NAO
National Audit Office
MALTA

Report by the Auditor General

Public Accounts

2015

Annual Audit Report

Public Accounts 2015

Contents

	Pages
List of Abbreviations	**5**
Guide to using this Report	**8**
Executive Summary	**10**
Financial Audit Opinion	**13**
Opinion on the Financial Audit to the House of Representatives	14
Financial Report	**17**
Analysis of the Financial Report 2015	18
Compliance Audit Opinion	**81**
Opinion on the Compliance Audits to the House of Representatives	82
Office of the Prime Minister	**85**
Public Service Commission - Expenditure and Personal Emoluments	86
Ministry for Education and Employment	**93**
Free Childcare Scheme	94
Foundation for Educational Services	114
Ministry for Sustainable Development, the Environment and Climate Change	**125**
Agriculture Support Scheme	126
Ministry for Transport and Infrastructure	**133**
Ministry for Transport and Infrastructure - Expenditure	134
Transport Malta - *Ex-Gratia* Grant Scheme	141

Ministry for the Economy, Investment and Small Business **145**

Ministry for the Economy, Investment and Small Business - Expenditure 146

Commerce Department - Trading Licences Revenue 158

Ministry for Home Affairs and National Security **167**

Armed Forces of Malta - Expenditure 168

Correctional Services - Expenditure 180

Ministry for Finance **189**

VAT Department - Expenditure and Personal Emoluments 190

Department of Contracts - Expenditure and Personal Emoluments 203

Ministry for Energy and Health **215**

Sir Paul Boffa Hospital - Contractual and Professional Services 216

Ministry for the Family and Social Solidarity **235**

Department of Social Security - Invalidity Pensions 236

Elderly and Community Care Department - Personal Emoluments 242

Ministry for Justice, Culture and Local Government **251**

Judicial - Expenditure 252

Ministry for Tourism **271**

Institute of Tourism Studies - Personal Emoluments 272

Other Reports **285**

Arrears of Revenue 2015 286

Malta Police General Fund 328

Co-operatives Board - Audit for Financial Year 2015 342

List of Abbreviations

AAR	Annual Audit Report
AFM	Armed Forces of Malta
AG	Attorney General
AIN	Asset Identification Number
ARR	Arrears of Revenue Return
AVS	Attendance Verification System
BO	Budget Office
BTL	Below-the-Line
CBM	Central Bank of Malta
CCF	Corradino Correctional Facility
CCTV	Closed Circuit Television
CD	Commerce Department
CEO	Chief Executive Officer
CFMS	Corporate Financial Management System
CIS	Childcare Information System
CoJ	Courts of Justice
CoP	Commissioner of Police
CPSU	Central Procurement and Supplies Unit
DAS	Departmental Accounting System
DC	Department of Contracts
DG	Director General
DG ECFIN	Directorate General for Economic and Financial Affairs
DIER	Department of Industrial and Employment Relations
DMD	Debt Management Directorate
DO	Direct Order
DSS	Department of Social Security
DSWS	Department for Social Welfare Standards
EAMS	Euro Area Member States
EBU	Extra Budgetary Units
ECB	European Central Bank
ECCD	Elderly and Community Care Department
EDA	Extra Duty Allowance
EFSF	European Financial Stability Facility
EGRD	Eco-Gozo and Regional Development Directorate
EoM	End-of-Month
ESA	European System of Accounts
ESDM	European Sovereign Debt Markets
ESM	European Stability Mechanism
EU	European Union

FES	Foundation for Educational Services
FMS	Fleet Management System
FR	Financial Report
FRA	Fiscal Responsibility Act
FRN	Floating-Rate Notes
GCC	General Contracts Committee
GDP	Gross Domestic Product
GP	General Practitioner
GPD	Government Property Division
GPDMA	Government Borrowing and Public Debt Management Act
HR	Human Resources
IEG	International Energy Group Malta Ltd
IMF	International Monetary Fund
IMU	Information Management Unit
IP	Invalidity Pensions
IPSAS	International Public Sector Accounting Standards
IRD	Inland Revenue Department
ISSAI	International Standards of Supreme Audit Institutions
IT	Information Technology
ITS	Institute of Tourism Studies
Kg	Kilograms
KGRH	Karin Grech Rehabilitation Hospital
LA	Letter of Acceptance
LMS	Licensing Management System
LPO	Local Purchase Order
MCA	Malta Communications Authority
MCH	Mount Carmel Hospital
MDH	Mater Dei Hospital
ME	Malta Enterprise
MEDE	Ministry for Education and Employment
MEH	Ministry for Energy and Health
MEIB	Ministry for the Economy, Investment and Small Business
MEPA	Malta Environment and Planning Authority
MFAC	Malta Fiscal Advisory Council
MFEI	Ministry of Finance, the Economy and Investment
MFIN	Ministry for Finance
MFSS	Ministry for the Family and Social Solidarity
MGA	Malta Gaming Authority
MGI	Malta Government Investments Ltd
MGOZ	Ministry for Gozo
MGS	Malta Government Stocks
MITA	Malta Information Technology Agency
MJCL	Ministry for Justice, Culture and Local Government
MPA	Malta Police Association
MPF	Malta Police Force
MPGF	Malta Police General Fund

MSDC	Ministry for Social Dialogue, Consumer Affairs and Civil Liberties
MSDEC	Ministry for Sustainable Development, the Environment and Climate Change
MSE	Malta Stock Exchange
MTA	Malta Tourism Authority
MTI	Ministry for Transport and Infrastructure
NAO	National Audit Office
NLA	National Literacy Agency
NMIP	National Minimum Invalidity Pension
NSO	National Statistics Office
OECD	Organisation for Economic Co-operation and Development
ORC	Other Ranks' Canteen
PAC	Public Accounts Committee
PBS	Public Broadcasting Services
PDMAC	Public Debt Management Advisory Committee
PH	Public Holiday
PHC	Primary Health Care
PMMS	*Pitkali* Markets Management System
PPR	Public Procurement Regulations
PSC	Public Service Commission
PSMC	Public Service Management Code
PV	Payment Voucher
RAA	Risk Analysis Application
SA	Social Assistant
SABS	Social Assistance and Benefits System
SAMOC	Sir Anthony Mamo Oncology Centre
SEPA	Single Euro Payments Area
SL	Sick Leave
SMPPMA	Special Market Policy Programme for Maltese Agriculture
SPBH	Sir Paul Boffa Hospital
SSA	Social Security Act, 1987 (Cap. 318)
SVPR	St. Vincent de Paul Residence
TLA	Trading Licences Act, 2002 (Cap. 441)
TLR	Trading Licences Regulations, 2006 (S.L. 441.7)
TM	Transport Malta
TOIL	Time Off *In Lieu*
TVLU	Television Licensing Unit
VAT	Value Added Tax
VERA	Vehicle Registration and Administration System
VL	Vacation Leave
WAC	Weighted Average Coupon
WAM	Weighted Average Maturity
WSC	Water Services Corporation

Guide to using this Report

As a result of the various Financial and Compliance audits carried out by the National Audit Office (NAO), the Auditor General is hereby presenting separate Audit Opinions, on the financial and compliance audits respectively, to the House of Representatives.

In line with normal practice, we sought to spread our reviews across Government Ministries and Departments or across Government-wide activities in accordance with the NAO Annual Audit Programme drawn up from year to year. We have also attempted to make this Report as user friendly as possible and thus have tried to adopt common language, although this was not always possible due to the technicality of some of the issues raised.

This Report is presented by ministerial portfolios as featuring in the Government of Malta Financial Estimates 2015, each containing either the Ministry itself, or one or more Departments or Entities which were the subject of our review. Most audit reports under the ministerial portfolios have the following structure:

Background

Includes a brief description of the relevant activities, roles and operations of the respective Ministry, Department or Entity under review. Where applicable, it may also include new legislation governing such Entity.

Good Practice

Makes reference to any areas where NAO expressed satisfaction on full compliance, solely in respect of specific areas subjected to audit review, and where this was applicable.

Key Issues

Highlight any material findings or outcomes of our audit and any major developments impacting on the respective Ministry, Department or Entity.

Control Issues

Outline any shortcomings that came to our attention relating to the Ministry's or Department's internal control and internal checking mechanisms. These controls are expected to be in place so as to serve as an effective safeguard of public assets and resources.

Compliance Issues

Summarise instances whereby the relative Ministry, Department or Entity lacked compliance with effective legislation, standing General Financial Regulations and/or Circulars issued from time to time.

Recommendations

This is the most important part of our Report since ultimately our principal objective is to ensure that public resources are used in the best manner possible, in line with existing public finance management rules and regulations. Thus, it outlines our suggestions to the respective Ministries and Departments, to encourage them to address any weaknesses that came to our attention, as well as to consolidate and improve upon the management and proper discharge of public funds. In general, our recommendations are aimed at improving the internal control systems, addressing areas where there is lack of compliance with pertinent rules and regulations, and promoting good practice in the best interest of the taxpayer.

Management Comments

Seek to include, in as comprehensive a manner as possible, the Management's reaction to NAO's comments and action taken, or planned to be taken, so as to address in a timely manner the issues and any shortcomings identified.

Executive Summary

The **Financial Report** (page 17), incorporating Financial Statements and Accounts for the year 2015, was submitted by the Acting Accountant General in terms of the Financial Administration and Audit Act, 1962. Following examination, in terms of the Auditor General and National Audit Office Act, 1997, it is emphasised that:

- Letters of Comfort and Bank Guarantees reached almost €1.5 billion (against €1,403,270,738 in 2014). These may translate into dues by Government should the companies call upon the former to make good for their debts;

- substantial excess of actual over budgeted figures of various items of Expenditure was once again reported, these being similar to those reported last year. The reasons for these reoccurrences are being noted accordingly;

- a detailed statement showing outstanding Advances made to various Government Departments, Agencies and Organisations is being provided, including the Ministry for Finance's plans to have such amounts settled. Pending advances at year-end totalled €96 million, of which €69.4 million will continue to be repaid from public funds out of an annual budgetary provision;

- following the enactment of the Government Borrowing and Public Debt Management Act, a number of measures will be implemented by Treasury thereby introducing a risk management framework with supporting Information Technology systems, together with a code-of-conduct and conflict-of-interest rules for debt management officers. An overview of Government's strategy on public debt during 2015 is also outlined; and

- the Government has now adopted the strategy to prepare for the full implementation in Central Government of accrual accounting based on the International Public Sector Accounting Standards (IPSAS). The national standards shall be based on IPSAS, but may include minor amendments to reflect local needs and requirements. To date, six Draft IPSAS along with the relative User Guidelines, as adopted by the Maltese Government, have been published.

A review of expenditure of the **Public Service Commission**, revealed a number of weaknesses, mainly in inventory management. Shortcomings were also identified in the controls related to personal emoluments, in particular the upkeep of daily reports, including Sick Leave and Vacation Leave forms. (page 86)

An audit on the implementation of the recently introduced **Free Childcare Scheme** revealed lack of control exercised by the Ministry for Education and Employment over the service providers. The implementation of a fully automated attendance recording system beginning 2016 only translated into a new set of risks, which still resulted in significant undue payments. (page 94)

Attendance records maintained by the **Foundation for Educational Services** were considered unreliable. No evidence was obtained to confirm that payroll is adequately verified prior to processing and that overtime was approved before it is performed. (page 114)

The method of calculating fruit and vegetables subsidies falling under the **Agriculture Support Scheme** was inconsistent and not in line with information obtained by NAO during the audit. Since documentation forming the basis of subsidy payments was not retained by the *Pitkali* Markets, information had to be obtained directly from private middlemen referred to as *Pitkala*. However, not all the requested documentation was forthcoming and hence, audit testing was hindered in this respect. *Pitkali* Markets also failed to provide a satisfactory explanation on whether certain transactions featuring in the *Pitkala* documentation were supposed to be taken into consideration in determining the subsidy entitlement to beneficiaries. (page 126)

The main weaknesses identified during an expenditure audit at the **Ministry for Transport and Infrastructure**, consisted of lack of adherence to the Public Procurement Regulations with respect to Direct Orders obtained retroactively for a number of services. Testing also revealed shortcomings in the areas of inventory, travel and general-use vehicles. (page 134)

An audit was carried out on the ***Ex-Gratia*** **Grant Scheme** managed by **Transport Malta (TM)**, in relation to the settlement of VAT balances due to vehicle owners, who paid registration tax on vehicles registered and licensed for personal use, between 1 May and 31 December 2004. NAO satisfactorily noted that procedures in relation to the Scheme were correctly followed by TM, that all eligibility criteria were met by applicants and the correct amounts were disbursed accordingly. (page 141)

Payments to a service provider, who was initially engaged by the **Ministry for the Economy, Investment and Small Business** for four months, were effected beyond this period, resulting in the contract price being substantially exceeded. Lack of supporting documentation and approvals were also identified while testing expenditure incurred following Malta's participation in the Expo Milan 2015. Concerns relating to travel abroad were also noted. (page 146)

An audit on revenue from trade license fees collected by the **Commerce Department**, revealed that insufficient verification was carried out by the latter on information submitted by the applicant during the application stage. The Department relies on the information submitted by the respective applicant and this is considered correct unless proven otherwise. Other shortcomings were identified in the area of collection of arrears, mostly due to delayed action by the Department. (page 158)

Certain procurement not in line with the applicable regulations, as well as insufficient controls on reimbursements of medical expenses to various members of the Force, were the main issues emerging from an audit of the **Armed Forces of Malta**. (page 168)

Corradino Correctional Facility was undergoing substantial changes in the management set-up when the audit on **Correctional Services** was in progress, with the result that a number of queries remained pending. NAO identified a number of shortcomings, amongst other issues, relating to procurement and stock management. (page 180)

A review of expenditure and personal emoluments at the **VAT Department** revealed lack of internal controls within the Human Resources and Payroll function. Amongst others, non-compliance with Procurement Regulations in the provision of legal services was also reported upon. (page 190)

An audit of expenditure at the **Department of Contracts** revealed shortcomings related to Government-owned vehicles, inventory and travel. In particular, the lack of proper verification of invoices pertaining to lease of equipment, led to an additional VAT element being paid over and above the contracted rate. Testing also identified a number of weaknesses in respect of personal emoluments. (page 203)

An audit of the expenditure on Contractual and Professional Services at **Sir Paul Boffa Hospital** and Sir Anthony Mamo Oncology Centre revealed a lack of internal control synonymous to management by crisis. This included expenditure falling outside the scope of the contracts in force, necessary authority for procurement obtained retrospectively, if at all, and habitual contract extensions hindering fair competition. Resorting to procurement through negotiated procedure without prior publication of a European Union contract notice for a number of services of substantial value was also of concern. (page 216)

An audit on selected Invalidity Pensions falling under Contributory Benefits paid by the **Department of Social Security** revealed lack of sufficient internal controls with regards to periodical re-assessment of cases. Such weaknesses gave rise to a number of miscalculations. NAO feels it pertinent to note that in the case of female applicants, the Invalidity Pension is paid at 'single rate', irrespective of their marital status. (page 236)

An audit on the personal emoluments disbursed during 2015 by the **Elderly and Community Care Department** revealed that, amongst other shortcomings, two General Practitioners were overpaid around €27,000 in total. Another employee who was working on a reduced timetable, was also found to be employed with a separate Government Department. (page 242)

The procedure for the nomination of Court Experts was still not formalised. This was noted from an audit on the **Judicial** Expenditure for 2015. Furthermore, official standard rates were not yet established. The tariffs actually applied are taxed by the Court after negotiating the fee with the respective Court Expert. Various control weaknesses, mainly related to contract management were also encountered. (page 252)

Control over attendance records and related payments was insufficient at the **Institute of Tourism Studies**. Lack of transparency and non-compliance with standing regulations were also noted when purchasing contractual services. (page 272)

Similar to previous years, a review of the **Arrears of Revenue** Return for 2015, submitted by Ministries/ Departments in terms of Treasury Circular No. 6/2016, revealed several issues in the collectability of outstanding balances. Furthermore, in reply to a Public Accounts Committee specific request, reflected in Treasury Circular No. 12/2016, the year-end balances were further analysed as amounts statute-barred, pending Court action, recoverable by departmental action and amounts which are recoverable. (page 286)

Notwithstanding the legal obligation for the accounts of the **Malta Police General Fund** to be submitted to NAO for audit, the first time these were submitted was for the year under review. It transpired that at year-end the Fund was in a net deficit position and the current level of expenditure is considered unsustainable. The quarterly members' contributions were still being paid in cash and adequate records were not being maintained. (page 328)

A clean audit opinion was issued following the financial audit on the Financial Statements of the **Co-operatives Board** for the year ended 31 December 2015. (page 342)

Financial Audit Opinion

Opinion on the Financial Audit to the House of Representatives

Audit Mandate

As stipulated by Article 108(5) of the Constitution of Malta and para. 7 of the First Schedule of the Auditor General and National Audit Office Act, 1997, I am hereby reporting on the presentation of the statements and accounts prepared by the Acting Accountant General in fulfillment of the provisions of Article 67 of the Financial Administration and Audit Act, 1962, for the financial year under review.

I consider the primary users of the statements and accounts to be Parliament and the Public Accounts Committee.

Respective Responsibilities of the Accountant General and Accounting Officers

As determined by the Financial Administration and Audit Act, 1962, the onus for the proper discharge of financial administration and the preparation of statements and accounts rests with the Accountant General and the Accounting Officers. They are also responsible for institution and application of such internal controls as deemed necessary, to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and to ensure that the audited entities' operations are in accordance with the pertinent rules and regulations.

These officers are entrusted with the sound management of public funds. They are therefore to demonstrate transparency, accountability and integrity in their actions, and are to exercise good governance for the resources with which they are entrusted.

Auditor's Responsibilities

NAO's responsibility is to obtain reasonable, rather than absolute, assurance as to whether statements and accounts of Government Ministries and Departments, as well as of other entities that were subject to audit, are free from material misstatement. Thus, it is not a guarantee that an audit conducted in accordance with International Standards on Auditing (ISA) will always detect material misstatements, arising from fraud or error.

Basis for Opinion

We conducted our financial audit in accordance with the relevant ISAs, the applicable public sector perspective provisions, and in line with NAO's auditing practices.

An audit of financial statements involves performing procedures to enhance the degree of confidence that intended users have in the financial statements and accounts under review. The procedures selected depend on the auditors' judgement, which entails the assessment of risk, evaluation of internal controls, consideration of sensitivity of particular areas and other qualitative factors, as well as the assessment of materiality in terms of value, nature or context in which it occurs.

I have complied with independence requirements in accordance with the International Standard of Supreme Audit Institutions (ISSAI) 30 *Code of Ethics* and NAO *Code of Professional Conduct* and have fulfilled my ethical responsibilities in accordance with such codes. I have also adhered to avoidance of conflict of interest regulations as stipulated by Article 108(3c) of the Constitution of Malta and fulfilled the independence requirement in accordance with Article 108(12) of the aforementioned Constitution.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion, which only draws on conclusions upon areas that have been examined.

Opinion

Clean Opinion

In my opinion, the statements and accounts subjected to our audit were fairly presented in accordance with the stated accounting policies applicable to the public sector by the Government of Malta.

In terms of para. 5(ii) of the First Schedule of the Act, I am to report that, subject to instances referred to in the 'Analysis of the Financial Report', I received all the information and explanations required for the carrying out of my duties.

A separate audit opinion is being published dealing with the compliance aspect.

Charles Deguara
Auditor General
29th November 2016

Financial Report

Analysis of the Financial Report 2015

Introduction

Statements of the Consolidated Fund Account, showing the comparative positions in 2014 and 2015, and the receipts and payments of funds created by law, were laid on the Table of the House of Representatives during Sitting No. 373 on 6 April 2016, after being reconciled with Treasury Books by the Auditor General in accordance with Sub-para. 1(c) of the First Schedule of the Auditor General and National Audit Office (NAO) Act, 1997.

The Financial Report (FR) statements and accounts for year 2015 were submitted by the Accountant General in terms of Article 67 of the Financial Administration and Audit Act, 1962, and were examined in terms of Sub-para. 1(e) of the First Schedule of the Auditor General and NAO Act, 1997. The Report was laid on the Table of the House of Representatives during Sitting No. 412 on 4 July 2016.

Further details of Government financial operations can be found by making reference to both the Annual Financial Statements and FR for 2015.

Consolidated Fund Statement – 2015

As detailed in Article 102(1) of the Constitution of Malta, the Consolidated Fund incorporates all moneys raised or received by the Government of Malta, not being revenues or other moneys payable into some other fund, being a fund established by or under any law, for the time being in force in Malta for a specific purpose. All disbursements out of the Consolidated Fund are authorised by means of Appropriation Acts of Parliament, which include the Supplementary Appropriation Bill.

The House of Representatives approved the year 2015 Budget (Estimates) for an expenditure of €4,161,421,000, as authorised by Warrant No. 1 of 2015 issued on 23 December 2014, and a further €337,814,000 approved by Supplementary Estimates Warrant No. 2 of 2015 dated, 23 December 2015. Following the closure of the 2015 Accounts, actual expenditure amounted to €4,295,808,000, which resulted into an excess of expenditure of €146,602,000, as detailed in *Table 1*, leading to an end-of-year consolidated negative balance of €170,138,000.

