory database. These are to be adequately identifiable and traced to the respective location. Room inventory lists are also to be updated to reflect the latest movements. This task is to be given due importance especially in view of Government's move towards accrual accounting.

Periodic physical verification of inventory items is also recommended, to ensure that inventory records truly reflect the description, quantity and location of fixed assets.

Developments: *Significant Progress*

During the follow-up audit, two CfR officials were carrying out an exercise to update the CfR's inventory list. As at the date of writing of this Report, this task was not yet finalised but given that CfR was one of the 10 pilot sites to implement accrual accounting, it was being given utmost priority.

Conclusion

This Office acknowledges the considerable efforts undertaken by the VAT Department to address the shortcomings highlighted in the 2015 Annual Audit Report. However, reviews carried out still revealed the need for the enhancement of a number of controls in specific areas, especially in light of the merger which took place with the Inland Revenue Department and the introduction of the accrual based accounting and Corporate Financial Management System.

2019-2020 (to date) Reports issued by NAO

NAO Work and Activities Report

April 2019	Annual Report and Financial Statements 2018 - Works and Activities

NAO Audit Reports

June 2019	Joint Audit: An Evaluation of the Community Work Scheme
July 2019	Cooperative Audit: Are adequate mechanisms in place for the designation and effective management of Marine Protected Areas (MPAs) within the Mediterranean Sea?
October 2019	Information Technology Audit: The Effective use of Tablets in State, Church and Independent Primary Schools
October 2019	Follow-up Reports by the National Audit Office 2019
November 2019	Report by the Auditor General on the Workings of Local Government 2018
November 2019	Performance Audit: An analysis of issues concerning the Cooperative Movement in Malta
December 2019	Report by the Auditor General on the Public Accounts 2018
December 2019	An investigation of contracts awarded by the Ministry for Home Affairs and National Security to Infinite Fusion Technologies Ltd
January 2020	Performance Audit: Community Care for Older Persons
February 2020	Performance Audit: Assessing the Public Transport Contract and Transport Malta's visibility on the service
March 2020	Information Technology Audit: ICT across Local Councils
March 2020	The disposal of the site formerly occupied by the Institute of Tourism Studies
April 2020	A review of the ethical framework guiding public employees
April 2020	Addendum Investigation: The Mater Dei Hospital Project
May 2020	Performance Audit: Tackling Child Abuse
May 2020	Annual Report and Financial Statements 2019