Table 1: Consolidated Fund 2015

	Estimated (Original & Supplementary)		Actual	
	€'000's	€'000's	€'000's	€'000's
Opening Consolidated Balance as on 1 January 2015				(23,536)
Revenue				
Ordinary (incl. Grants)	3,555,049		3,634,798	
Capital	540,002	4,095,051	514,408	4,149,206
Expenditure				
Recurrent	(3,123,637)		(3,056,834)	
Public Debt Servicing	(649,323)		(616,434)	
Capital	(726,275)	(4,499,235)	(622,540)	(4,295,808)
Net Cash Flow		(404,184)		(146,602)
Closing Consolidated Balance as on 31 December 2015				**(170,138)**

(Source: FR 2015, page xv)

Table 2 hereafter shows the same end-of-year consolidated negative balance of €170,138,000 as in the preceding Table, highlighting figures relating to the Recurrent Deficit for 2015, amounting to €232,835,000, as well as the financing of present Foreign and Local Loans, totalling €387,001,000. This led to a total Public Sector Borrowing Requirement of €619,836,000, which was partly financed with the issue of new Local Loans, amounting to €473,235,000.

Table 2: Consolidated Fund 2015

	2015	
	€'000's	€'000's
Total Recurrent Revenue		3,634,798
Total Recurrent Expenditure	(3,289,165)	
Capital Expenditure	(578,469)	
Overall Expenditure		(3,867,634)
Recurrent Deficit		(232,835)
Financing (excluding New Loans)		
Foreign	(6,465)	
Local	(380,536)	
Total Financing		(387,001)
Public Sector Borrowing Requirement		(619,836)
Opening Consolidated Balance as on 1 January 2015	(23,536)	
Local Loans Issuance	473,235	
		449,698
Closing Consolidated Balance as on 31 December 2015		**(170,138)**

Figures in Statement may not add up due to rounding up.
(Source: FR 2015, page xvii)

Revenue

Details of Revenue collected during 2015, classified by heads and subheads, as compared with the Estimates, are shown in FR pages xxi to xxiii, including reasons for variation.

For the financial year 2015, it transpired that the Grand Total Variation in Revenue amounted to a favourable variance of €54,155,000, as compared to a positive difference of €113,130,000 in 2014.

Furthermore, this Office satisfactorily noted that the improvement registered in the previous financial year with respect to explanations given for variations in Revenue, was maintained for the financial year being reported upon. Some of the major recognised variances are listed in *Table 3*. This is followed with explanations for these variances, as provided by the Ministry for Finance (MFIN).

Table 3: Major Variances in Revenue for Financial Year 2015

Revenue	Budget Estimates	Actual	Variation
	€'000's	€'000's	€'000's
Tax Revenue			
Direct:			
Income Tax	1,112,000	1,184,628	72,628
Indirect:			
Excise Duties *of which* Petroleum	123,600	152,991	29,391
Licences, Taxes and Fines *of which* Duty on Documents	88,000	111,133	23,133
Non Tax Revenue			
Grants	263,322	176,165	(87,157)
Miscellaneous Receipts	6,500	38,237	31,737
Loans	500,000	473,235	(26,765)

(Source: FR 2015, pages xxi-xxiii)

Reasons for Variations

Direct Tax Revenue – Income Tax

The favourable variance arose mainly due to enhanced enforcement and an increase in employment rate, in line with economic growth. The actual increase exceeded the element factored in budget estimation.

Upon enquiry, the Inland Revenue Department has confirmed that according to the record classifications maintained by the Department, it is possible to extract data on the collection of revenue arrears based on performance for each full year. In fact, throughout 2015, enforcement action by the Department to collect arrears of income tax due to Government, retrieved almost €77 million in aggregate, whilst the difference to include the total outturn refers to collection for 2015 proper, as the Department continues to ensure that its revenue collection efforts for the current year continue to be pursued.

Indirect Tax Revenue – Excise Duties (Petroleum)

Similar to the previous year, there was an increase in receipts of accrued excise duty payments on petroleum from Enemalta p.l.c. of €29,391,000.

Licences, Taxes and Fines – Duty on Documents

The upsurge in revenue arising from Duty on Documents resulted from an increase in the number of contracts and the corresponding total values over 2014. The favourable variance of €23,133,000 outweighed the corresponding element factored into the original budget estimates.

Non Tax Revenue – Grants

The adverse variance of €87,157,000 in income arising from Grants emerged from reimbursements in respect of foreign financed projects under the 2007-2013 programme, including those originally budgeted for in 2015, which will continue to be received in 2016.

Similar to what was reported in last year's Report by the Auditor General – Public Accounts 2014[1], at time of compilation of the Financial Estimates, an equivalent amount to the pre-financing (European Union (EU) funds) provided under the respective Capital Votes also featured under Revenue, working on the assumption that the projected amounts should cater for reimbursements in respect of the previous year (in this case, 2014) and part of the current year (in this case, 2015). However the amount of reimbursements actually received by year-end will depend on the rate of progress registered on project implementation, as well as the rate at which the amounts are certified, claims for reimbursement are made to the EU Commission, and reimbursed by the said Commission. Budget Office (BO) noted that any funds not received in the current year will be accrued for in the accrual-based statements forwarded to the EU Commission according to the European System of Accounts (ESA) methodology, hence leaving a neutral effect on the budget deficit target for the respective year being reported upon.

Miscellaneous Receipts

The favourable variance in income collected from miscellaneous receipts of €31,737,000, originated from due accounting treatment according to the respective projects' financing sources, as well as transfers from below-the-line accounts.

The main part of this variance derived from the recoupment, through EU funding, on eligible projects carried out in previous years, expenditure which was originally met out of national funds. In order to reflect such transactions in Government's accounts through the Departmental Accounting System (DAS)

[1] Thereafter referred to as Annual Audit Report (AAR).

and enable eventual claims for reimbursement to be submitted to the European Commission, BO explained that corresponding budgetary provisions were made available on the expenditure side of the budget, to be subsequently transferred to Miscellaneous Receipts (Revenue) by means of Transfer Schedules. Once the expenditure was eventually reimbursed through EU funds at a later stage, such reimbursements were then credited to the corresponding EU funds Revenue Item in the Consolidated Fund.

To a lesser extent, another reason for the variance under this item was the result of MFIN's efforts to close-off existing below-the-line accounts in the Treasury Clearance Fund, following the necessary verifications that the balances held therein were not required to cover any firm commitments. As a result of such initiatives, the unrequired balances were transferred to Revenue in the Consolidated Fund. To this effect, NAO was provided with supporting evidence that verifications were carried out prior to effecting transfers to Revenue, in order to be compliant with Article 18 of the Financial Administration and Audit Act.

Loans

The negative variance of €26,765,000 emerged from the rejection on non-compliant applications in the first issuance of the year (oversubscribed by retail investors), which could only be identified after the allocation policy was announced. In addition, contributions to the Special Malta Government Stocks (MGS) Sinking Fund[2] were less than estimated, since according to the Debt Management Directorate (DMD) within Treasury, during the year 2015, the Public Debt Management Advisory Committee (PDMAC) deemed it necessary to make a contribution in the local secondary securities market of only €25 million out of a total maximum budget of €50 million.

The trends and drivers which determine the level of support for market liquidity required through the buying of MGS by the Special MGS Sinking Fund is determined primarily by the investors' behaviour and the willingness to absorb demand and supply imbalances. It is to be noted that factors such as the current low-yield environment, along with unusually accommodative monetary policy, may be influencing the underlying trends in the current investors' behaviour.

Expenditure

The appropriations for expenditure during 2015, authorised by the issue of MFIN Warrant Nos. 1 and 2, were made under the following Statutes:

		€
a.	Appropriation Act	2,876,347,333
b.	In terms of Special Laws	1,619,719,000
c.	In terms of the Constitution	3,168,667

Analysis of Appropriations

a. *Appropriation Act*

	€
Appropriated by Act XXXIX of 2014 (Original Budget)	2,539,983,333
Appropriated by Act XLII of 2015 (Supplementary)	336,364,000

[2] In 2014, a Special Sinking Fund was established for the purpose of the repurchase of loans raised under Article 26(2) of the Local Loans (Registered Stock and Securities) Ordinance, in an effort to enhance the market liquidity, which in turn contributes towards a broader effort to develop the domestic financial market, and at the same time reap some return from the investment on MGS.

b. *Special Laws*

The following amounts (including Supplementary Estimates as detailed in Warrant No. 2 of 2015) were appropriated in terms of the various laws as indicated:

Table 4: Amounts Permanently Appropriated in terms of the various Laws

Description	2015	2014
	€	€
Expenses of the Electoral Commission – General Elections Act (Cap. 354)	370,000	350,000
Expenses of the Broadcasting Authority – Broadcasting Act, 1992 (Act XII of 1991 – Cap. 350)	583,000	620,000
Expenses under Re-letting of Urban Property Ordinance (Cap. 69) and Agriculture Leases (Re-letting) (Cap. 199)	81,000	81,000
Land Acquisition (Public Purposes) Ordinance (Cap. 88)	115,000	115,000
Social Security Act, 1987 (Act X of 1987 – Cap. 318)	869,600,000	859,560,000
Pensions Ordinance (Cap. 93)	88,380,000	88,400,000
Expenses of the Office of the Ombudsman (Cap. 385)	1,140,000	1,437,000
Expenses of the Permanent Commission Against Corruption (Act XXII of 1988 – Cap. 326)	40,000	40,000
Interest plus contribution to the Sinking Funds in respect of Local Government Stock – Registered Stock and Security Ordinance 1959 (Cap. 161)	636,089,033	790,514,663
Interest plus contribution to the Sinking Funds in respect of Foreign Loans (Cap. 213)	8,281,967	8,770,269
Malta Arbitration Centre (Act II of 1996 – Cap. 387)	67,000	67,000
Expenses of the NAO (Act XVII of 1997 – Cap. 396)	2,700,000	2,600,000
Refunds under Value Added Tax/Customs & Excise Tax Acts	1,388,000	1,388,000
Widows' and Orphans' Pensions Act (Cap. 58)	500,000	525,000
Personal Injuries (Emergency Provisions) Ordinance (Cap. 111)	50,000	45,000
Members of Parliament (Retiring Allowances) (Act XVII of 1966), Members of Parliament Pensions Act (Act XXVI of 1979) as amended by Act XIII of 1981 and Act VII of 1989 (Cap. 280)	1,500,000	1,480,000
Short Term Borrowing – Treasury Bills Act (Cap. 133)	2,907,000	4,700,068
€56,378,732 Interest payable on ex-Malta Drydocks/ Malta Shipbuilding Co. Ltd Loans (Act XV of 2003)	2,247,000	2,247,000
Lease of Parliament Building – Budget Measures Implementation (Act V of 2012)	3,680,000	1,825,000
Totals	**1,619,719,000**	**1,764,765,000**

Following queries forwarded to BO, the following explanations were provided to explain major increases of actual expenditure over the previous year:

Social Security Act, 1987 (Act X of 1987 – Cap. 318)

The increase of €10,040,000 in 2015 over the previous year's budget was due to rises in the number of beneficiaries, as well as the cost of living element by which social security benefits are indexed. These increases were budgeted for and the total vote provisions were not exceeded.

Lease of Parliament Building – Budget Measures Implementation (Act V of 2012)

A higher budgetary allocation over the previous year, totalling €1,855,000, was made available since the amounts were provided according to the month in which, at budget preparation time, it was estimated that the Parliament building would be completed. This increase was budgeted for and the total vote provision was not exceeded.

c. *In terms of the Constitution*

In terms of Article 107(2) of the Constitution, the following amounts were permanently appropriated in respect of:

	€
The President of Malta	76,968
The Attorney General	76,834
Judges and Magistrates	2,925,794
The Public Service Commission	89,071
	3,168,667

Budgetary Procedure for 2015

Following NAO query, BO provided a detailed description of the 2015 budgetary process' main elements, as outlined below.

The top-down[3] approach for budgetary allocations has been in use for the past years and was also adopted in 2015, which process commenced through MFIN Circular No. 1/2014 – '2015 Financial Plans'. By means of this Circular, all Ministries, Departments and Entities, were requested to submit their respective expected revenue, as well as recurrent and capital expenditure projections. Ministries were asked to look specifically into the published projections for 2015 (apart from 2016 - 2017), ensuring that in the Business and Financial Plans to be submitted, revenue does not fall below, and expenditure does not exceed, the published projections on a Ministry basis.

Given that Government's policy remained one of ensuring a further reduction in the yearly fiscal deficit, Ministries were encouraged to strive towards expenditure containment and the enhancement of revenue generation.

[3] This means that MFIN sets the overall expenditure ceiling and sub-ceilings, and delegates detailed resource allocation decisions to line Ministries.

Indications for additional funding, if any, were to be kept at an absolute minimum, limited only to those instances where non-provision of funds, above the parameters set through the said Circular, would adversely impact the core workings of the respective Ministries and Departments.

The plans to be compiled were to be based on the most recently announced medium-term fiscal strategy. Dedicated statements showing the three-year revenue and expenditure projections for 2015 to 2017, at Ministry level, had been integrated in the 2015 Financial Estimates publication. These projections were to serve as the parameters within which the business and financial planning exercise for 2016 and the years that follow, was to be undertaken.

Following assessment of the financial plans received from all line Ministries, MFIN went on to assess the requests submitted and compare against its internal projections for the years 2015 to 2017, which included considerations on revenue and expenditure trends, known commitments and performance for the current year (which at that point was 2014).

Following assessment, a first round of bilateral meetings was held between MFIN's Permanent Secretary and each Ministry's respective Permanent Secretary, together with key officials from the Budget Affairs Division, as well as from the line Ministries and their respective entities. The contents of the financial plans submitted were discussed during these meetings and any points requiring further clarifications were handled accordingly.

A second round of bilateral meetings was then held between the Minister for Finance and the Minister responsible for the line Ministries, together with key officials as necessary. The main purpose of these meetings was to address any issues which required further consideration, as well as to discuss new initiatives which Government was planning to undertake. Together with any budget measures being contemplated, the revenue and expenditure projections were adjusted to incorporate due changes as deemed appropriate, keeping in view, however, the fiscal framework targeting a reduction of 1.6% in Government's deficit for 2015. Eventually, the projections comprised the 2015 Financial Estimates, which were presented to Parliament.

Excess of Expenditure over Estimates

The Supplementary Estimates contributed in part to the overall fiscal outturn for 2015, with the other contributing element being revenue performance. *Table 5* portrays those votes whose expenditure exceeded budgeted figures, by well over €1 million. In particular, five Ministries reported this excess in both their Capital and Recurrent Votes.

Table 5: Excess of Expenditure over Original Budget by Vote

Vote	Original Budget 2015	Actual 2015	Variation Actual 2015/ Original Budget 2015
	€	€	€
Recurrent Expenditure			
Vote 5: Office of the Prime Minister	24,896,000	32,626,469	7,730,469
Vote 9: Electoral Office	5,193,000	7,795,468	2,602,468
Vote 10: Government Property Division	4,932,000	8,912,185	3,980,185
Vote 11: Ministry for European Affairs and Implementation of the Electoral Manifesto	12,977,000	15,214,813	2,237,813
Vote 13: Ministry for Education and Employment	212,973,000	228,029,465	15,056,465
Vote 14: Education	196,138,000	204,430,001	8,292,001
Vote 15: Ministry for Sustainable Development, the Environment and Climate Change	48,865,000	53,794,838	4,929,838
Vote 16: Ministry for Transport and Infrastructure	82,802,000	84,548,963	1,746,963
Vote 23: Armed Forces of Malta	42,315,000	44,203,393	1,888,393
Vote 24: Police	54,233,000	57,147,737	2,914,737
Vote 25: Correctional Services	9,322,000	10,864,122	1,542,122
Vote 28: Ministry for Finance	112,207,000	127,037,365	14,830,365
Vote 30: Pensions	90,705,000	91,967,163	1,262,163
Vote 37: Ministry for Energy and Health	63,148,000	65,811,925	2,663,925
Vote 38: Health	414,015,000	449,484,914	35,469,914
Vote 43: Elderly and Community Care	75,767,000	84,921,553	9,154,553
Vote 47: Ministry for Tourism	48,231,000	53,604,771	5,373,771
Capital Expenditure			
Vote II: Office of the Prime Minister	13,302,000	14,893,823	1,591,823
Vote V: Ministry for Education and Employment	67,584,000	83,484,100	15,900,100
Vote VI: Ministry for Sustainable Development, the Environment and Climate Change	77,667,000	95,467,205	17,800,205
Vote IX: Ministry for Social Dialogue, Consumer Affairs and Civil Liberties	1,922,000	3,138,187	1,216,187
Vote X: Ministry for the Economy, Investment and Small Business	43,449,000	60,422,134	16,973,134
Vote XI: Ministry for Home Affairs and National Security	21,422,000	23,861,199	2,439,199
Vote XIII: Ministry for Energy and Health	86,560,000	108,104,090	21,544,090
Vote XV: Ministry for Justice, Culture and Local Government	19,570,000	23,856,151	4,286,151
Vote XVI: Ministry for Tourism	1,443,000	4,268,809	2,825,809
Totals	**1,831,638,000**	**2,037,890,843**	**206,252,843**

(Source: FR 2015, pages xi - xiii, 43 - 176)

Excess expenditure over original budgeted figures exceeding €1 million occurred in the Line Items shown in *Table 6*. It is interesting to note that same Line Items experienced a similar excess of expenditure during 2014, as portrayed in the same Table. In the majority of cases noted, the 2015 excess was even higher than the one reported in 2014.

Table 6: Excess of Expenditure over Original Budget/Revised Estimates by Item

Vote, Item	Original Budget 2015	Revised Estimates 2015[4]	Actual 2015	Variation Actual 2015/ Revised Estimates 2015	Variation Actual 2015/ Original Budget 2015	Variation Actual 2014/ Original Budget 2014
	€	€	€	€	€	€
Vote 5: Office of the Prime Minister						
Item 5365: CHOGM 2015	4,500,000	6,800,000	6,570,281	(229,719)	2,070,281	1,971,256
Vote 9: Electoral Office						
Item 5219: Electoral Commission Activities	3,500,000	6,300,000	6,134,175	(165,825)	2,634,175	2,350,892
Vote 10: Government Property Division						
Item 5672: Dues to Malita Investments p.l.c.	-	3,650,000	3,650,000	-	3,650,000	1,640,200
Vote 13: Ministry for Education and Employment						
Item 5024: Church Schools	53,000,000	60,500,000	60,249,449	(250,551)	7,249,449	5,630,326
Item 5364: Students' Maintenance Grants	24,100,000	25,900,000	25,498,202	(401,798)	1,398,202	4,210,225
Item 5503: Learning Support Assistants in Private Schools	800,000	2,467,000	2,481,682	14,682	1,681,682	1,234,330
Item 5703: Child Care for All	8,000,000	11,400,000	11,150,496	(249,504)	3,150,496	1,516,779

[4] Revised estimates are made up of the Original Budget 2015 and the Supplementary Estimates for the same Item.

Table 6: Excess of Expenditure over Original Budget/Revised Estimates by Item *cont./*

Vote, Item	Original Budget 2015	Revised Estimates 2015[2]	Actual 2015	Variation Actual 2015/ Revised Estimates 2015	Variation Actual 2015/ Original Budget 2015	Variation Actual 2014/ Original Budget 2014
	€	€	€	€	€	€
Vote 14: Education						
Item 12: Salaries and Wages	150,000,000	156,000,000	155,871,709	(128,291)	5,871,709	7,691,219
Item 27: Transport	6,250,000	8,250,000	7,819,901	(430,099)	1,569,901	1,379,212
Vote 38: Health						
Item 12: Salaries and Wages	125,534,000	135,934,000	132,249,325	(3,684,675)	6,715,325	6,768,325
Item 16: Allowances	59,868,000	67,168,000	68,464,736	1,296,736	8,596,736	9,756,375
Item 17: Overtime	4,972,000	7,272,000	6,727,448	(544,552)	1,755,448	2,865,238
Item 5400: Medicines and Surgical Materials	84,000,000	90,000,000	92,015,090	2,015,090	8,015,090	9,409,144
Item 6029: Mental Health Services	27,000,000	29,600,000	29,415,657	(184,343)	2,415,657	1,508,157
Vote 41: Social Security Benefits						
Item 5140: Invalidity Pensions	23,000,000	23,000,000	24,676,865	1,676,865	1,676,865	2,346,396
Item 5148: Disability Pensions/Allowance	13,000,000	13,000,000	15,329,205	2,329,205	2,329,205	1,446,909
Vote 43: Elderly and Community Care						
Item 16: Allowances	8,200,000	9,500,000	9,461,748	(38,252)	1,261,748	2,333,514
Item 17: Overtime	1,300,000	3,000,000	2,851,669	(148,331)	1,551,669	1,485,793
Item 30: Contractual Services	10,000,000	12,400,000	12,563,805	163,805	2,563,805	3,498,944
Item 5029: Residential Care in Private Homes	6,500,000	8,800,000	8,498,053	(301,947)	1,998,053	2,772,387

Table 6: Excess of Expenditure over Original Budget/Revised Estimates by Item *cont./*

Vote, Item	Original Budget 2015	Revised Estimates 2015[2]	Actual 2015	Variation Actual 2015/ Revised Estimates 2015	Variation Actual 2015/ Original Budget 2015	Variation Actual 2014/ Original Budget 2014
	€	€	€	€	€	€
Capital Vote III: Ministry for European Affairs and Implementation of the Electoral Manifesto						
Item 7805: External Borders Fund	13,030,000	20,330,000	20,012,922	(317,078)	6,982,922	1,440,680
Capital Vote V: Ministry for Education and Employment						
Item 7801: EU Structural Funds 2007 – 2013	33,620,000	46,120,000	44,233,517	(1,886,483)	10,613,517	9,803,788
Item 7901: EU Structural Funds 2007 – 2013	5,285,000	12,285,000	10,871,090	(1,413,910)	5,586,090	4,925,149
Capital Vote VII: Ministry for Transport and Infrastructure						
Item 7266: Grand Harbour Regeneration Corporation	800,000	4,300,000	5,020,550	720,550	4,220,550	1,312,847
Item 7283: Road works relating to EU Funding	1,792,000	5,592,000	5,791,777	199,777	3,999,777	4,590,587
Capital Vote XIII: Ministry for Energy and Health						
Item 7801: EU Structural Funds 2007 – 2013	37,090,000	39,690,000	43,431,244	3,741,244	6,341,244	1,859,168
Item 7901: EU Structural Funds 2007 – 2013	18,978,000	23,478,000	22,754,228	(723,772)	3,776,228	1,304,696

Table 6: Excess of Expenditure over Original Budget/Revised Estimates by Item *cont./*

Vote, Item	Original Budget 2015	Revised Estimates 2015[2]	Actual 2015	Variation Actual 2015/ Revised Estimates 2015	Variation Actual 2015/ Original Budget 2015	Variation Actual 2014/ Original Budget 2014
	€	€	€	€	€	€
Capital Vote XVI: Ministry for Tourism Item 7801: EU Structural Funds 2007 – 2013	80,000	4,180,000	3,209,642	(970,358)	3,129,642	1,887,696

The following reasons as published in the Supplementary Estimates of Expenditure 2015 and/or further submissions from BO following NAO queries, were forwarded in respect of the repeated excess expenditure over original budgeted figures of the above-quoted Line Items.

Vote 5: Office of the Prime Minister - Item 5365: CHOGM 2015

Following a claim received for an additional amount of €2.3 million from OPM, a reconsideration of the original payment schedule was deemed necessary by BO, due to expected claims, which needed to be settled in 2015, instead of early 2016 as originally planned. Therefore, budgetary adjustment by means of the Supplementary Estimates, arose due to payment timing issues. NAO was informed by BO that the approved overall budget for this event was maintained.

Vote 9: Electoral Office - Item 5219: Electoral Commission Activities

Supplementary budget of €2.8 million was required in connection with the 'Spring Hunting' referendum.

Vote 10: Government Property Division - Item 5672: Dues to Malita Investments p.l.c.

Although an original budget was not allocated, a supplementary amount of €3.65 million was provided for payments due out of this Recurrent Vote until the certification processes of the Parliament building are finalised. An equivalent sum remained unspent under the House of Representatives Recurrent Vote.

Vote 38: Health - Item 5400: Medical and Surgical Materials

Following discussions held with the Central Procurement and Supplies Unit within the Ministry responsible for Health, it transpired that for reasons of service delivery, so as not to increase the amount of creditors, as well as to manage stock flows and prevent issues of out-of-stock supplies, it was necessary to augment the approved budgetary provision with total supplementary funds of €6 million.

Vote 38: Health - Item 6029: Mental Health Services

It became necessary for BO to supplement the approved budgetary provision with respect to the Mental Health Services, without impinging on the general fiscal parameters set for the year, after having assessed the documentation and accounts submitted by Mental Health Services with respect to its financial position. It was deemed appropriate that, in order to respond to demands arising in this sector as the year progressed, an additional allocation of €2.6 million was made, to enable the Mental Health Services to meet its current obligations.

Vote 41: Social Security Benefits - Item 5140: Invalidity Pensions; and Item 5148: Disability Pensions/Allowance

The need for Supplementary Estimates did not arise during 2015, since the expenditure under the total approved vote budgetary provision allocated against the several line items, comprising Recurrent Vote 41 'Social Security Benefits', was not exceeded by the end-of-year reported upon. The shortfalls of €1,676,865 and €2,329,205 under Items 5140 'Invalidity Pensions' and 5148 'Disability Pensions/Allowance' respectively, were therefore compensated by savings registered under other items within the same Recurrent Vote, in terms of the Financial Administration and Audit Act.

Vote 43: Elderly and Community Care - Item 30: Contractual Services

As explained by BO, a further sum of €2.4 million was essential to cover services rendered, including a change in contractual rates of precarious work, particularly in respect of cleaning services and carers, outsourcing of catering services, as well as to cater for a reduction in the credit period of outstanding invoices.

Vote 43: Elderly and Community Care - Item 5029: Residential Care in Private Homes

In order to address the need to acquire additional beds and cater for the demand in this sector, an additional amount of €2.3 million was allocated.

Capital Vote V: Ministry for Education and Employment; Capital Vote XIII: Ministry for Energy and Health; Capital Vote XVI: Ministry for Tourism – Items 7801 and 7901: EU Structural Funds 2007-2013; and Capital Vote III: Ministry for European Affairs and Implementation of the Electoral Manifesto - Item 7805: External Borders Fund

The aggregate of €19.5 million were necessary as Supplementary Estimates for the Ministry for Education and Employment (MEDE) to finance payments on projects, which are co-financed by EU, in terms of its funding programme, based on estimates made available.

In order to cover commitments on various projects, a total supplementary figure of €7.1 million was contributed to the Ministry for Energy and Health (MEH).

Additional funds of €4.1 million were estimated to be required by the Ministry for Tourism to cover commitments on various projects, which part was financed by EU.

Similarly, a further amount of €7.3 million was essential to cover projects by the Ministry for European Affairs and Implementation of the Electoral Manifesto, being the EU financing element.

As explained in 2014 AAR, at time of compilation of the Financial Estimates during the budget preparatory process, all Managing Authorities of EU funds were requested to make available their submissions on the budgetary allocations that were expected to be required to cover planned expenditure for the following year.

Utilisation of the funds provided depends on project gestation and implementation periods. In this case, projects advanced at a steadier pace than as was anticipated at budget preparation time, thus the need to provide supplementary funding arose. In such way, risk on eventual loss of EU funds during such year was minimised. Moreover, it is to be noted that expenditure incurred out of EU funded items is subsequently reimbursed by EU in response to claims made by the Certifying Authorities.

Capital Vote VII: Ministry for Transport and Infrastructure - Item 7266: Grand Harbour Regeneration Corporation

An additional €3.5 million were provided to settle financial obligations becoming due, since as the year progressed it transpired that supplementary funding was required for the Grand Harbour Regeneration Corporation to be in a position to finance its project commitments. Claims for supplementary funding were favourably considered in a manner which did not adversely impact the published deficit target for the year, as stated by BO.

Assets and Liabilities

Article 67(j) of the Financial Administration and Audit Act, 1962, states that the Accountant General shall prepare "... *a statement of assets and liabilities of the Government at the end of the financial year* ...".

This Statement may be looked upon as a statement of end-of-year balances in the Treasury books, which result from cash transactions accounted for in the Public Account during the year. Given that Central Government accounts are still cash-based, not all Government's assets and liabilities are included in this statement as would be under an accruals-based accounting system.

Assets

Table 7 represents the Statement of Assets.

Table 7: Statement of Assets

	2015	2014
	€'000's	€'000's
Public Credit		
Shareholding	838,545	721,762
Other Investments[5]	113,569	113,568
Loans	67,729	108,145
	1,019,844	943,476
Investments held on behalf of		
Sinking Funds (Local)	150,759	122,878
Sinking Funds (Foreign)	21,300	25,531
Trust Funds	1,578	1,650
	173,637	150,060
Advances		
Advances	96,037	111,173
Bank and Cash		
Banks[6]	6,549	6,059
Central Bank of Malta – Public Account	94,484	92,976
	101,033	99,035
Total Assets	**1,390,551**	**1,303,743**

Figures in Statement may not add up due to rounding up.
(Source: FR 2015, page 195)

[5] This includes a revised balance of Euro Coins which supersedes the figure published in the Annual Financial Statements for 2015, as explained further under 'Public Credit – Other Investments' in this Report.
[6] Consists of bank accounts held by foreign Embassies/Commissions and the National Lottery Good Causes Fund.

Public Credit – Shareholding

As at 31 December 2015, the value of direct investments stood at €838,545,381 (€721,762,235 in 2014). This was made up of €516,046,832 unlisted shares valued at purchase cost, and €322,498,549 listed shares valued at market price as at year-end.

The following were the major changes in investments during the year:

New Investment

International Energy Group (IEG) Malta Ltd

The Energy Ministry replaced Malta Enterprise as shareholder in IEG Malta Ltd, with 100,000 Ordinary B Shares having a nominal value of USD 100,000. Documentation reported that the implementation of this initiative was aligned to Malta's strategy to become an important Mediterranean energy-trading hub between Europe and Asia.

By way of background information, IEG Malta Ltd was formed in May 2015 between the Malta Enterprise and New Silkroutes Group (Europe) Ltd. A board resolution was passed to facilitate the transfer of the 10% stake held by Malta Enterprise in IEG Malta Ltd to MEH, by means of a Share Transfer Agreement dated 5 November 2015.

Increase in Paid-up Share Capital

Air Malta p.l.c.

In accordance with the Subscription Agreement dated 6 October 2012 entered into between the Government and Air Malta p.l.c., the Government subscribed to a further 52 million Ordinary Shares, being its *pro rata* share of the issue by the company of 53,088,957 shares of €1, offered to all shareholders of Air Malta p.l.c. By end-of-year 2015, Government paid the cash sum of €47,216,000, equivalent to 90.8% of the nominal value.

Moreover, in connection with the 78 million shares allotted to Government in 2012 by virtue of the same Agreement, amounts due for 2015 in respect of the unpaid part of the aforementioned Ordinary Shares, led to an increase of €25.8 million in the paid-up share capital.

Government is expected to contribute the full 100% of the nominal value of Ordinary Shares by 15 January 2016. Government's shareholding in Air Malta p.l.c. as at 31 December 2015, stood at 99.98%.

Increases in Investments

European Investment Bank

Following the decision of the Board of Governors of the European Investment Bank taken in 2012 to increase its capital by an aggregate paid-in amount of €10 billion, the share of the capital increase to be paid by Malta amounted to €4,235,500. During 2015, a third instalment of €1,058,875 was paid, representing the full value of Malta's contribution to the capital increase, thus bringing Government's total paid-in capital by the end of the year to €9,156,975. Moreover, as *per* confirmation dated 15 March 2016, the nominal value of Malta's share in the subscribed capital of the European Investment Bank as at end-of-year 2015 stood at €102,665,000.

Bank of Valletta p.l.c.

By means of Company Announcement dated 17 December 2014, Bank of Valletta p.l.c. capitalised the amount of €30 million from the company's reserves for the purpose of a bonus issue of an equal amount of fully paid Ordinary Shares with a nominal value of €1 *per* share.

Based on the allocation ratio of one bonus share for every 11 shares held, a total amount of 7,569,035 Ordinary Shares were allotted to Government. To this effect, the nominal value of Government's investment as at 31 December 2015 amounted to €90,828,421. Moreover, shares in Bank of Valletta p.l.c. experienced a rise in market value during the year under review, in contrast with the considerable drop noted during 2014.

Termination of Investment

Malta Public Transport Services Ltd

Following an expression of interest issued by the Authority for Public Transport in Malta on 27 January 2014, Malta Lines Ltd (the purchaser) submitted an offer in response to the said expression of interest notice, opting to acquire the company and operate under the concession subject to certain amendments. Malta Public Transport Services Ltd and Malta Government Investments (MGI) Ltd (the vendors) agreed to sell the total issued share capital, following an agreement signed on 20 December 2014. Treasury confirmed that the investment cost of €999,999 was repaid to Government during 2015.

War Stock 3.5%

On 9 March 2015, Her Majesty Treasury announced the redemption of the 3.5% War Stock, as published in the London Gazette early in December 2014. As a registered holder, Malta Government was entitled to the redemption proceeds and the final interest payment due. Holdings of the Stock were redeemed at *par* (£100 for every £100 nominal held) and the final interest payment at the rate of £0.94 *per* £100 nominal held. Malta Treasury confirmed that the total value of investment of £75,175, equivalent to €104,617, was repaid to Government during 2015.

Movements in Values of Existing Investments

During 2015, the cost of investments in:

a. Council of Europe Development Bank;
b. International Bank for Reconstruction and Development;
c. Malta Freeport Corporation Ltd;
d. Mediterranean Offshore Bunkering Co. Ltd; and
e. Multilateral Investment Guarantee Agency,

increased by €1,267,239 due to favourable changes in United States Dollar exchange rate.

Public Credit – Other Investments

Investment in Industry

A Schedule of Investments submitted by MGI to the Accountant General showed that the total cost of investment in 45 companies amounted to €16,328,354 as at 31 December 2015.

MGI estimated that the net book value of these investments amounted to €14,075,400, after an accumulated provisional loss of €2,252,954. Further details are provided in *Table 8*.

Table 8: Investments through Malta Government Investments Ltd

Investment Type	No. of Companies	Cost	Provisional Loss	Net Book Value
		€	€	€
Subsidiary Companies	27	14,871,477	1,146,502	13,724,975
Associated Companies	2	1,455,858	1,106,452	349,406
Other Companies of Minority Interest	16	1,019	-	1,019

The Schedule includes eight companies that were undergoing liquidation procedures, and another two companies that were struck off during the year under review.

At the end of 2015, the total of investment in industry as reported by Treasury amounted to €16,350,729 as against €16,349,729 on 31 December 2014, an increase of €1,000 over the previous year. Such movement was due to a new investment in Core Malta Education Solutions Limited (a subsidiary company).

It is to be noted that indirect investments at year-end, as reported by Treasury, do not tally with MGI aggregate balances reported. The difference of €22,375 between Treasury's and MGI's records emanates mostly from an investment of €22,369 in Topwear Ltd, that is not reported on MGI records, this being an investment made from Government funds by the former Malta Development Corporation.

Movements in 'Other Investments'

Euro Coins

During 2015, CBM made Euro Coin issues on behalf of Treasury totalling €8,113,383, bringing the total amount of Euro Coins in circulation as at 31 December 2015 to €68,510,383. This differs from the figure of €67,860,000 published in the Annual Financial Statements for 2015, on the basis that, "... *CBM explained that it was an accounting error by the MCDC, the Malta Coins Distribution Centre* ..." and that "... *this is a very rare occurrence*". To this effect, CBM confirmed to Treasury that "*The figure was revised due to previous years' circulation coins (in sets) sold by MCDC but not accounted for as circulation coins issued*". NAO acknowledges Treasury's comment that "... *this was an extraordinary circumstance and not within Treasury's contro*l".

Dividend/Profit Received

Central Bank of Malta

During the year under review, a total of €48 million was received in six tranches from Central Bank of Malta (CBM), consisting of 2014 net profits due to Government.

Malta Financial Services Authority – Capital Fund

Total surplus funds amounting to €7 million were received in one tranche from the Malta Financial Services Authority during 2015, in terms of Article 26(3) of the Malta Financial Services Act (Cap. 330).

Inspection of Securities/Investments - Government Securities Board

The purpose of the Government Securities Board is to verify and certify the List of Securities held by the Government at year-end, with the relative Stock Certificates held by Treasury. Representatives from NAO attend the annual meeting in an observer capacity.

The Board is made up of three members, namely the Chairperson, this being MFIN Permanent Secretary, a Malta Investments Management Company Ltd representative and the Acting Accountant General.

The Acting Accountant General certified the List of Securities in the presence of NAO representatives during the meeting held on 27 October 2016.

Public Credit – Loans made by Government and Repayments thereof

Balances and other details of all loans issued by Government as on 31 December 2015 as reported in Appendix E of FR 2015, are summarised as follows:

		€
a.	Loans under Act II of 1956	23,099
b.	Other Loans	67,705,999

Other Loans at *(b)* consist of the following:

	€
Aids to Industries Scheme	3,718
Agriculture – Assistance to Co-operatives	66,620
Water Services Corporation	4,567,885
Loan Facility Agreement with the Hellenic Republic	50,683,923
Loan Facility Agreement with Air Malta p.l.c.	11,984,000
Loan – Mariam Al Batool	399,854

(Source: FR 2015, page 177)

Existing Loan Agreements

Agriculture – Assistance to Co-operatives

A total balance of €66,620 was still due as at year-end by four different Co-operatives, for loans given to them during the period 1983 to 1985.

Water Services Corporation

The loan to the Water Services Corporation (WSC) is interest free, and repayable either through a direct payment to Treasury in the event that no subvention is required by the Corporation or through a Transfer Voucher in the event that the Government's subvention is still required. The initial amount of the loan was of €10,482,180.

A loan repayment amounting to €400,000 was effected by the Corporation during the year 2015, leaving a closing balance as at 31 December 2015 of €4,567,885.

Loan Facility Agreement with the Hellenic Republic

The loan to the Hellenic Republic originated from an €80 billion Loan Facility Agreement signed between the Euro Member States (the Lenders) except Greece, and the Hellenic Republic (the Borrower), dated 8 May 2010. The maximum amount that the lenders shall contribute under the Facility was established in this Agreement, which in Malta's case, stood at €74,543,026.

The balance of the loan facility agreement with the Hellenic Republic as at 31 December 2015 amounted to €50,683,923. The principal repayments were rescheduled between 15 June 2020 and 15 September 2026.

Loan Facility Agreement with Air Malta p.l.c.

As already reported in the previous year's AAR, on 15 November 2012, a 'commercial' loan of €52 million was granted to Air Malta p.l.c. as part of a restructuring plan, which was authorised by the European Commission. The first repayment of €40 million fell due in January 2015, whilst the remainder sum of €12 million fell due in January 2016.

In fact, on 9 January 2015, the Government and Air Malta p.l.c. entered into a Set-off and Payment Agreement, whereby the first repayment of €40,016,000 in part settlement of the outstanding balance, was set off in accordance with the Loan Agreement, against the acquisition by Government of additional Ordinary Shares in Air Malta p.l.c., as earlier agreed. Further details of the Government's investment in Air Malta p.l.c., in accordance with the restructuring plan, may be found under 'Investments' on page 33 of this Analysis.

Loan – Mariam Al Batool

During 2011 and 2012, Government lent a total of €399,854 to the Mariam Al Batool School, due to the suspension of the financial subsidy which the School used to receive from Libya, as *per* agreements dated 28 April 2011 and 14 December 2011. The repayment dates were scheduled at a rate of €25,000 at end of each quarter for the period March 2014 to December 2017. However, up to the writing of this Report, the first 11 payments due, totalling €275,000, were not honoured. Upon enquiry, NAO was informed that Treasury does not have formal documentation explaining why the School is not servicing the loan.

Investments held on behalf of Sinking Funds

Article 27 of the Local Loans (Registered Stocks & Securities) Ordinance, (Cap. 161), requires the Treasury to invest any contributions made in the sinking fund and any return generated from the investment in other financial assets with the aim to generate some return. Therefore, contributions and investment income generated will be invested or reinvested again in Government Securities. Any investment of this type is excluded from total Government debt.

The following is a breakdown of Investments held on behalf of Sinking Funds:

Table 9: Sinking Funds Investments

Investment	Sinking Funds - Local	Sinking Funds - Foreign
	€	€
Central Bank of Malta Deposit Accounts	83,179,508	21,299,911
Malta Government Stocks	67,579,199	-
Totals	**150,758,707**	**21,299,911**

(Source: FR 2015, page 191)

Advances

Accounting for Advances

Article 89 of the General Financial Regulations, 1966 stipulates that "... *it shall be the duty of the Accounting Officers to see that such accounts are repaid as early as possible in the manner specified in the warrant*".

Appendix L of FR incorporates a detailed statement of balances remaining outstanding as on 31 December 2015, in respect of advances made to various Ministries on behalf of Government Departments, Agencies and Organisations.

Pending advances were reported as amounting to €96,037,248 as on 31 December 2015, as against €111,172,533 outstanding by the end of the previous year.

Advances Repaid

An advance in relation to Gozo Channel Co. Ltd – Debt Repayment amounting to €291,172 was fully repaid by said Company, according to BO. Another advance for €10,623,291 pertaining to Malta Drydocks Corporation (2000) was fully repaid out of public funds – Item 7189 (Contribution towards Treasury Clearance Fund).

Outstanding Advances

Outstanding advances as at 31 December 2015, apart from advances forwarded to the former Malta Drydocks Corporation and Malta Shipbuilding Co. Ltd, were the following:

Table 10: Outstanding Advances

Description	Amount
	€
Malta Development Corporation on 24 July 1984, for the purchase of Verdala Hotel	1,724,785
Ministry of Finance to the Bank of Valletta Employees Foundation, for the purchase by the Foundation of 1,385,406 ordinary shares in Bank of Valletta Ltd in 1995	1,836,314
Commissioner of Inland Revenue, to meet loans in terms of Article 4 of the Monte Di Pieta` Act (No. XXXIX) of 1976	305,899
Ministry of Finance, for the purchase of shares held by Enemalta Corporation in Mediterranean Offshore Bunkering Co. Ltd	9,317,494
Treasury for the purchase of shares held by Sea Malta Co. Ltd in Mediterranean Offshore Bunkering Co. Ltd. The amount so advanced should be accounted for and repaid out of proceeds forthcoming from the eventual privatisation of the same Company, immediately such proceeds become available to Government.	1,109,173
Ministry of Finance and Commerce, to be utilised as a loan facility by the Maltacom Employees Foundation, to purchase ordinary shares in Maltacom p.l.c. in 1998	4,907,504
Ministry for Economic Services, for the purpose of settling during 1999 and further servicing costs of Malta Freeport loans	4,977,644
Ministry for Economic Services, to meet expenditure in connection with the privatisation process of the Malta Freeport operations	2,118,836
Ministry for Economic Services, for the purpose of settling Malta Freeport equipment claims	10,482,180
Treasury for the purchase of Medigrain shares from Mid-Med Bank p.l.c. in 1999	614,927
Ministry of Finance, advanced to Mid-Med Employees Foundation, for the purpose of investment, pursuant to the agreement dated 3 December 2002 and entered into between Malta Government and the Foundation in the interest of the members of the said Foundation	6,988,120
Ministry of Finance, the Economy and Investment for the purpose of extending loan Facilities to Mariam Al Batool School	399,854
Total	**44,782,730**

Remarks

Purchase of Verdala Hotel – €1,724,785

This advance was made to Malta Development Corporation on 24 July 1984 for the purchase of Verdala Hotel, and is still showing in the books of Malta Enterprise as due to Government. This company entered into a deed of sale in 1997. Legal proceedings covered outstanding dues to Malta Enterprise and the unfulfilled obligations for the development and operation of a new hotel complex. MFIN was informed by Malta Enterprise that the matter is still pending with legal proceedings in Court. Hence, no indication is yet available as to when this issue will be settled.

Bank of Valletta Employees Foundation - €1,836,314

Treasury stated that Bank of Valletta Foundation benefitted twice from the tax at source withheld on its holding of shares in Bank of Valletta p.l.c. In the first case, the amount of tax at source was transferred on MFIN request and credited against the loan account balance in terms of the 1995 Loan Agreement between

the Government of Malta and the Foundation. The latter claimed the tax at source as credit in its income tax return through the self assessment system, which claim eventually resulted in a tax refund. MFIN confirmed that a repayment was received from the Foundation during 2015 in terms of the repayment schedule. The said Ministry shall continue to pursue the annual repayments of the balance due on this advance.

Purchase of Mediterranean Offshore Bunkering Co. Ltd Shares from Enemalta and Sea Malta Co. Ltd - €9,317,494 and €1,109,173 respectively

As in previous years, MFIN confirmed that the amount advanced is planned to be repaid out of proceeds forthcoming from the eventual privatisation of the Mediterranean Offshore Bunkering Co. Ltd.

Loan to Maltacom Employees Foundation - €4,907,504

The Ministry for Finance is pursuing the repayment of the loan through annual amounts due, together with possible renegotiation with the Foundation of the original terms under which the loan was granted.

Malta Freeport Loan Servicing and Purchase of Medigrain Shares from Mid-Med Bank p.l.c. - €4,977,644 and €614,927 respectively

The Finance Ministry stated that it will continue to gradually repay these advances out of the annual budgetary provision under Item 7189 (Contribution towards the Treasury Clearance Fund) of MFIN Capital Vote, as is done each year in the case of other similar past advances. During 2015, a repayment of €3,000,000 was made in respect of Malta Freeport Loan Servicing, whilst an amount of €700,000 was repaid in respect of Medigrain Shares.

Malta Freeport Privatisation Process and Malta Freeport Equipment Claims - €2,118,836, €10,482,180 respectively

As confirmed by MFIN, both advances are planned to be repaid by public funds out of the annual budgetary provision under Item 7189 (Contribution towards Treasury Clearance Fund) of MFIN Capital Vote.

Mid-Med Bank Employees Foundation - €6,988,120

As stated by MFIN, the repayment of this loan is expected to commence in 2018, when the 15-year *moratorium* of the loan agreement expires.

Loan Facilities to Mariam Al Batool School - €399,854

The Ministry for Finance stated that the programme of Government is being kept in view when considering the outstanding amount due on this advance.

Other Outstanding Advances

Further pending advances to be repaid out of the 'Contribution towards Treasury Clearance Fund' are listed in *Table 11*.

Table 11: Pending Advances to the former Malta Shipbuilding Co. Ltd and Malta Drydocks Corporation

Description	Amount
	€
Construction of ships at Malta Shipbuilding Co. Ltd	21,643,890
Malta Drydocks Corporation – 2001	29,610,628
Total	**51,254,518**

The Finance Ministry stated that it plans to repay these advances out of the annual budgetary provision under Item 7189 (Contribution towards the Treasury Clearance Fund) of MFIN Capital Vote, as in the case of other past advances issued to the Malta Shipbuilding Co. Ltd and Malta Drydocks Corporation, respectively. In fact, as indicated in the 2015 FR, an amount of €10.6 million of public funds was utilised in full settlement of the advance of Malta Drydocks Corporation – 2000, whilst €376,708 was paid in relation to the advance of Malta Drydocks Corporation – 2001.

Central Bank of Malta Public Account

Treasury submitted to NAO outstanding monthly reconciliation statements for the Public Account for the period September 2014 to December 2015.

As reported in last year's AAR, NAO noted that discrepancies classified as '*Other Adjustments*' between the reconciled balance as *per* CBM Statement and the balance reported in the Cash Book, fluctuated from €5.5 million in September 2014 to €4 million as at December 2015. The explanation forwarded by Treasury stated that "... *This discrepancy can arise since there might have been some adjustments done during the year. A close off which was omitted either from the cash book or from the CBM side may* ..." result in this discrepancy.

With regards to the reconciliation for the period June 1992 to December 2001, Treasury once again confirmed no development in this respect, and its position remained the same as detailed in the 2014 AAR[7].

Boards of Survey

Boards of Survey at Treasury and at the Ministry for Gozo were appointed in terms of Section 98 of the General Financial Regulations, 1966, in order to take account of moneys, deposits and other values as at 31 December 2015.

Meanwhile, the Board of Survey at Treasury met in mid-December 2015 to certify the correctness of the relevant statements for the year ended 2014, since the Government Securities Board approved the 2014 List of Securities held at Treasury late in the year on 28 October 2015. NAO received the Report prepared by the Board on 23 December 2015, with no adverse remarks.

The Reports of the Board of Survey at Treasury and Gozo reached this Office in November 2016, with no adverse remarks.

[7] Treasury still maintains that the start-off date of the new reconciliation exercise should be January 2002. Treasury stated that during the indicated 10-year period, there had been various changes both in Government's accounting system and in that of CBM, making it impossible to embark on any kind of reconciliation for the years in question. This decision is based on cost considerations and human resources requirements.

Ministerial/Departmental Bank Accounts

Treasury Circular No. 1/2016 - 'End of Year (2015) Statements of Account Cash in hand and Bank Balances held at Local Commercial Banks and Central Bank of Malta', issued on 6 January 2016, requested Heads of Departments and other Accounting Officers to submit both soft and hard copies of the Return indicating the cash and bank balances as at 31 December 2015, including the position of each bank account held both at local commercial banks and CBM. In addition, officers were to submit a hard copy of these balances to Treasury, clearly indicating those bank accounts against which a liability exists, as well as identify bank accounts in respect of Trust Funds.

The respective balances were published accordingly in FR 2015 (pages i to vii refer). Whilst the credit balance as *per* Bank Statement consists of the 'Liability', 'Trust' and 'Resulting Balances', the 'Debit Balance' on the other hand, should portray only credit card accounts. An exception to this was reported in FR in relation to four Ministries/Departments, which had overdrawn balances as at year-end, totalling €99,592. The majority of this overdrawn balance (€97,193) pertained to the Ministry for Sustainable Development, the Environment and Climate Change. Treasury duly queried such overdrawn balances with the respective Ministries and Departments, and corrective action was taken as necessary.

NAO also noted that the Return submitted by the Education Department was erroneously overstated by €19,693, thus resulting in FR being overstated by same amount.

Liabilities

Table 12 features the Statement of Liabilities:

Table 12: Statement of Liabilities

	2015	2014
	€'000's	€'000's
Public Debt	**5,111,737**	**4,996,343**
Euro Coins issued on behalf of Treasury[8]	**68,510**	**60,397**
Treasury Bills	**222,050**	**140,356**
Deposits		
Court and Other Deposits	143,531	91,958
Other	23	23
	143,554	**91,982**
Funds		
Sinking Funds	172,059	148,410
Contingencies Fund	1,165	1,165
Trust Funds	2,018	1,891
	175,241	**151,466**
Total Liabilities	**5,721,093**	**5,440,543**
Excess of Total Liabilities over Total Assets	**(4,330,542)**	**(4,136,800)**
Accumulated Fund		
Consolidated Fund at year end	(170,138)	(23,536)
Net Public Debt/Public Credit	(4,160,404)	(4,113,264)
	(4,330,542)	**(4,136,800)**

Figures in Statement may not add up due to rounding up.
(Source: FR 2015, page 196)

[8] A revised balance of Euro Coins supersedes the figure published in the Annual Financial Statements for 2015, as explained under 'Public Credit – Other Investments' in this Report.

Public Debt

Debt Composition

In general, Government's borrowing programme includes MGS and Treasury Bills. The Government sets the long-term Public Debt management goal, and its preference as to the type of debt and the maturity profile helps provide the market with long-term confidence about the nature of Government's future borrowing consistent with an acceptable level of risk.

Debt Composition of the Government Sector Debt as at end-of-year stood as follows (*Tables 13* and *14* refer):

Table 13: Debt Composition – Domestic and External

2015		2014	
Domestic Debt	External Debt	Domestic Debt	External Debt
%	%	%	%
96.43	3.57[9]	95.90	4.10[9]

(Source: Refer to *Table 14* for percentage calculations)

Table 14: Government Sector Debt

Type of Debt	2015		2014	
	Amount	Percentage of Total Debt	Amount	Percentage of Total Debt
	€'000's	%	€'000's	%
Malta Government Stocks (Consolidated)	4,953,923	88.11	4,828,016	89.06
European Financial Stability Facility (Rerouted Debt)[10]	171,189	3.05	181,794	3.35
Treasury Bills	222,050	3.95	140,440	2.59
Extra Budgetary Units and Local Councils	120,118	2.14	113,726	2.10
Euro Coins	68,510	1.22	60,397	1.11
Other Local Loans	56,379	1.00	56,379	1.04
Foreign Loans	29,775	0.53	40,389	0.75
Total Debt	**5,621,944**	**100**	**5,421,141**	**100**

(Source: Budget Speech 2017; Quarterly Accounts for General Government: Q2/2016 – National Statistics Office News Release No. 173/2016; DMD)

[9] Excludes MGS held by non-residents which in 2015 amounted to 6% (2014: 5%) and includes the European Financial Stability Facility (EFSF) (Debt Rerouting).

[10] EFSF was established on 7 June 2010 for the purpose of providing stability support to Euro Area Member States (EAMS). EFSF finances such support by issuing or entering into bonds, notes, commercial paper or other financing arrangements. The operations are backed by guarantees of EAMS on the basis of an agreed 'Adjusted Contribution Key'. On 27 January 2011, Eurostat decided that the debt issued by EFSF for each support operation must be rerouted to the Public Accounts of EAMS providing guarantees, proportionately to their contribution key. Therefore, the recording of such flows will impact the Gross Government Debt (as defined in the Maastricht Treaty), but not the net debt.

[11] Public Debt balance as at 31 December 2014 has been updated from the balance reported in the previous year's AAR to provide a more accurate analysis as *per* most recent publications.

Public Debt Percentages

Table 15 portrays debt as a percentage of Gross Domestic Product (GDP) as at 31 December.

Table 15: Debt as a Percentage of Gross Domestic Product

2015			2014		
Public Debt	Gross Domestic Product	Ratio Public Debt to Gross Domestic Product	Public Debt	Gross Domestic Product	Ratio Public Debt to Gross Domestic Product
€'000's	€'000's	%	€'000's	€'000's	%
5,621,944[12]	8,788,351[13]	63.97	5,421,141[12]	8,092,894[14]	66.99

As at end-of-year 2015, the percentage of Government's debt to the country's GDP amounted to 63.97%, resulting in a decrease of 3.02% over the previous year. This indicates that the economy grew faster than debt during 2015. Such result was in line with Government's core medium-term fiscal objective of restoring the trajectory of public finances to a sustainable path.

As reported in the Government's Annual Report, which was issued by MFIN in June 2016, in line with Article 41 of the Fiscal Responsibility Act (FRA), the notable decline in the debt ratio primarily reflected a more buoyant macroeconomic environment than that expected in the earlier Update of the Stability Programme. Overall, both in the 2016 Stability Programme and the Commission 2016 Spring forecast, it was deemed that the debt rule has been respected in 2015 in its forward-looking dimension.

Local Loans

On 31 December 2015, the local Public Debt amounted to €5,420,980,000, representing an increase of €221,303,000 over the corresponding reported figure for 2014. In addition to MGS totalling €4,953,923,000, the closing local Public Debt balance is inclusive of Treasury Bills outstanding at year-end, debts of Extra Budgetary Units (EBU) and Local Councils, Euro Coins, as well as Domestic Loans with Commercial Banks, amounting to €222,050,000, €120,118,000, €68,510,000 and €56,379,000 respectively (Details in *Table 14*).

Foreign Loans

The authorisation and regulation of raising foreign loans is governed by the Development Loan Act (Cap. 229), which authorises the Government of Malta to enter into agreements with foreign governments, international organisations or other institutions, to obtain financing from abroad to support Malta's economic development.

Whereas all domestic borrowing by the Maltese Government is by way of public offer of securities, all foreign borrowing is in the form of bilateral non-marketable loans with foreign governments and international institutions.

The policy of borrowing from overseas through bilateral agreements with foreign governments/organisations lies within the remit of MFIN, and is usually sought to finance specific projects. All loan agreements are subject to the final approval of the Minister for Finance, after consulting CBM on the terms and conditions of each loan. DMD is ultimately responsible for the recording and servicing of such loans. The process of sourcing foreign loans falls exclusively under the responsibility of MFIN.

A detailed analysis of the existing foreign loans due, which as at end 2015 stood at €29,775,000, is provided in *Table 16*.

[12] Source: *Table 14* refers.
[13] Source: Budget Speech 2017; Gross Domestic Product: Q2/2016 – National Statistics Office News Release No. 142/2016.
[14] GDP balance as at 31 December 2014 has been updated from the figure reported in the previous year's AAR to provide a more accurate analysis as *per* most recent publications. Source: Gross Domestic Product: Q2/2016 – National Statistics Office News Release No. 142/2016.

Table 16: Foreign Loans Analysis

Foreign Loan	Financing Purpose	Year of Issue	Amount Disbursed	Interest Rate	Date of Maturity	Balance due as at 31 December 2015
				%		€'000's
Council of Europe Fund for Development 2003	Mater Dei Hospital	2003	€75.5 million	4.65	07/05/2018	22,650
Council of Europe Fund for Development 2002	Mater Dei Hospital	2002	€25.5 million	5.06	11/12/2017	5,100
European Union Loan C	Solid Waste Composting Project	1987	€3 million	1.00	15/09/2027	1,308
European Union Loan B	Improvements in the Grand Harbour	1979	€5 million	1.00	15/11/2018	571
Government of Canada	Telephone cables and equipment	1974	CAD 1 million	-	31/05/2024	141
Total						**29,770**[15]

(Source: FR 2015, page 181; AAR 2014, page 45)

In addition to the aforementioned foreign loans, the closing external Public Debt balance is inclusive of EFSF Rerouted Debt amounting to €171,189,000 (Details in *Table 14*).

Debt Management

Background

The Debt Management Directorate was established within the Treasury Department in December 2006 with responsibilities for debt and cash management for the central Government and for providing specified funding requirements as authorised by Parliament.

As illustrated in *Figure 1*, the principal objective of the Directorate in its debt and cash management activities is to raise funds, as well as to carry out other financial transactions in such a way as to ensure that:

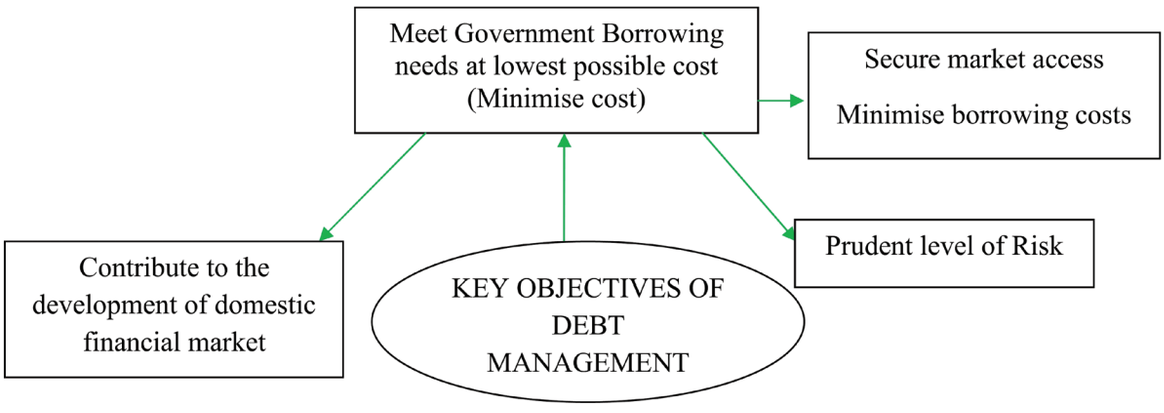
a. central Government borrowing programme (short and long-term) is financed at the lowest possible long-term borrowing costs and subject to a prudent level of portfolio risk;

b. liquidity of Government funds is adequate to meet Government's payment obligations as they arise and fall due; and

c. domestic financial markets are given the necessary support.

[15] The total balance due as at 31 December 2015 in the *Table* above does not agree with the balance of €29,775,000 reported in respect of Foreign Loans in *Table 14*. This difference arose since the balance due from the loan made with the Government of Canada as was reported in the Financial Report was converted to Euro using the respective rate as at 31 December 2015, whilst in the *Table* showing the Government Sector Debt, the same balance in Canadian Dollars was converted to Euro using the prevailing rate of exchange upon the preparation of the 2017 Budget figures.

Figure 1: Key Objectives of Debt Management



(Source: 'The functions of a Sovereign Treasury – Treasury of Malta Perspective')

Legal Framework for Borrowing

The current statutory basis for central Government borrowing is set out under the following primary and subsidiary legislation:

a. Malta Treasury Bills Act, Cap. 133

b. Malta Treasury Bills (Dematerialisation) Regulations, 2007

c. Local Loans (Registered Stock and Securities) Ordinance, Cap. 161

d. Local Loans (Registered Stock) Regulations, S.L. 161.01

e. Development Loan Act, Cap. 229 (in respect of bilateral loans raised outside Malta)

f. An annual budget law that authorises the Minister for Finance to raise loans on behalf of the Government for an established amount during the financial year by the issuing of securities, and also provides the main purposes for which Government can apply such borrowing (for year 2015, Act No. XIII of 2015 'The Budget Measures Implementation Act' refers).

It is to be noted that during 2015, the Treasury continued to work with the Commonwealth Secretariat on the new Government Borrowing and Public Debt Management Act (GPDMA).

Government Borrowing and Public Debt Management Act

The scope of the GPDMA is to replace the different pieces of legislation enacted long time ago and which currently govern borrowing by the Maltese Government. Apart from bringing the different pieces of borrowing legislations under one Act, it shall introduce the concept of management of public debt consistent with international best practice in debt management.

As at the date of writing of this Report, the GPDMA was referred to the Attorney General for the legal drafting. Once DMD receives the first copy of the Draft Bill from the Attorney General's Office, the Directorate shall be referring it to the Cabinet Office for its approval.

Moreover, in Part I, Article 4(2) of the Budget Measures Implementation Bill presented in Parliament on 17 October 2016, a reference was made to the substitution of the Local Loans (Registered Stocks and Securities) Ordinance with a new law, on such terms and conditions as the Minister for Finance may approve.

General Economic Factors

General economic factors are likely to have an influence on the nature and extent of Public Debt Management activities. During the year 2015, such factors included:

a. Lower Tax Rates

Lower income tax rates, amongst other factors, contributed to the strong economic growth rate registered during 2015, and thus led to positive variances when comparing actual with estimated tax revenue. As a result, lower tax rates did not generate a shortfall in tax revenue that instigated higher financing needs.

b. Lower Interest Rates

The low interest rate environment in domestic and foreign financial markets persisted and intensified during 2015, especially with the further loosening of the European Central Bank (ECB)'s standard and non-conventional monetary policies. These conditions were undoubtedly advantageous for sovereigns, as low interest rate environment eased the trade-off between cost and risk, as well as presented an opportunity for low-cost migration of roll-over risks. On the backdrop of the low interest rate environment, DMD continued to issue long-dated MGS at historic low coupon rates. The Directorate took this opportunity to keep on extending the Weighted Average Maturity (WAM) of the MGS portfolio (from 8.6 years to 8.7 years), thus further reducing refinancing risk and locking-in low cost financing for longer periods of time. The overall effect is reflected in the relatively marginal increase in total public debt interest expenditure registered in 2015 over 2014 (+0.5%)[16]. On the other hand a negative effect of the low interest rate policies adopted by the ECB is the levying of negative interest rates on cash balances held at the Central Bank above specific thresholds.

In 2015, for the first time in history, DMD registered a negative weighted-average interest rate on total Treasury Bills issued of minus 0.0192%. The Directorate started receiving and allotting bids with negative interest rates for 91-day Treasury Bills auctions towards the end of May 2015. Twenty-eight day and 273-day Treasury Bills at negative interest rates started being allotted from October and November 2015 respectively. Total interest received on Treasury Bills issued during 2015 amounted to €75,539, of which €9,937 were attributable to the same year. The net total interest expense incurred on short-term borrowing in 2015 amounted to €98,110 (€108,047 - €9,937), which is substantially lower compared to the €2.9 million outlay estimated in the Financial Estimates and €1.9 million spent in 2014.

c. Lower Euro Strength

Although the Euro Area showed timid signs of economic recovery in 2015, this was not enough to trigger the desired inflationary pressures, forcing the ECB to step-up its stimulus measures. Although the exchange rate is not a policy target of the ECB, the various monetary easing measures adopted

[16] Financial Report 2015 page xvii, Interest on Public Debt increased marginally to €232,331 (2014: €231,096).

inevitably put downward pressure on the Euro. Furthermore, the relatively stronger economic recoveries registered in the United States and United Kingdom fed market expectations of imminent interest rate increases in these countries, exerting further pressures on the Euro. Indeed, the United States Federal Reserve raised interest rates from historical lows in December 2015, after nearly 10 years of near-zero rates since the onset of the global financial crisis.

The Directorate finalised repayment of the United States Government loan in November 2015. Hence, any further Euro weakening against the United States Dollar will not affect the Directorate's servicing needs and costs. The only outstanding foreign-currency denominated loan is the Canadian Government loan, whose repayment is amortised until 2024, but with a modest balance of CAD 212,500 (€140,580) as at 31 December 2015. Thus, exchange rate risk will minimally affect its servicing, and hence, borrowing needs and costs.

d. Euro Zone/Greek Debt Crisis

Euro Area sovereign yields dropped upon the announcement by the ECB of its Public Sector Purchase Program in January 2015. The program, which commenced in March 2015, is intended to lower interest rates across various maturities to stimulate borrowing, consumption, investment, economic growth and finally inflation, towards the ECB's inflation target. The bond price rally started reversing in spring of 2015, but continued from summer onwards, although at a slower pace. Since inflation rates did not increase much as a result of the ECB's policies, in December 2015 it was decided to strengthen the stimulus measures: an extension of financial asset purchases for a further six months until at least March 2017; a widened range of eligible financial assets; and a lower negative deposit rate on cash held at Euro Area central banks from minus 0.20% to minus 0.30%. The program adjustments did not meet market expectations and a general rise in Euro Zone sovereign yields ensued. Secondary market MGS yields broadly followed other Euro Area yield patterns.

After registering a mild economic recovery from mid-2014 and a consequent fall in its benchmark 10-year bond yields, Greece's prospects turned negative again towards the end of 2014 and early 2015, due to rising political uncertainty and the acrimonious nature of negotiations taking place with official creditors. Renewed sovereign default and Euro-zone break-up concerns caused peripheral Euro Area bond yields to start rising again, moderately affecting also the domestic MGS market. The situation stabilised and yields resumed their downward drift from mid-July 2015 onwards, as a third bailout agreement, totalling €86 billion financed by the European Stability Mechanism (ESM) was announced. These funds will be disbursed in tranches, conditional on the scheduled implementation of a number of agreed structural reforms, and are intended to help Greece meet economic restructuring and debt servicing costs.

The nature of Malta's €171.2 million exposure (as at 31 December 2015) to the temporary EFSF is in the form of guarantees. The EFSF is not providing new financing programmes since July 2013, and is only servicing existing credit facilities until maturity. Hence, this exposure is expected to gradually fall as programme countries pay back their EFSF debt. Malta's exposure to the ESM is in the form of a €58.5 million paid-in shareholding, out of a total capital subscription of €511.7 million. Each ESM member's capital subscription is calculated according to the key of the country's capital subscription to the ECB's capital.

Main Aspects of Debt Management

As already reported in the previous year's AAR, the five main aspects of Debt Management that need to be audited every year, as part of International Best Practices are Policy, Operations, Risk Control Procedures, Information Technology (IT) Systems, and the Financial Aspect.

Methodology for the Analysis of Public Debt

As part of this year's analysis of Public Debt, NAO deemed it appropriate to forward to DMD a number of queries related to each of the five main aspects of Debt Management. These questions were based on the existing local Legal Framework and the latest Revised Guidelines for Public Debt Management dated 1 April 2014, as prepared by the World Bank and the International Monetary Fund (IMF). Moreover, in preparation for the adoption and implementation of the International Public Sector Accounting Standards (IPSAS)[17] by the Maltese Government[18], this Office featured a number of additional questions, based on a number of related International Standards of Supreme Audit Institutions (ISSAIs)[19], as well as material issued by the United Nations Institute for Training and Research, all relating to the auditing of Public Debt.

The applied standards are outlined as follows:

a. ISSAI 5410 – Guidance for Planning and Conducting an Audit of Internal Controls of Public Debt

b. ISSAI 5421 – Guidance on Definition and Disclosure of Public Debt

c. ISSAI 5440 – Guidance for Conducting a Public Debt Audit – The Use of Substantive Tests in Financial Audits

In this regard, DMD provided a detailed description of the main elements comprising the 2015 Debt Management, as further outlined.

Characteristics of Public Debt Management Activities

The following two tables[20], as listed in ISSAI 5440, provide checklists of issues drawn from the aforementioned Guidelines for Public Debt Management, which auditors may wish to consider when developing their understanding of public debt management. The lists are illustrative and not intended to encompass every characteristic that might be present in the International Organisation of Supreme Audit Institutions countries.

[17] IPSAS are a set of accounting standards issued by IPSAS Board for use by public sector entities around the world in the preparation of financial statements.

[18] The adoption and implementation of IPSAS by the Maltese Government will revolutionise the current system from a cash to an accruals-based public sector accounting system based on IPSAS.

[19] The ISSAIs were issued by the International Organisation of Supreme Audit Institutions.

[20] The two tables were originally compiled by the International Organisation of Supreme Audit Institutions on the basis of a questionnaire sent to public debt managers in many countries in order to identify the key features of public debt management operations. The tables are not meant to be a comprehensive list of factors that should be present in all public debt management arrangements.

Table 17: Characteristics of Public Debt Management Activities – Institutional Arrangements

Common Institutional Arrangements	Is this feature present in DMD?
	Yes/No/Not Applicable
An annual borrowing authorisation	Yes
A public debt ceiling limit	Yes
Domestic and foreign currency public debt programs managed together	Not Applicable
Separate public debt management agency	No
Separate front and back offices	Yes
Separate Risk Management Unit (middle office)	Yes
Formal guidelines for managing market and credit risk	No[21]
Annual public debt management reports	Yes
Regular external peer reviews of public debt management	No
Annual audits of public debt management transactions	Yes
Code-of-Conduct and conflict of interest guidelines for public debt management staff	No[22]
Business recovery procedures in place	Yes

(Source: ISSAI 5440 – Guidance for Conducting a Public Debt Audit – The Use of Substantive Tests in Financial Audits; Replies provided by DMD and/or noted by NAO throughout the Analysis of Public Debt Management)

[21] No formal guidelines for managing market and credit risk are available at DMD. However, upon enquiry, DMD provided a detailed explanation of how the Directorate manages such risk, as explained further on under 'Risk Control Plan and Procedures' in this Report.

[22] A Code-of-Conduct for public debt management staff is planned to be implemented during 2017. Further details are outlined later in this Report under 'Responsibilities and Accountabilities'.

Table 18: Characteristics of Public Debt Management Activities – Features of Primary and Secondary Markets

Features of Primary Markets for Public Debt Instruments	Is this feature present in DMD?
	Yes/No/Not Applicable
Auctions used to issue domestic public debt	Yes
Fixed-price syndicates used to issue domestic public debt	Not Applicable
Benchmark issues for domestic market	Yes
Pre-announced auction schedule	Yes
Central bank participates in the primary market	No
Primary dealer[23] system	No[24]
Universal access to auctions	Yes
Limits of foreign participation	No
Collective action clause, domestic issues	Yes
Collection action clause, external issues	Not Applicable
Features of Secondary Markets for Public Debt Instruments	
Over-the-counter market	Yes
Exchange-traded market mechanism	Yes
Sound clearing and settlement systems	Yes

(Source: ISSAI 5440 – Guidance for Conducting a Public Debt Audit – The Use of Substantive Tests in Financial Audits; Replies provided by DMD and/or noted by NAO throughout the Analysis of Public Debt Management)

Further details on the above-mentioned characteristics will follow in this Report.

Malta Government Stocks – Strategy and Implementation

Government's 2015 borrowing strategy was broadly on the same lines as that of previous years. It continued to tap the domestic capital market, by issuing both fixed-rate and floating-rate-Euro-denominated securities (zero currency risk) in the medium and long-term maturity horizons. The conventional fixed-rate MGS constitute Treasury's primary financial instrument by which central Government's borrowing requirements are funded. In fact, as at the end of December 2015, fixed rate bonds accounted for 95% of the total of MGS portfolio, similar to the levels prevailing at the end of the previous year.

As the structure and development of the sovereign bond market continued to evolve, the principles of debt management, including flexibility in primary market operations, communication with investors, predictability and transparency, remained of critical importance to DMD.

The Directorate adopted a front loaded approach in the first half of the year on the backdrop of a substantial fall in yields across the Euro Zone. The ECB's unprecedented accommodating policies launched its version of Quantitative Easing[25]. This deliberate policy exerted downward pressure on yields both at the short and long-end in an already low interest rate environment. It also presented an opportunity for DMD to issue long-dated securities and lengthen the redemption profile, hence mitigate the roll-over risk at a low cost.

[23] A Primary dealer is a bank/financial institution that buys Government securities directly from a Government, with the intention of reselling them to others, thus acting as a market maker of Government securities.

[24] In the absence of a primary dealer system, DMD has in place a comprehensive process of reconciliation, including daily reconciliations between Treasury's selling agents and Treasury's accounting system.

[25] ECB's asset purchase programme (Quantitative Easing) is an unconventional monetary policy in which a Central Bank purchases Government Securities (from the secondary market) or other investment grade securities from non-public undertakings (both from the primary and secondary market) in order to lower interest rates and increase the money supply.

This strategy has been encouraged in response to the strong demand for Government paper[26] both from the retail, as well as from institutional investors, shrugging off concerns that declining long-term bond yields may impair demand for MGS. This was a case where Treasury adopted a degree of flexibility and adapted quickly to changing market and other conditions.

The reliance on funding from local sources is driven by the strong demand for Government paper both from the retail and wholesale sectors, and for its benefits that help cushion the impact from the volatility and uncertainty prevailing in the international capital markets. The objective of Treasury is to meet demand within the parameters of its risk-management framework.

The Treasury designed its strategy in such a way as to ensure, as far as possible, that the best balance is reached among a number of competing factors and trade-offs, including issuing bonds where there is demand for them, debt servicing cost and refinancing risk. To this effect, the Treasury, launched consultation with different market segments and key stakeholders, with the aim of preserving transparency of its activities that would support the achievement of the desired results.

As can be seen from the Bid-to-Cover ratios in *Table 19*, there was strong participation from both institutional and retail investors. This strong demand for MGS has mitigated the risk of relying too much on few domestic players within the local capital market.

Table 19 summarises the issuance performance of MGS for the year 2015, including the level of overall participation by domestic investors.

Table 19: 2015 Malta Government Stocks Issuance Performance

Date	On offer (plus over-allotment)	Total participation	Bid-to-Cover
	€'million	€'million	
March[27]	120 + 60	443.1	3.7
June[28]	50 + 40	193.6	3.9
October	120 + 60	231.4	1.9
November[28]	35 + 0	59.3	1.7
Totals	**325 + 160**	**927.4**	

(Source: DMD 2015 Annual Report)

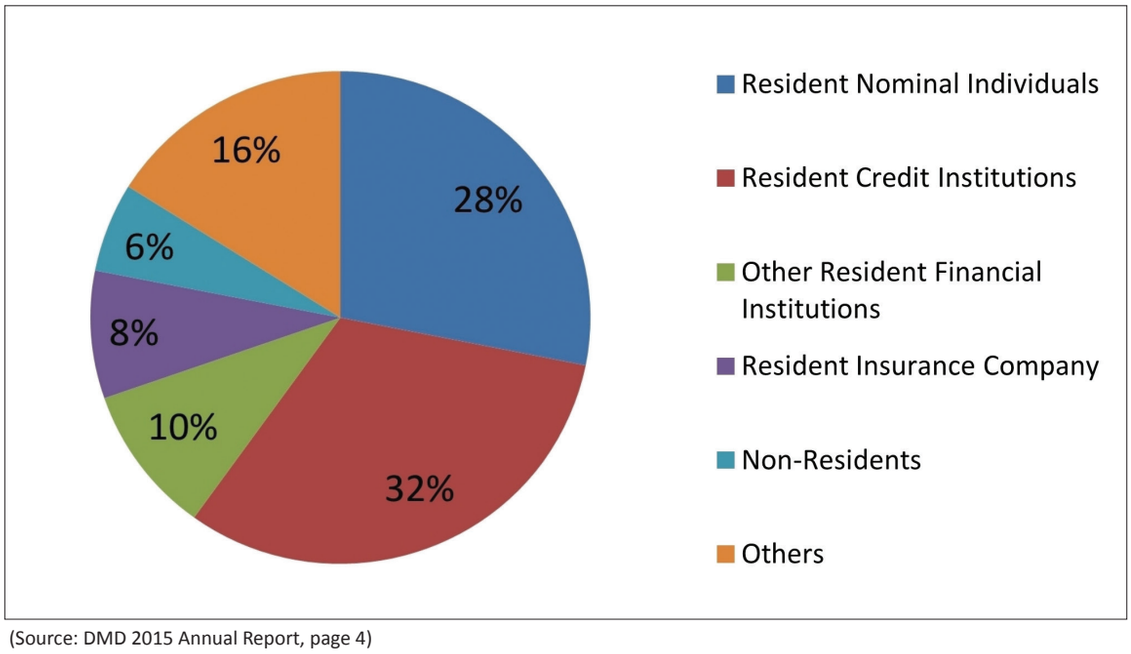
The distribution of MGS among the different types of investor categories as at 31 December 2015 is depicted in *Chart 1*. The two most significant holders of MGS are resident credit institutions and resident nominal individuals, with 32% and 28% respectively. Resident insurance companies held 8%, whilst other resident financial institutions held 10%. The level of non-resident holdings increased to 6% (from 5% a year earlier). Holdings by other investors, principally resident entities not falling under the main categories, including non-profit entities, Local Councils and public non-market units collectively amounted to 16%.

[26] 'Government paper' refers to debt securities that are issued or guaranteed by a sovereign Government.

[27] March issue was over-subscribed by retail investors.

[28] Issues (by auction) targeted for institutional investors only.

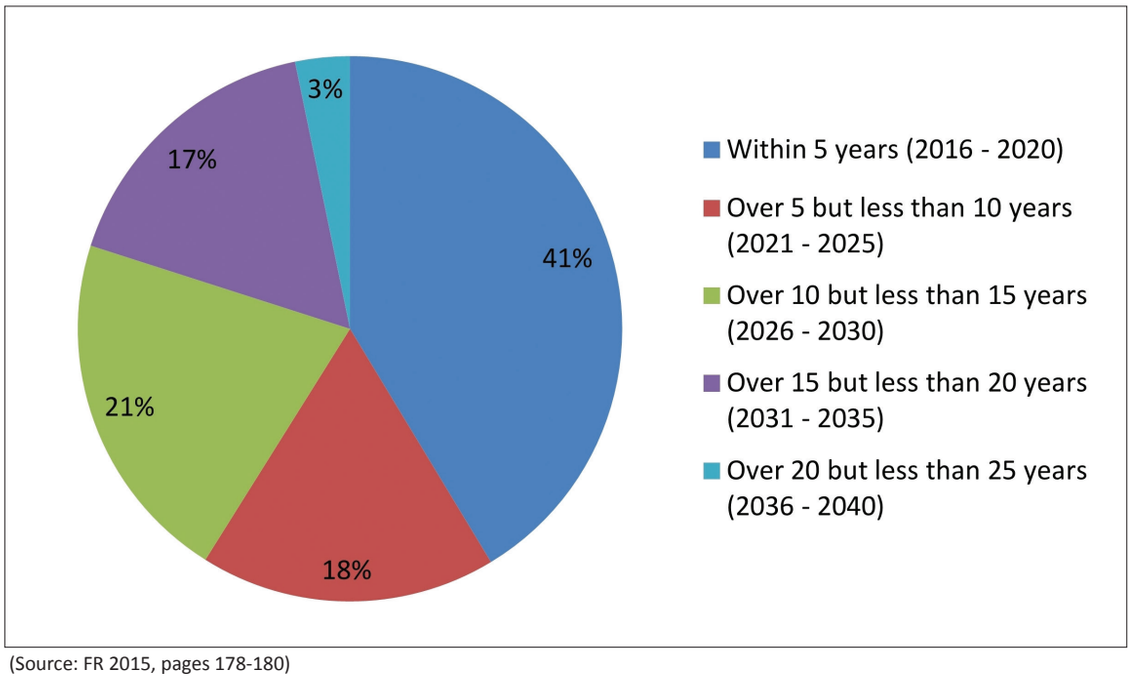
Chart 1: Malta Government Stocks Holder Distribution as at 31 December 2015



(Source: DMD 2015 Annual Report, page 4)

The gross outstanding nominal value of MGS as at 31 December 2015 reached €5,025,588,624, representing a 2.6% increase over the end-2014 balance. Forty-one percent of the total existing MGS, as at 31 December 2015, are due for redemption by Government within five years. Moreover, a further 18% are due for redemption ranging between six and 10 years. Further analysis is illustrated in *Chart 2*.

Chart 2: Maturity Profile of Malta Government Stocks as at 31 December 2015



(Source: FR 2015, pages 178-180)

This short-term maturity in the majority of the existing MGS increases potential risks in terms of rollover, concentration and duration. In this regard, in the current low interest rate scenario where interest rates touched historical lows, DMD deemed it suitable to issue longer dated bonds with a relatively attractive coupon intended for investors in search of bonds that yield a higher return. Moreover, in 2015, DMD extended the maturity profile by further six years from 2034 to 2040.

At the end of the year 2015, the WAM of MGS stood at 8.7 years, compared to 8.6 years 12 months prior. The WAM has risen remarkably from 6.6 years at the end of the year 2010. This was a deliberate policy adopted during the years mainly intended to bring about an easing in redemption profile thus limiting roll-over risk.

The WAM compares very well with other EAMS, as well as with other G7 countries. A recent publication of the Organisation for Economic Co-operation and Development (OECD) estimated that the average of outstanding marketable central Government Debt in selected OECD countries has been close to eight years in 2015. This means that Malta is positioned among the top performers when it comes to the WAM metric.

Treasury Bills – Strategy and Implementation

The Directorate also issued weekly Treasury Bills to support its daily cash management activity given that Treasury Bills is the only cash management instrument used in the cash management operations. As in previous years, in 2015 the Directorate made extensive use of the instrument in order to manage the cash balance at CBM and smooth the fluctuations in the cash balance arising from the mismatch between the timing of receipts and payments. Contrary to the trend seen in recent years, as at the end-of-year 2015, the Treasury Bills balance increased by €81.6 million to reach €222.1 million.

As a result of the levying of negative interest rates on cash balances held at the Central Bank above specific thresholds, combined with an already low interest rate environment, for the first time, the Treasury allotted Treasury Bills at negative interest rates. The negative interest earned in 2015 amounted to €75,539.

In 2012, a standard operating manual was compiled by the Management Efficiency Unit[29] following discussions held with DMD staff. The manual covers the operational procedures involved in the issuance of debt issuing, as well as compilation of reports. There were no changes in the Treasury Bills issuance process from 2012 to-date, except for the fact that the settlement period allotted through the auction system was harmonised with that of the secondary market on a T+2[30] basis on 1 October 2015.

Funding Programme

In 2015, funds were raised to finance:

a. the redemption of six MGS amounting to €349.4 million;

b. central Government Budget Deficit of €232.8 million; and

c. to effect changes in central Government's debt portfolio, in line with Government's debt management policies.

[29] The Management Efficiency Unit forms part of the Office of the Prime Minister.

[30] The T stands for transaction date, which is the day the transaction takes place. The number following the 'plus sign', in this case '2', denotes how many days after the transaction date the settlement/transfer of money and security ownership shall take place.

Operational Planning

The Directorate relies on its operation processes to successfully execute a significant number of market and financial transactions. To this effect, DMD considers the management of operational risks to be critical to its operations and for the safeguard of the reputation of the sovereign. The Directorate fosters a risk-aware culture in which all members of staff are encouraged to understand and own the risks that are inherent in their own processes and operations. This is complemented by specific guidance manuals in the form of Gantt Charts and timetables, which are issued prior to every new issuance of MGS. There are also clearly defined authorisation levels in place for the processing of financial and market transactions.

An event calendar is also shared among responsible officers to indicate the dates where action is needed to be taken, including processing of interest payments, redemptions, rate announcements and stop trading instructions. The shared calendar, which is maintained on a spreadsheet template, was created to avoid concentration of key activities or related controls on one individual or small group of staff.

Risk Control Plan and Procedures

The main risks faced by DMD relate to market risk, amongst which interest rate and exchange rate risks, refinancing, liquidity, credit, settlement, operational and fraud risks. The risk exposures of a public debt portfolio are determined by the composition of such portfolio, including the share of the short-term *versus* the longer-term debt in the portfolio, the variable interest rate debt relative to fixed rate debt, and debt denominated in foreign currency.

a. Market Risk

Market risk refers to the possibility of increases in the cost of the debt arising from changes in market variables, such as interest rates and exchange rates. DMD's exposure is mainly related to the interest rate risk given that all marketable debt is issued in the domestic currency. The interest rate risk exposure is managed in two main areas arising from weekly cash management operations and on a daily basis monitoring of the interest rate in the MGS secondary market.

When possible, DMD avoids issuances of medium-to-long-term debt during times of market stress or volatility. Any change in market conditions can affect the demand for Government paper and therefore the interest cost. An additional measure aimed at enhancing the sources of funding is the proposed inclusion of a provision in the new draft legislation which opens up the possibility for Government to issue marketable debt in the international markets if such need arises.

b. Interest Rate Risk

Interest Rate risk is defined as the risk of increases in the cost of debt arising from changes in interest rates. The re-fixing risk of central Government Debt portfolio as at the end-of-year 2015 for debt maturing in respect of Floating-Rate Notes (FRN) within one and five years respectively, stood below the Euro Area average. Such Euro Area benchmarks emanate from the quarterly publications of a set of risk metrics agreed upon by EAMS in the European Sovereign Debt Markets (ESDM). These metrics are published for consumption and analysis within the Economic and Financial Committee. The re-fixing risk metrics calculate the amount of debt as a proportion of the total debt portfolio that will be exposed to the interest rate.

The outstanding level of Treasury Bills in the central Government's debt portfolio is a major determinant of the interest rate risk. However, the relevance of the re-fixing risk has to be viewed in the context of current domestic money market environment, which during 2015 has been characterised by strong participation (bid-to-cover ratio of 3.44) combined with issuances of Treasury Bills moving into the territory of negative interest rates.

In this regard, DMD bases the coupon of new medium-to-long-term securities to be issued in the primary market on the yields prevailing in the secondary market. The final decision on the coupon[31] is taken by PDMAC during meetings specifically conveyed to discuss new issues of MGS. This Committee's discussion also focuses on the current yields offered by other countries, how yields are expected to move, and how markets are reacting together.

For prudence purposes, and in order to mitigate the risk from an increase in interest, the Directorate keeps the level of Floating-Rate Debt below 10%. As at 31 December 2015, such ratio stood at 4.94%. It is to be noted that as a matter of policy, DMD does not enter in any interest swap agreements and its portfolio does not include any derivatives instruments. The Directorate also monitors the market conditions to identify the ideal time to intervene in the market, as well as decide on the type of instruments to be offered, so that a balance is struck between cost, associated risks and demand.

c. Exchange Rate Risk

Exchange Rate risk refers to the risk of increases in the cost of debt arising from changes in exchange rates. With regard to exchange rates, DMD's exposure for exchange rates is limited to a minor balance of foreign loans, totalling €140,580, representing only 0.47% of the total debt at year-end, rendering such risk immaterial.

d. Refinancing Risk

Refinancing risk is the danger that debt will have to be refinanced at an unusually high cost or cannot be refinanced at all. Rollover risk is traditionally and conceptually assessed by the debt metric known as WAM. Over the past years, DMD has pursued a strategy of lengthening the average maturity of its debt portfolio as this implies the reduction of rollover risk.

The structure of the redemption profile of central Government debt is not particularly challenging to refinance given the strong WAM, combined with a relatively smooth redemption profile. The current low interest environment has made it more attractive for DMD to pursue a policy of lengthening of WAM because it has become cheaper to limit the rollover risk. Borrowing cost became more predictable over time and this advantage was achieved at more limited cost than in the past.

Moreover, DMD has an internal policy that the outstanding balance of MGS shall not exceed a pre-established amount. Consequently, from time to time, the Directorate reviews MGS portfolio and if need be, it recommends the PDMAC to evaluate the use of a bond switch transaction.

e. Liquidity Risk

Liquidity risk refers to a situation where the volume of liquid assets diminishes quickly as a result of unanticipated cash flow obligations and/or a possible difficulty in raising cash through borrowing in a short period of time. Every week the Treasury Bills' 'Take-up Projections' sheet is compiled to take into account all information in respect of expected receipts from main revenue generating departments, expenditure and redemptions.

DMD takes a broader time horizon of the cash flow projections based on information made available to the Directorate. These projections are fine-tuned every Tuesday before the Treasury Bills' take-up. When planning the monthly Treasury Bills' calendar, DMD officials take into consideration various factors, such as the expected stream of revenue and expenditure, as well as financing items falling due in a particular week and the target balance of Treasury Bills at the end of the year.

[31] A 'coupon' represents the interest rate stated on a bond when it is issued.

The medium-term liquidity projections compiled by DMD are also used for the planning of the monthly Treasury Bills auction calendar. These projections are intended to highlight the liquidity needs for the month ahead and are used in combination with other market information to determine the maturity tenors of Treasury Bills to be offered in the money market.

The approach adopted to determine the liquidity needs was critical to enable DMD to perform strongly in carrying out its cash management function, with all related objectives achieved despite the challenges posed by the existing small domestic money market. This system helped the Directorate to provide all funding needs, covering all the expenditure, whether expected or unexpected. DMD plans to continue operate this system and continue to improve it. In collaboration with the Cash and Banking Unit of the Treasury, it shall strive to track other sources of revenue and expenditure with an acceptable degree of accuracy, to obtain a better picture of the funding needs and try to anticipate any unexpected expenditure of a certain amount.

f. Credit Risk

Credit risk is associated with non-performance by borrowers on loans or other financial assets, or by a counterparty on financial contracts. The financial transactions that arise from DMD's activities are recorded in the Consolidated Fund. The Directorate is responsible for the liabilities side of the financial transactions, which mainly involves the issuance of Government securities. The monitoring of receipts arising from investments held by Government does not fall within the remit of DMD, except for the receipt of interest from the Greece loans[32].

The Treasury does not enter into derivative contracts related to the management of risk of its debt portfolio. In this regard, risks arising from counterparties from such contracts do not arise.

g. Settlement Risk

Settlement risk relates to the possibility that counterparties do not deliver a security as agreed in a contract, after the Government has already made the payment according to the agreement. DMD encounters no such risk, since Treasury does not have any interest swap agreements or any other financial contracts directly related to the risk management of its portfolio. As a result, DMD's exposure to the delivery of a security after the payment is made is limited to a small number of transactions related to Sinking Funds. The exposure arising from these transactions does not create any risk in view of the quality of the counterparties with which such transactions are conducted. Moreover, in the case where investors who were successful at the auction and allotted Treasury Bills or MGS, fail to pay the amounts due, the Directorate will not register the investment in their name with the Malta Stock Exchange (MSE). Furthermore, the retail investors who subscribe for MGS are required to pay for the Stocks applied for with the application.

h. Operational Risk

Operational risk is the possibility of loss (financial/non-financial) resulting from inadequate or failed internal processes, people and systems, or from external events that impact Government's ability to operate its on-going business processes. DMD relies on its operational processes to execute successfully a significant number of high value transactions on a daily basis. The Directorate considers operational risks to be one of the critical areas of risks, so it ensures that its business operations are fully supported by efficient and secure systems and processes. The identification, monitoring and mitigation of operational risks is discussed with Senior Management staff and functional teams on a

[32] A financial transaction entered into by Malta as an EAMS, as part of its commitments at European level to participate in a financial support programme to the Hellenic Republic.

regular basis. Senior staff regularly monitors and reviews significant risk issues stemming from existing, as well as new business activities.

In order to ensure that reputation risks are kept to the minimum, DMD keeps a customised operational logbook, whereby the critical actions that must be taken in connection with the servicing of debt are documented by all officers involved in Debt Management operations. The main events included in this logbook include the payments of interest; any reject or partial rejects/returns which are followed up and payment issued accordingly; re-setting of interest rates of FRN; redemptions; the due dates of interest and capital repayments on all foreign loans repayments; as well as mergers and fungibility issues. Additionally, an officer working within the Operations Section continuously updates such logbook with the latest information.

Moreover, an important element in DMD's control framework to mitigate the risks arising from human errors, is the segregation of duties to ensure independent checking and reconciliation, as well as avoid concentration of key activities on individuals or small groups of staff. A case in point is the segregation of duties, which takes place between front and back office activities.

i. Fraud Risk

Fraud risk refers to the possibility of an intentional act or omission, which is committed to secure unfair or unlawful gain. In order to minimise such risk, DMD's systems and procedures include a number of functions inbound in all processes as a means of control, such as approvals and authorisations from senior staff prior to proceeding with a particular process. A number of random checks are performed throughout all processes in order to avoid as much as possible errors and other risks. Moreover, the outcome of DMD's debt issuance processes are immediately published on the Treasury's website, and are thus subject to scrutiny by external users.

When it comes to the external users, DMD performs a number of checks on the data received from third parties, including information received from Investment Services Providers. For example, when it comes to MGS issuance, the bank accounts listed on all the applications are checked for their validity. The data on all MGS applications is checked with the electronic batch forms (compiled by the selling agents) for its correctness and are further corroborated with MSE's data. Any discrepancies are highlighted and corrected.

Risk Management Framework

In 2013's AAR, NAO recommended that an implicit risk management framework was to be created and regularly updated by DMD as necessary. This will provide the necessary evidence that the structured risk plan is actually carried out. In the same AAR, DMD commented that the draft GPDMA requires the Minister for Finance to prepare a medium-term Debt Management strategy. Such strategy will set forth Government's strategic priorities that guides its borrowing policies and Debt Management operations, and seeks to achieve the objectives of public Debt Management, by assessing the range of cost and risks to the debt portfolio. The strategy, covering a time horizon of a minimum of three years, is to be approved by the Minister for Finance and shall take into account:

a. the future borrowing needs of Government;

b. the current conditions and medium-term outlook on macro-economic and market conditions;

c. macroeconomics and other shocks to which the economy is exposed; and

d. any other factors which may be related to market development and the public debt management strategy.

Upon enquiry by this Office for an update on this matter, DMD stated that due to the fact that GPDMA has not yet been enacted, the medium-term Debt Management strategy was not yet formally compiled. However, DMD officials also highlighted the fact that Government's strategic priorities, the risk management tolerances and policies were thoroughly discussed during PDMAC meetings. Various meetings were held during the year with CBM and MSE, to discuss risk management, the medium term macro-economic outlook, market conditions, including other factors which may be related to market development.

Moreover, DMD explained that it considers the management of risk related to the management of the Government debt portfolio as an integral part of a wider strategic debt management framework based on the best practices of comparable sovereign borrowers. The risk management function is a central feature of DMD. It is a fact that strategic benchmarks play a key role in the control of risk. In its function as a management tool, the benchmark requires the Government to specify its risk tolerance and other portfolio preferences concerning the trade-off between expected cost and risk. In fact, it is expected that these will be part of the official Risk Management Framework when the GPDMA is enacted.

In addition, as part of its risk management strategy, DMD implements timely corrective actions when the need arises. In order to eliminate as much as possible the risks on its portfolio, the Directorate implements a strategy whereby it limits the issuances of FRN, keeps the WAM of the MGS portfolio above seven years and limits the maturity horizon of newly issued debt in a way that does not exceed the €470 million mark in any particular year. To this end, DMD also used various analytic tools and scenarios to assess the cost-risk trade-offs of different borrowing strategies.

Furthermore, towards the end of the year 2015, DMD expressed its interest to join a Working Group formed by EAMS within the ESDM[33] to develop a set of key debt metrics to monitor and assess the evolving cost-risk characteristics of the debt structure of each of the EAMS.

In January 2016, the Working Group was officially set up specifically to discuss this matter and to develop a set of risk metrics. The Treasury, through DMD, is a member of this ESDM Risk Metrics Working Group.

Currently, member states are reporting a number of risk metrics on a quarterly basis, including:

a. Average Life;

b. Average Time to next Re-fixing;

c. Refinancing risk within one and five years (Rollover risk);

d. Re-fixing risk for one and five years (to illustrate interest rate and budgetary risks);

e. Ratio of Foreign Debt to Total Debt (before and after derivatives); and

f. Ratio of Floating Debt to Total Debt (before and after derivatives).

These debt metrics were developed to monitor and assess the evolving cost-risk characteristics of the debt structure. They also consider the objectives of debt management, evaluate and monitor the impact of decisions regarding the debt strategy with respect to a number of risks and highlight areas were corrective action may be necessary. In addition to providing information on the evolution of the debt portfolio over time, these metrics allow cross-country comparison of debt structures.

[33] Source: http://europa.eu/efc/content/about-sub-committee_en

Debt Sustainability Analysis

The Sovereign debt sustainability position within an economy depends on a number of factors which have a contrasting impact on the sovereign debt level. In this regard, the higher the initial level of debt as a proportion of the size of the economy, the riskier is the sovereign debt predicament for the economy. This is due to the fact that a higher Debt-to-GDP ratio implies that *ceteris paribus*, Government runs a higher risk of being unable to meet commitments as they become due. Such commitments involve the roll-over of maturing debt and the borrowing requirement for registered fiscal deficits.

However, the initial level of the debt position of an economy only partially determines the predicament of Government's debt sustainability position. The latter is also influenced by the inter-linkages between the interest burden, the nominal growth rate of the economy and the primary balance that is expected in the foreseeable future. In this regard, a higher interest payable on Government debt, due to a higher risk premium, or due to an increase in interest rates, leads to a more pronounced debt burden on Government and its future evolution over time. On the other hand, a higher rate of economic growth in nominal terms and a surplus in the primary balance reduce the applicable burden of the national debt and its future evolution over time.

In this regard, IMF Guidelines require public debt managers to regularly conduct stress tests of the debt portfolio on the basis of the economic and financial shocks to which the Government and the country more generally are potentially exposed.

Upon enquiry whether DMD assessed such risks, NAO was informed that the Economic and Policy Department within MFIN performs Debt Sustainability Analysis. The Departnment confirmed that the Debt Sustainability Analysis carried out during the year, presents alternative debt trajectories based on alternative GDP forecast, interest rate and primary balance, including a scenario with a call of contingent liabilities.

Monitoring of Government Debt and the Debt Portfolio

The monitoring of the Government Debt and the Debt Portfolio provides valuable information for debt sustainability, to identify any vulnerabilities arising from interest rate and refinancing risk. DMD analyses the Government debt portfolio in order to identify years were maturities in the short-term (one or two years) are too high, leading to a recommendation to PDMAC to authorise the initiation of a bond switch, and thus reduce the amount of redemptions. DMD also monitors the movement in interest rates, and any sign of an increase in interest rates will again prompt a recommendation to PDMAC. DMD also monitors investors' behaviour, both in the primary and secondary markets, as these are deemed necessary to achieve successful issuance outcomes.

Coordination with Monetary, Fiscal and Financial Sector Policies

Debt Management should be secured in sound macroeconomic and financial sector policies to ensure that the level and rate of growth in public debt are sustainable. In this regard, DMD is involved in various meetings and committees where officials from the monetary, fiscal and financial sectors are also involved.

With regards to monetary authorities, DMD communicates regularly with CBM. Preceding every issue, PDMAC is convened where *inter alia* the funding requirements and maturity profiles are discussed. Closer to the issuance, bilateral discussions between CBM and DMD are held on the pricing of the new MGS to be issued to the retail sector. Such prices take into account the prices prevailing in the secondary market that would reflect secondary market conditions.

In addition, DMD is invited by CBM to attend and participate in the Financial Markets Committee meetings, which is a forum organised and chaired by the latter that gathers all credit institutions operating in Malta. DMD is neither an official member of this Committee nor an observer. It is invited by CBM to deliver *post mortem* presentations on issued debt and to communicate other initiatives that the Directorate will embark on during the year. DMD's attendance to these invitations provides an opportunity to the Directorate and the banking community to exchange views on matters of interest to both parties.

In respect of fiscal authorities, DMD compiles the data on Government Debt published in the Budget Estimates. The data includes a list of MGS balances as at end of the following year, together with the amount of Stocks to be issued. These expected securities will be based on the budgetary projections published in the previous year, which includes a three-year budget projection, including the amount of MGS to be issued. DMD also prepares the budgetary interest expenditure for the following year, based on MGS balance and the projected new MGS to be issued, as well as Treasury Bills' take-ups. Moreover, DMD updates the BO on a monthly basis, with the interest expenditure for that particular month, together with information on the total interest expenditure *versus* the budgeted interest expense. BO is also kept updated with changes that will affect the budget plans, both in the current or forthcoming year.

In view of the financial sector policies, DMD also holds a number of meetings and discussions with MSE about developments in the local market. The latter also updates DMD with all communications issued to the market. Moreover, the Malta Financial Services Authority regularly updates DMD with developments in the financial sector that can have effect on sovereign debt.

Role in promoting efficient markets in Public Debt Instruments

The Revised Guidelines for Public Debt Management stipulate that in order to minimise cost and risk over the medium to long term, debt managers should take adequate measures to develop an efficient government securities market. An efficient market for securities provides the Government with a mechanism to finance its expenditures and borrowing needs. Moreover, by promoting the development of a deep and liquid market for its securities, debt managers, in tandem with the Central Bank, supervisors, and regulators of financial institutions, as well as market participants, can achieve lower debt servicing costs.

Thus, all market participants, including DMD, CBM, MSE, the Malta Financial Services Authority and other stakeholders must work together to promote an efficient market. Since DMD is by far the largest issuer in the local capital market, it therefore plays an important role.

The role of DMD in promoting efficient markets in public debt instruments works around the implementation of a number of principals considered to be crucial for effective market efficiency in public debt instruments. These mainly include the enhancement of transparency of strategies in debt management operations, since this principle increases credibility, accountability and predictability.

In this regard, during the first week of January, DMD publishes the indicative calendar for the year. Moreover, if it may be necessary for DMD to divert from the published indicative calendar due to changes in the market conditions, the Directorate would publish a revised indicative calendar. In 2015, due to fact that in the June issuance, the Treasury offered a stock maturing in a year other than that announced in the indicative calendar published in January 2015, a revised indicative calendar was published in May of the same year. Moreover, the results of the auctions are announced and published immediately after the closure of the auction (normally two hours after the closure of the auction). The Directorate makes extensive use of the Treasury's website to publish regularly and timely debt information, such as investors distribution, credit ratings by the main three credit rating agencies and outstanding levels of marketable debt.

DMD gives due importance to the liquidity in the secondary market for Government securities, since the secondary market liquidity is an essential feature of a well-functioning and resilient Government bond market. Given that issuance size is usually a necessary condition for a liquid market, the Directorate issues fungible Stocks to increase the size of the Stocks.

Furthermore, DMD holds regular meetings with CBM to discuss issues and trends of liquidity in the secondary market. The latter performs the market-making role for MGS. In an effort to enhance the liquidity and the efficiency of the secondary market, in 2014, the Treasury established a Sinking Fund for the purpose of the repurchase of loans raised under the Local Loans (Registered Stocks & Securities) Ordinance.

In 2015, DMD maintained contacts and held a number of consultations with a diversified set of stockholders and institutions with a view to support the development of the Government bond market, as well as domestic financial markets in general given that Government bonds play an important reference (benchmark) in the financial markets.

Relations with Stakeholders, Sovereign Credit Rating Institutions and Other Institutions

The Revised Guidelines for Public Debt Management explain that the Government is likely to benefit from a function within debt management office that deals regularly with the main debt stakeholders and produces investor-friendly reports with debt statistics and other relevant information.

The Directorate has regular contact with stakeholders. Among others these include, Treasury's selling agents, financial institutions, MSE and CBM. In the absence of a primary dealer system, DMD does not have a ready market for the sales of MGS. In this regard, it seeks to maintain a good business relationship with its selling agents in the MGS market environment, where retail investors play an important role.

To this effect, during 2015, the Treasury launched a consultation exercise with its selling agents after the first issuance was heavily oversubscribed by retail investors. Agents were asked to provide their feedback and practical suggestions on how improvements could be made to the current system of retail subscriptions. These were later discussed at the PDMAC with a view to ease the administrative burden of retail subscriptions, both on the selling agents, as well as on the operations of the Directorate.

Senior officials from DMD also meet with financial institutions to seek their views on market issues and their investment needs. Institutional investors represent an important market segment for the Directorate and it was important to keep market access to this segment of the MGS market. DMD's plan is to further involve all stakeholders prior taking any important decision that can have an effect on the market and their operations.

Moreover, in 2015, DMD participated in various meetings with Credit Rating Agencies (namely Standard and Poor's, Fitch, Moody's and DBRS), the Directorate General for Economic and Financial Affairs (DG ECFIN), as well as IMF missions. In all meetings, except for that held with DG ECFIN, DMD prepared an information document, which included a review of the results achieved in the previous year and the outlook for the year 2015, including details on the issuance strategy for such year. Meetings held with DG ECFIN focused on how the Government was going to meet the debt targets, interest rates expenditure, as well as development in the local sovereign debt market.

The Directorate also gave its input towards the annual Article IV consultation process carried out by IMF. To this effect, the Directorate together with officials from MFIN, participated in the annual meeting with officials from the IMF Mission held in November 2015. During these meetings various issues related to debt management and positions on central Government debt were discussed.

Responsibilities and Accountabilities

The operational responsibility for debt management activities of DMD is separated into Front, Middle and Back Offices with distinct functions and accountabilities, and separate reporting lines. This is in line with the best International Practices. The Front Office executes Government's debt policy regarding the issuance of securities, the Middle Office undertakes market research and analysis, while the Back Office deals with the registration, administration and settlements of central Government debt.

International Guidelines recommend that staff involved in debt management should be subject to a code-of-conduct and conflict-of-interest rules regarding the management of their personal financial affairs. In this regard, DMD confirmed that based on NAO's previous year recommendation, a draft code-of-conduct was lately approved by MFIN and will be discussed shortly with the debt management officers, with the aim of being implemented during the year 2017.

In addition, DMD pointed out that all MGS are subject to the scrutiny of all the members of PDMAC. The final decision on which stock and coupon is to be issued on the primary market is discussed and approved by PDMAC. In this regard, DMD provided to NAO a copy of the minutes of PDMAC meetings and related correspondence.

Control Environment and Activities

A system of control environment requires a framework of risk mitigation where DMD must always be in a position to transact the underlying business required to meet its remit. The Directorate's mitigation of risks actions typically include the segregation of duties and having in place different levels of approvals across different areas of activities. DMD employs clear lines of management delegation and reporting, as well as robust business continuity arrangements.

Although there are no official control checklists, as a result of the training provided over the years and their experience, DMD confirmed that its staff are well aware of the risk associated with each process and immediately alert Senior Management when they identify problems/risks prior to the introduction of new processes and during the execution of daily operational tasks.

External peer reviews of Public Debt Management

As per ISSAI 5440, one of the factors that is considered to be valuable in a public debt management arrangement, is the conduct of external peer reviews. However, upon enquiry by this Office, DMD confirmed that in 2015, no external peer reviews of its public debt management activities have taken place.

Internal Audit Function

Similar to what was reported in last year's AAR, DMD stated that even though it does not have an Internal Auditor, there are a number of functions inbound in all processes as a means of control, including authorisations from senior staff prior to proceeding with a particular process, and random checks of the work performed. Moreover, DMD stated that from time to time Senior Management reviews and monitors the internal controls and updates them where necessary, without introducing unnecessary bureaucratic procedures which may hinder the efficiency of the day-to-day operations of the Directorate.

Additionally, as with all Departments, DMD is subject to any internal audits that the Internal Audit and Investigations Department may wish to undertake, apart from external ones conducted by NAO.

Accounting, Communication and Information Technology Systems in place

All transactions in connection with MGS and Treasury Bills are recorded on DAS. As a means of control, a small number of officers within DMD have access to DAS, whilst there is one Senior Officer within the Directorate responsible for inputting all debt transactions in DAS.

DMD aims at using a transparent debt management framework supported by strong communication policy. The Directorate views transparency in its debt management operations as an enabler of credibility, accountability and predictability. DMD adopts consistent standard measures and indicators, as well as publishes the central Government debt statistics in a timely manner. Moreover, the Treasury announces and publishes all the data/information in connection with MGS and Treasury Bills on its website, and disseminates information to MSE and Investment Services Providers.

The Directorate keeps all data in respect of MGS issuance, Treasury Bills, and interest payable, on spreadsheets, which were specifically compiled to accommodate the Directorate's requirements. These templates are used to conduct MGS and Treasury Bills auctions, compile auction results and publications to the market, as well as serve as a general database for the Middle Office from which analytical reports, budgeting forecasts and plans are compiled. In this regard, the spreadsheets are central to DMD achieving its objectives for the release of accurate debt management data.

In addition, the Directorate has in place business continuity arrangements to ensure it is able to continue its market operations in the event of an internal or external incident that undermines the operations. With the support of the Information and Communications Technology Business Unit within Treasury and the Malta Information Technology Agency (MITA), there is IT recoverability of data facilities. DMD also has online access (viewing facility) to MGS Register maintained by the MSE, and to the Public Account held at the CBM.

As already recommended in the previous years' AAR, the debt management activities should be supported by a reliable, accurate and comprehensive IT management system with proper safeguards, which produces accurate debt data and ensures timely payment of debt service. The IT management system is to capture all relevant cash flows, be fully integrated with the Government's accounting system, as well as enable the management of the medium-term strategy, cash management and contingent liabilities.

Upon enquiry by this Office for an update on this issue, DMD confirmed that this will be addressed once the Corporate Financial Management System (CFMS)[34] is implemented. Any new debt reporting system to be procured by Treasury must be compatible with CFMS and thus a new system can only be procured once CFMS is fully implemented. Nevertheless, the safeguards for timely payment of the debt servicing (interest/capital repayment) depend on the close coordination among Treasury, MSE and CBM, as well as having in place an audit trail system as that adopted by Treasury to track the movements of pending processes until payment is affected. The MSE generates the interest and redemption reports through their IT infrastructure in line with the statutory provisions and existing agreement between Treasury and MSE. Upon receipt of the electronic payment file, it is referred to CBM to be uploaded in the CBM's system; the Single Euro Payments Area (SEPA),[35] for execution of payment on the due date.

Furthermore, as a result of the increase in demand from retail investors for MGS, the Treasury initiated the process to source an IT system for the subscription in MGS in the primary market in order to replace the current manual system. The move from a manual to an online system should also give Treasury more flexibility when it comes to the Debt Management strategy.

Business Recovery Procedures

A backup of all data and information held on the aforementioned spreadsheets is kept by MITA in accordance with Government policy. The IT Section within Treasury is responsible for these backups which are taken on a daily basis. Similarly, operational transactions related to the management of the Government Debt Portfolio are held and backed up on MITA servers, whilst the maintenance of the Government Securities' Register is under the responsibility of the MSE.

In addition, DMD holds a hard copy of all the applications received in respect of all Stocks issued for seven years after the maturity date of the security. This represents one year more than the Government's discharge of liability on the Stock as prescribed by the law.

[34] CFMS shall be a full-accrual accounting package that Government will be implementing as part of its move towards accrual accounting.

[35] The Single Euro Payments Area (SEPA) is where more than 500 million citizens, over 20 million businesses and European public authorities can make and receive payments in Euro under the same basic conditions, rights and obligations, regardless of their location.

Financial Aspect

Table 20 portrays the servicing cost of the central Government Debt.

Table 20: Central Government Debt Interest Expense

Description	2015	2014	Variance
	€	€	€
Local Loans:			
Treasury Bills	108,047	1,877,535	(1,769,488)
Malta Government Stock	228,158,924	224,666,766	3,492,158
Ex-Malta Drydocks/Malta Shipbuilding Co. Ltd Loan	2,246,458	2,246,458	-
Sub-Totals (Local)	**230,513,429**	**228,790,759**	**1,722,670**
Foreign Loans	1,817,317	2,305,483	(488,166)
Totals	**232,330,746**	**231,096,242**	**1,234,504**

(Source: FR 2015, pages 141-144)

During year 2015, the overall servicing cost of Government's debt totalled €232.3 million, resulting in an increase of €1.2 million over the previous year. Notwithstanding the fact that the servicing cost on local short-term debt decreased by €1.8 million, the overall servicing cost of Government's domestic debt totalled €230.5 million, resulting in an increase of €1.7 million over the prior year.

The cost of MGS amounted to €228.2 million, resulting in an increase of 1.6% over the interest paid in 2014, partly reflecting Government's allotment policy which was systematically biased towards the long-term end of the curve, and on the back of the higher outstanding levels of MGS at the end-of-year 2015. The strategy to issue MGS in the long end of the curve was intended to take advantage of the low interest rate environment and lock in at low rates for long dated Stocks, as well as satisfy the strong demand from the retail sector. In fact, this strategy has had a positive impact on the WAM of the central Government's debt portfolio. Moreover, the MGS portfolio Weighted Average Coupon (WAC)[36] as at 31 December 2015 continued to decrease to 4.56% from 4.82% a year earlier.

Finally, the servicing cost of foreign loans marked a decrease of €0.5 million over 2014, as a result of the decrease in foreign loans balances as at end-of-year 2015, including the maturity of one of the loans (United States of America Government) on 20 November 2015.

Contingent Liabilities

As already reported in 2013 and last year's AAR, risk assessment needs to be carried out by DMD prior to a Guarantee being granted in favour of the entity. Moreover, where contingent liabilities exist, information on their cost and risk aspects should be disclosed in the Public Accounts. Since it was stated in the same Report that Government Guarantees were not being managed by DMD, but resided within MFIN, this Office expressed its opinion that there should be a link between Treasury and MFIN with regards to Government Guarantees. Moreover, this Office had recommended that DMD should be properly equipped to be able to assess the risks associated with a particular guarantee before it is actually granted.

In addition, NAO also recommended that Government should monitor the risk exposures that it is entering into through its explicit contingent liabilities, and ensure that it is well informed of the associated risks of such liabilities. In such cases, DMD should not only be informed of the explicit contingent liabilities that the Government intends to undertake, but also be conscious of the conditions that could trigger such liabilities.

[36] WAC of the MGS portfolio is the weighted average gross interest rate of the outstanding MGS portfolio at a particular point in time, in this case, 31 December 2015.

Upon enquiry by this Office, during this year's analysis, DMD confirmed that up to the date of writing of this Report, there were still no updates in this regard since the new legal framework has not yet been enacted. However, DMD officials also stated that once the law is enacted, they will start planning on how DMD shall report and monitor all Government Guarantees, including those issued prior to the enactment of GPDMA.

Moreover, upon further enquiry whether such planning can commence prior to the enactment of the new law, DMD explained that considering the fact that the draft Act has not yet been referred for the Cabinet's endorsement, let alone enacted by Parliament, the Directorate is of the opinion that at this stage it is premature to start working on this area. However, the plan is that once the Cabinet endorses the Act, DMD will start working on this area, as well as on other areas related to the new legislation, such as the subsidiary law that need to be enacted and the general prospectus.

The Directorate also stated that it is aware that the Guarantee Assessment and Reviews Section (the new Section to be established within the Directorate) must have the necessary competence in the fields of risk assessment, accounting and financial, as well as other legislation, irrespective of whether it operates within the remit of DMD or outside of it. If the proposed line of action contemplated in the proposed new Debt Management legislation materialises, DMD shall take all the necessary steps to ensure that there is the necessary competence for such operations to be absorbed by the Directorate.

To this effect, DMD shall be a making an official request (via the Human Resources plan exercise) to MFIN to engage an officer (once the legislation is enacted by Parliament), who shall be responsible to assess proposals related to guarantees for the consideration of the Minister, as well as assess the financial risk for the Government stemming from the total outstanding amount in respect of all other guaranteed loans and performance guarantees.

Moreover, DMD also pointed out that MFIN conducts due diligence tests and risk analysis on the financial position and the creditworthiness of the entities requesting guarantees before a guarantee is issued. Once a guarantee is granted, the Ministry regularly reviews the financial position of the entities that benefited from the guarantee.

Cash Management

Strategy and Implementation

The latest Revised International Guidelines stipulate that there should be cost-effective cash management policies in place to enable the authorities to meet their financial and budgetary obligations as they fall due. The need for cost-effective cash management recognises that the window of opportunity to issue new securities does not necessarily match the timing of expenditures. A liquidity buffer consisting of cash, liquid financial assets, and contingent credit lines can provide flexibility in debt and cash management operations, in the event of temporary financial market disturbances.

In seeking to ensure that sufficient funds are always available to meet any net daily Government cash shortfall, DMD collaborates with the Cash and Banking Units of the Treasury to obtain timely forecasts of central Government cash flows and end-of-day account balances. The efficiency and effectiveness with which cash management operations are conducted, very much depends on having accurate, detailed and timely cash forecasts, which are communicated to DMD.

In formulating these forecasts, Treasury relies heavily on the information provided by Ministries and Departments. For this purpose, all Ministries and Departments are required to send on the first week of January, a statement of Cash Flow Projections, split on a month-by-month basis, covering a financial year (i.e. till 31 December). To streamline and secure a more reliable forecast of cash flows, major revenue earning and heavy spending Departments are required to submit their Statement every month, with revisions submitted on a weekly basis in advance.

Moreover, DMD seeks to maintain an adequate minimum balance at CBM. In this context, DMD issues Treasury Bills on a weekly basis to fine-tune any fluctuations to the cash balance at CBM. In this way, it offsets the impact on CBM's cash balance, which arises from the mismatch between the timing of receipts and payments, and at the same time ensures that adequate cash is available to meet Government's daily expenditure.

The Debt Management Directorate has also developed a spreadsheet model which forecasts Government's financing needs for a number of months ahead. Such forecasts are derived using a hybrid approach, by basing forecasts on previous years' trend of actual revenue and expenditure, whilst factoring in current budgetary forecasts of income and expenditure for the year. This will take into account foreseeable expenditure, which would be 'accurately known' well in advance, such as wages, social security benefits, interest payments and redemptions.

Close coordination between Cash and Banking Units of the Treasury and DMD is vital for the latter to take debt issuance decisions, in the context of achieving its objective, to meet Government's daily obligation in the most cost-effective manner.

Liquidity Buffer

In the unlikely event that emergency funds would be required after the Treasury Bills' auction is held, and cannot be met, either in full, or partly from CBM account, DMD can resort to transfer funds temporarily from:

a. the Sinking Funds to CBM account, and redeposited again in the former together with the interest due; and

b. other Department bank accounts held with CBM, after consultation is held with that particular Department.

Fiscal Responsibility Act

During the year 2014, Government introduced a set of major reforms in the fiscal framework, aimed at aligning Malta's fiscal law with the legal obligations in the Fiscal Compact and the relevant EU Regulations and Directives on economic governance. In fact, fiscal responsibility was enforced through Act XXVII of 2014 on 8 August of the same year. In this context, the FRA establishes the Medium-Term Budgetary Objective as defined in Council Regulation (EC) No. 1466/97, Article 2.

In summary, the FRA provides for the following:

a. Fiscal Responsibility and Objectives of Fiscal and Budgetary Policy

Government shall define and carry out its fiscal and budgetary policies according to the principles of transparency, stability, fiscal responsibility, equity, efficiency, effective management of personnel spending, as well as effective financial and asset management.

Moreover, Government should pursue its fiscal and budgetary policy objectives, in addition to formulating and executing its annual fiscal strategy, in accordance with the fiscal rules specified in the same Act.

b. Fiscal Rules

Government is to secure that both budgetary rule requirements imposed by Articles 8 and 9 of this Act, which derive from Articles 3 and 4 of the Treaty on Stability, Coordination and Governance, are complied with.

c. Monitoring of Fiscal Rules and Endorsement of Official Forecasts

There shall be an independent body to be recognised as the Malta Fiscal Advisory Council (MFAC) to perform the functions conferred or imposed on it by FRA. The Council is to monitor and at least once a year provide an assessment on whether obligations related to the requirements of the above-mentioned Treaty, are being adhered to. Moreover, MFIN must also publish the official forecasts to be used in the context of the national medium-term fiscal plan, in addition to the draft budget.

d. Budgetary Process

Each Ministry, Department, Public Sector Authority, Entity and Agency, as well as Local Council that is in receipt of a Government subvention, shall prepare a three-year rolling Business and Financial Plan, as prescribed, from time to time, by the Minister for Finance.

Fiscal Outlook and the Medium-Term Fiscal Strategy

(Source: Malta: Update of Stability Programme 2015 – 2018)

The Government's fiscal policy objective remains that of ensuring a sustainable fiscal position by gradually, but consistently reducing the fiscal imbalance, aiming to reach a balanced budget in the medium-term. Fiscal consolidation is necessary to ensure the sustainability of the Government's fiscal position, thus regaining the necessary fiscal flexibility that would spur long-term economic growth.

In this context, the medium-term fiscal strategy is consistent with both the FRA and the calendar of convergence established by the Commission for Malta. In fact, the deficit in 2015 has been reduced to 1.5% of GDP with further gradual reductions envisaged over the medium-term horizon. Moreover, the Debt-to-GDP ratio has declined to 64% of GDP in 2015.

An improvement in the primary surplus projected over the medium-term, together with positive growth prospects, sustained investor confidence, as well as an efficient and effective Debt Management strategy should ensure further improvements in the underlying debt dynamics. In this respect, the Debt-to-GDP ratio is expected to exhibit a downward trajectory and to approach the 60% target by the end of year 2018.

Furthermore, consistent with the requirements of the national fiscal rules, the Government is targeting an average structural effort of 0.65% points of GDP *per annum* which foresees the attainment of the Medium-Term Budgetary Objective in 2019.

Government Annual Report

(Source: Government Annual Report 2015 published by MFIN in June 2016)

In June 2016, MFIN published the Government's Annual Report for the year 2015, in line with Article 41 of FRA. As required in terms of Article 42(2) of the same Act, the Government's Annual Report provides information on the execution of the Budget for 2015 and compares the outcomes with the strategic objectives and priorities outlined in the fiscal strategy and the fiscal targets, as announced in the Budget for the same year. It analyses how the Government has respected the principles and rules stipulated in the FRA.

Procedures are now established for the independent assessment of macroeconomic and fiscal forecasts and the independent monitoring of compliance with fiscal rules. During the first year, the reports issued by the MFAC contained a number of different but inter-related observations and recommendations on the conduct of fiscal policy and the budgetary process, ranging from proposals on public expenditure control to pension reforms and the public debt. MFIN has taken note of many of MFAC proposals. The Ministry has also held preliminary discussions with MFAC to exchange views on these observations and further meetings are envisaged to ensure continued progress.

The Government's Annual Report also shows how the fiscal and budgetary policies in the completed budget year are in line with the Medium-Term Objective stipulated in the fiscal strategy, and provides explanations regarding any deviations in the context of the Government's European commitments, in particular the terms of the Stability and Growth Pact.

Moreover, in July 2016, MFAC published its overall assessment of the above-mentioned Government's Annual Report, in line with Article 13 of FRA. Overall, the Council considered that the 2015 Annual Report published by MFIN adequately met the requirements prescribed in Article 41 of the FRA. However, the Council drew attention to the fact that whereas the structural balance pillar and the debt criterion are explicitly referred to in the FRA, the Stability and Growth Pact specifies another principle, namely the expenditure benchmark, which must also be taken into account when assessing adjustment towards the Medium-Term Objective.

While acknowledging that the expenditure benchmark is only indirectly referred to in FRA, the Council considers the evaluation of compliance with the expenditure benchmark of importance within the context of the Stability and Growth Pact. In this respect, the Council recommended that MFIN also dedicates a specific section to the analysis of the expenditure benchmark in its Annual Report. This would ensure a more comprehensive ex-post assessment of the conduct of fiscal policy during the previous year, in the context of the Government's European commitments.

Letters of Comfort and Bank Guarantees

When a Government entity applies for a loan or overdraft facility, the banks usually request a Letter of Guarantee or Comfort as a security on such banking facilities. As a result, when MFIN receives such a request from an entity, through its respective Ministry, it takes into account Government (Guaranteed) Debt in the context of the Maastricht criteria and State Aid Regulations. With respect to the latter, such request has to be referred to the State Aid Monitoring Board for their comments and recommendations.

As detailed in MFIN's Manual of Procedure on the subject matter, prior to its approval, MFIN also takes into account aspects as to whether:

a. the purpose of the related loan involves the financing of capital programmes required to improve the operations of the entity concerned and to enhance its assets;

b. Government will be eventually financing the interest, or the interest and capital, of the loan;

c. such loan is being taken to replace another already existing loan, and whether the interest rate of the new loan will be the same, or less than the interest rate of the loan being replaced;

d. a Government bank guarantee is required in the national interest; and

e. a clear and specific loan repayment schedule is available for the purpose of eventual monitoring of such schedule, especially when, and if, a subsequent request for guarantee extension is made. Such schedule is requested by MFIN in those cases where the Entity fails to provide it when submitting its request for a guarantee in the first instance.

In the light of the above guidelines, after having assessed each request, MFIN must also consider whether any specific reason exists behind the request for a Government bank guarantee.

The Manual of Procedures, applies to the issue, extension, cancellation and compilation of data on Letters of Guarantee/Comfort. NAO carried out detailed testing to ascertain that procedures were being fully adhered to during the year under review, with no particular exceptions noted.

The position of Contingent Liabilities as at 31 December 2015, otherwise referred to as Government Debt, as reported upon in Part I of FR 2015 and comparative figures for 2014 are reproduced in *Table 21*, a breakdown of which can be found in *Table 22*.

Table 21: Contingent Liabilities

	2015	2014
	€	€
Government Guarantees:		
Local	812,171,140	889,028,146
Foreign	644,520,281	488,980,624
	1,456,691,421	1,378,008,770
Letters of Comfort	25,276,434	25,261,968
Totals	**1,481,967,855**	**1,403,270,738**

Table 22: Actual Guarantees made by Government

Beneficiary	31 Dec 2015	31 Dec 2014	Remarks
	€	€	
	-	9,114,599	A Letter of Guarantee was issued for an amount of €10,000,000 on 5 January 2009, to secure overdraft facility.
	-	20,000,000	A Letter of Guarantee was issued for this amount, on 27 November 2008, to secure temporary short-term overdraft facility.
	-	20,921,097	This Letter of Guarantee, originally issued on 9 July 2009 and amounting to €27,000,000, was issued to cover loan facility. This was cancelled during the year.
	146,673,368	149,655,249	This Guarantee secures loan taken on 22 September 2008 to part-finance the Corporation's investments in the national electricity supply system and distribution network.
	34,117,600	47,058,800	A Letter of Guarantee was issued for €50,000,000 on 9 December 2010, to secure loan facility in connection with the construction of interconnector between Malta and Sicily.
Enemalta p.l.c.	-	46,488,095	This Letter of Guarantee, originally issued on 14 December 2010 and amounting to €50,000,000, was issued to secure loan facility in connection with the construction of interconnector between Malta and Sicily. This was cancelled during the year.
	100,000,000	100,000,000	This Guarantee secures loan for €100,000,000, taken on 20 December 2010, to part-finance the construction of the interconnector between Malta and Italy.
	-	37,413,821	On 25 March 2014, a Letter of Guarantee was issued to secure loan facility of €50,000,000 in connection with Interconnector project. This was cancelled during the year.
	-	17,650,000	On 28 July 2014, a letter of Guarantee was issued to secure a loan facility of €18,900,000. This was cancelled during the year.
	-	75,000,000	On 28 July 2014, a Letter of Guarantee was issued to secure Loan Facility of €75,000,000. This was cancelled during the year.
	280,790,968	**523,301,661**	

Table 22: Actual Guarantees made by Government *cont./*

Beneficiary	31 Dec 2015	31 Dec 2014	Remarks
	€	€	
Malta Enterprise Corporation (ex Malta Development Corporation)	987,558	1,276,792	The Letters of Comfort issued to cover the Loan Guarantee Scheme taken over from the Institute for the Promotion of Small Enterprise Ltd, and the New Enterprise Loan Guarantee Scheme, were replaced by Letters of Guarantee for €2,911,717, dated 19 May 2009, and by a Letter of Guarantee dated 3 March 2010.
	2,500,000	1,503,639	Letter of Guarantee issued on 6 July 2001 to secure loan/credit facilities made available to the Corporation.
	2,036,890	1,956,741	A Letter of Guarantee issued on 21 October 1991 for the amount of €5,823,433 was reduced to €2,500,000 in 2012.
	101,680	-	On 26 February 2015, a Letter of Guarantee was issued with a local bank to secure overdraft facility of €500,000.
	1,232,473	-	On 12 August 2015, a Letter of Guarantee for €2,500,000 was issued to secure increased overdraft facility to finance soft loan schemes.
	1,710,335	-	On 3 November 2015, a Letter of Guarantee for €2,500,000 was issued with a local bank to secure increased overdraft facility to finance soft loan schemes.
	8,568,936	**4,737,172**	
Water Services Corporation	46,531,583	54,724,980	Three Letters of Guarantee issued on 30 April 2007 in connection with Loan 1 and Loan 2 facility for €31,912,416, and to secure general banking facility for €4,658,747. Another Letter of Guarantee was issued on 1 October 2008, originally for €37,269,974, to cover general banking facility.
	36,818,437	38,570,537	On 30 November 2007, WSC entered into a Guarantee agreement with a foreign bank for €40,000,000 to undertake a project concerning investments in the sector of water supply and wastewater collection and treatment.
	83,350,020	**93,295,517**	

Table 22: Actual Guarantees made by Government *cont./*

Beneficiary	31 Dec 2015	31 Dec 2014	Remarks
	€	€	
Malta Freeport Corporation Ltd	3,540	3,285	Letter of Guarantee was issued in substitution of the Letter of Guarantee covering the balance on the loans of €18,052,644.
	200,754,838	200,754,838	On 20 January 2004, Malta Freeport Corporation Ltd entered into a Currency SWAP agreement with a private company over the 2028 bonds (original denomination US$250m). This SWAP agreement is guaranteed by the Government of Malta, but does not increase the overall exposure of the Government of Malta. As a result, the currency denomination has been changed to Euro.
	-	25,977,394	On 6 March 2014, a Letter of Guarantee was issued to secure overdraft facility of US $65,000,000.
	200,758,378	**226,735,517**	
Malta Industrial Parks Ltd	15,844,552	18,178,474	Letter of Comfort issued on 31 January 2007 in connection with the development of a specialised facility at Luqa Airport leased land. This Letter of Comfort was replaced by a new one dated 10 March 2011 for €27,000,000, and again superseded on 10 July 2012.
	2,511,054	2,613,641	Letter of Comfort dated 10 March 2011 for €6,000,000 replaced a former Letter of Comfort issued on 4 February 2008 to secure loan facility in connection with capital projects. This Letter of Comfort was amended to €4,500,000 during 2012.
	10,045,647	10,441,598	A Letter of Guarantee, originally amounting to €13,000,000, was issued to secure loan facility. This was superseded by Letter of Guarantee dated 10 July 2012 for €11,650,000.
	754,811	1,005,560	A Letter of Guarantee, originally amounting to €7,500,000, was issued with a commercial bank in connection with the Medavia Project, to replace a Guarantee dated 4 March 2010 in favour of Malta Enterprise. This was superseded by a Letter of Guarantee dated 10 July 2012.
	8,059,796	6,368,471	On 9 August 2012, Letter of Guarantee was issued to secure loan facility of €12,000,000.

Table 22: Actual Guarantees made by Government *cont./*

Beneficiary	31 Dec 2015	31 Dec 2014	Remarks
	€	€	
Malta Industrial Parks Ltd	595,000	595,000	Letter of Guarantee issued on 10 July 2012 with a local bank to supersede the one issued on 12 June 2009 to cover a Bank Guarantee facility.
	1,380,774	1,427,307	Letter of Guarantee issued on 3 January 2013 with a local bank to secure loan facility of €3,000,000.
	28,526,129	29,600,000	On 5 December 2014, a Letter of Guarantee was issued for €29,600,000 to secure loan facility.
	45,640,482	47,018,126	On 24 September 2014, a Letter of Guarantee was issued to secure a loan facility of €50,000,000.
	113,358,245	**117,248,177**	
Malta Government Technology and Investment	290,318	386,336	A Letter of Comfort was issued for €1,000,000 on 12 February 2009 to secure loan facility. This was replaced by a Letter of Guarantee dated 12 March 2009 for the same amount.
Malta Government Investments Ltd	8,000,000	8,000,000	On 23 April 2014, a Letter of Guarantee was issued to secure loan facility of €15,000,000.
Foundation for Tomorrow's Schools	76,241,307	71,796,459	A Letter of Guarantee issued on 29 August 2013 to secure loan facilities for €123,200,000 in replacement of Letter of Guarantee dated 19 September 2011.
Authority for Transport in Malta	1,087,868	5,171,774	A Letter of Guarantee was issued for €11,086,270 on 11 August 2011 to replace the former Letter of Guarantee, amounting to €13,976,240, which was issued on 29 March 2010.
	5,000,000	5,000,000	On 31 January 2014, a Letter of Guarantee was issued to secure loan facility of €5,000,000 to replace Letter of Comfort of €56,000,000 dated 9 February 2011.
	6,087,868	**10,171,774**	
Grand Harbour Regeneration Corporation	2,192,972	998,192	A Letter of Comfort issued on 31 October 2012, to secure overdraft facility and finance services/works associated with the City Gate project. This Letter of Comfort was replaced by a new one dated 27 January 2015 for €2,500,000. Subsequently, this Letter of Comfort was replaced by one for €3,300,000 dated 3 March 2015.

Table 22: Actual Guarantees made by Government *cont./*

Beneficiary	31 Dec 2015	31 Dec 2014	Remarks
	€	€	
Housing Authority	-	1,437,709	A Letter of Guarantee was issued on 7 March 2007 with a local bank for €4,658,747 to secure overdraft facilities.
Public Broadcasting Services	3,030,856	3,471,661	Letter of Comfort issued on 26 September 2012 to secure loan facility up to €6,800,000, to finance investment in equipment upgrade and the development of the company's properties.
	53,656	-	A Letter of Guarantee was issued on 20 April 2015 to secure guarantee facility of €330,000.
	3,084,512	**3,471,661**	
Vault Finance Ltd	290,548,560	224,687,075	Letter of Guarantee issued on 31 December 2012 to secure loan facility for €318,500,000 and replace Enemalta Guarantees.
Electrogas Ltd	-	30,749,739	On 19 December 2014, a Letter of Guarantee was issued to secure 80% of the €110,000,000 bridge loan facility granted to Electrogas Ltd. This was cancelled during the year.
	160,273,638	-	A Letter of Guarantee was issued on 31 July 2015 to secure loan facilities with two local banks for €90,000,000, respectively.
	160,273,638	-	A Letter of Guarantee was issued on 31 July 2015 to secure loan facility with two foreign banks for €90,000,000 each, totalling €180,000,000.
	320,547,276	**30,749,739**	
Malta Investment Management Co. Ltd	1,451,495	1,253,749	On 30 April 2014, a Letter of Guarantee was issued to secure loan facility of €10,000,000.
Petromal Co. Ltd	85,000,000	85,000,000	On 27 August 2014, a Letter of Guarantee was issued to secure a loan facility of €85,000,000 to finance the takeover of Enemalta's Petroleum Division.
Enemed Ltd	1,697,000	-	Letter of Comfort was issued on 16 February 2015 in connection with a foreign exchange facility of €8,000,000.
Totals	**1,481,967,855**	**1,403,270,738**	

The above Letters of Comfort and Bank Guarantees offered to Government entities and EBU may translate into dues up to €1,481,967,855 by Government, should the companies call upon the latter to make good for their debts. This represented an increase of €78,697,117 (5.6%) over the amount reported in the previous year, which movement also represented 0.9% of GDP for 2015.

Government's exposure of €1,481,967,855 differs from that as reported by the National Statistics Office (NSO), since the latter "*... reports the Government Guaranteed Debt in line with Eurostat requirement*. *The main difference is that NSO data includes Guarantees granted by the EBUs, but exclude Government Guarantees provided to EBUs*".

Moreover, premiums received by Government during 2015, with respect to Letters of Comfort and Bank Guarantees amounted to €11,756,545, which revenue was appropriately accounted for under 'Guarantee Fees' in MFIN note.

Creditors' Analysis

In order to facilitate regular monitoring and evaluation of the implementation of the approved budget, Article 39(5) of FRA, 2014, mandates that "*Heads of Ministries, Departments, Authorities and other entities shall ensure full observance and compliance with the statutory and other reporting requirements as provided in this Act or as may be prescribed, from time to time, by the Ministry for Finance, the Treasury and/or the National Statistics Office* ...". Failure to abide by the provisions of the Act shall lead to disciplinary proceedings.

According to MF Circular No. 10/2001 - 'Government Accrual Accounting: Procedures for the Control of Debtors and Creditors', a quarterly analysis of creditors shall be submitted to the Accountant General.

Fifty-three Ministries and Departments submitted to Treasury an 'Analysis of Creditors' as at 31 December 2015, in the required accruals' template. Total creditors reported in this analysis amounted to €137,336,618 as at year-end. The opening balance as at 1 January 2015 was made up of balances submitted by 55 Ministries and Departments, with an aggregate amount of €164,602,726. The House of Representatives and Corradino Correctional Services failed to submit to Treasury the 'Analysis of Creditors' form as at year-end 2015.

At the end of the year under review, eight Ministries and Departments reported a 'Nil' creditors balance in their Return. Merely €251,317 of total creditors related to contested amounts. *Table 23* shows an ageing analysis of the remaining creditors' balances as at 31 December 2015:

Table 23: Ageing of Remaining Creditors

Days Overdue	2015		2014	
	Amount Due	Percentage	Amount Due	Percentage
	€	%	€	%
01 - 30	38,501,487	28.09	21,249,372	12.93
31 - 60	16,204,592	11.82	43,033,292	26.19
61 - 90	11,804,408	8.61	14,269,124	8.68
91 - 180	10,997,050	8.02	15,360,761	9.35
181 - 360	8,621,141	6.29	14,097,711	8.58
Over 360	50,956,623	37.17	56,325,689	34.27
Totals	**137,085,301**	**100**	**164,335,949**	**100**

Credit balances overdue by over 360 days related mainly to the Government Property Division, Mater Dei Hospital, Central Procurement and Supplies Unit, Ministry for Sustainable Development, the Environment and Climate Change, and Sir Paul Boffa Hospital, with aggregate amounts of €44,237,457, €4,776,615, €597,416, €418,715 and €412,175 respectively.

School Council Fund

The opening balance in the 2015 Statement of Revenue and Expenditure pertaining to the School Council Fund of MEDE, as reported in Part I of FR, stood at €1,037,492. This figure does not agree with the closing balance reported in the previous year of €1,047,520, by €10,028, resulting from the following:

a. Four schools failed to submit their annual return for year 2015, and "… *were taken out of the list* …" by MEDE. The aggregate balance as at 31 December 2014 in respect of these schools amounted to €14,323.

b. Another school closed its doors during year 2015, and its opening balance amounting to €1,572 was eliminated from the Statement.

c. Following review by MEDE, it transpired that "… *three schools* … ... *had the closing balance of 2014 which was not correct*.", as confirmed with balances as *per* bank statements provided by the respective schools. In aggregate, the closing balance in the 2014 FR was overstated by €1,559.

d. The figures pertaining to one of the schools were erroneously recorded twice in the previous year's Statement, resulting in an overstatement of €1,726 when compared to 2015 figures.

e. On the other hand, an additional school opened its doors in June 2014 and the amount of €9,152 was erroneously omitted in the previous year's closing balance. Nevertheless, the figure was included in the opening balance in the Statement presented in the 2015 FR.

Moreover, NAO noted a change in the 'Total Revenue' reported in FR 2015 amounting to €2,061,448, as against the balance earlier reported for the same schools in the Financial Statements, which amounted to €2,061,895. From correspondence between MEDE and Treasury, it transpired that the net difference of €447 resulted from errors in the balances reported in respect of five schools, which were later corrected accordingly.

Moving towards Accruals-based Accounting

(Source: Treasury)

Although Government is using a Cash-based System for its accounting of central government operations, accrual accounting concepts are currently in use, with such system defined as Modified Accrual Accounting (Cash-based DAS plus Accrual Accounting Templates). NSO uses the information received on the Accrual Accounting Templates from the Treasury for the compilation of ESA Government Statistics as required by Eurostat.

The Government of Malta has now adopted the strategy to prepare for the full implementation in Central Government of accrual accounting based on IPSAS. The national standards shall be based on IPSAS, but may include minor amendments to reflect local needs and requirements. In fact, the current draft versions are referred to as 'IPSAS as adopted by the Maltese Government'. In this regard, the Accounting Methodology and Compliance Unit within Treasury is promoting the introduction of Accrual Accounting throughout Government Ministries and line Departments, as a platform to provide more meaningful financial information, both for accountability and decision-making purposes. This Unit is also currently responsible for collecting and checking accrual accounting returns submitted by Government Departments on a quarterly basis.

Moreover, the Unit is also involved in ongoing communication with Government Ministries and line Departments to identify challenges, and assist in paving the way forward towards the implementation of IPSAS, which will also be accompanied by another major project, the change-over from DAS to a new CFMS.

The main reasons behind the adoption of IPSAS by the Government of Malta, include:

a. the attainment of a clearer picture of Government's financial performance and position;

b. greater transparency over the use of resources;

c. improved quality and reliability of information;

d. the possibility to assess accountability for all resources under Government's control;

e. the completeness records and therefore improved asset management; and

f. facilitate planning with respect to future funding requirements (asset maintenance and replacement), as well as repayment of liabilities.

Furthermore, in October 2015, the local IPSAS Project Board[38] approved the adoption of the Conceptual Framework for General Purpose Financial Reporting by Public Sector Entities. The framework was issued by IPSAS Board, the independent standard-setting board, which establishes accrual-based standards used for the preparation of general-purpose financial statements by governments and other public sector entities around the world.

The Conceptual Framework establishes the concepts that underpin general purpose accruals-based financial reporting. Up to the date of writing of this Report, Treasury had published six Draft IPSAS along with the relative User Guidelines, as adopted by the Maltese Government.

Good Practice

NAO is satisfied that requested documentation was available. Moreover, once again, Treasury and MFIN staff were cooperative at all times during the conduct of the audit. More importantly, NAO satisfactorily noted that most recommendations were acted upon, with corrective action being taken immediately, wherever possible.

[81] NAO representative attends in an 'observer capacity'.

Compliance Audit Opinion

Opinion on the Compliance Audits to the House of Representatives

Audit Mandate

As stipulated by Article 108(5) of the Constitution of Malta and para. 7 of the First Schedule of the Auditor General and National Audit Office Act, 1997, I am reporting on whether the audited entities, subjected to review, are in compliance with identified criteria, namely, the applicable rules and regulations, as well as the principles of sound financial management, among others.

I consider the primary users of the Annual Audit Report to be Parliament and the Public Accounts Committee.

Respective Responsibilities of the Accountant General and Accounting Officers

As determined by the Financial Administration and Audit Act, 1962, the onus for the proper discharge of financial administration rests with the Accountant General and the Accounting Officers. They are also responsible for the institution and application of such internal controls as deemed necessary, to enable the processing and recording of financial transactions to be free from material misstatement, whether due to fraud or error, and to ensure that the audited entities' operations are in accordance with the pertinent rules and regulations.

These officers are entrusted with the sound management of public funds. They are therefore to demonstrate transparency, accountability and integrity in their actions, and are to exercise good governance for the resources with which they are entrusted.

Auditor's Responsibilities

NAO's responsibility is to obtain reasonable, rather than absolute assurance as to whether statements and accounts of Government Ministries and Departments, as well as of other entities that were subject to audit, are free from material irregularity. Thus, it is not a guarantee that an audit conducted in accordance with International Standards on Auditing (ISA) will always detect non-compliance and material misstatements, arising from fraud or error.

Basis for Opinion

We conducted our compliance audits in accordance with the relevant ISAs, the applicable public sector perspective provisions, and in line with NAO's auditing practices. Regularity audits involve audit procedures to test compliance with standing rules and regulations, as well as with the principles of sound financial management, through direct testing of transactions.

The procedures selected depend on the auditors' judgement, which entails the assessment of risk, evaluation of internal controls, consideration of sensitivity of particular areas and other qualitative factors, as well as the assessment of materiality in terms of value, nature or context in which it occurs. Our audit sample is designed to provide an estimate of the level of error in the audited population. Our approach is thus not designed to gather data on the frequency of error in the population as a whole.

I have complied with independence requirements in accordance with the International Standard of Supreme Audit Institutions (ISSAI) 30 *Code of Ethics* and NAO *Code of Professional Conduct* and have fulfilled my ethical responsibilities in accordance with such codes. I have also adhered to avoidance of conflict of interest regulations as stipulated by Article 108(3c) of the Constitution of Malta and fulfilled the independence requirement in accordance with Article 108(12) of the aforementioned Constitution.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for our opinion, which only draws on conclusions upon areas that have been examined.

Opinion

Adverse opinion

Based on the audit work performed, I am of the opinion that the activities of a number of the audited entities under review were not, in all material respects, in compliance with the pertinent rules and regulations, and compliance deviations were pervasive.

In terms of para. 5(ii) of the First Schedule of the Act, I am to report that, except for instances reported upon, I received all the information and explanations required for the carrying out of my duties.

A separate audit opinion is being published dealing with the financial aspect.

Charles Deguara
Auditor General
29th November 2016

Office of the Prime Minister

Public Service Commission

Expenditure and Personal Emoluments

Background

The Public Service Commission (PSC) is an independent statutory body composed of a Chairman, Deputy Chairman and a maximum of three other members, as entrenched in Article 109 of the Constitution of Malta. The PSC Regulations (Legal Notice 32 of 1960), as well as Article 110 of the Constitution of Malta authorise the Commission to give advice and recommendations to the Honourable Prime Minister on appointments to public offices, the removal of persons from such office and the exercise of disciplinary control over public officers.

The PSC was allocated a recurrent expenditure 2015 budget of €648,000, consisting of Personal Emoluments of €526,000, and Operational and Maintenance Expenses of €122,000. The actual expenditure incurred during the year was €525,906, being €419,428 for Personal Emoluments and the remainder for Operational and Maintenance Expenses.

Audit Scope and Methodology

The main objective of the audit was to ascertain that adequate internal controls, over the procurement and payment of selected line items, were in place during the financial year under review. This exercise also aimed to ascertain the efficient administration of public funds in line with existing regulations, policies and procedures.

It was also ensured that personal emoluments for 2015 were appropriately recorded and processed according to the Public Service Management Code (PSMC) and other pertinent circulars. The adequacy of internal controls, intended to ensure accuracy and validity of salary payments, was also determined.

Targeted accounts consisted mainly of Utilities, Rent, Office Services, Professional Services, Cleaning and Improvements to Property. A sample of 28 transactions, with an aggregate value of €82,317 was selected, based on materiality and frequency of expenditure. Selected payments were traced to Local Purchase Orders (LPOs) or Letters of Acceptance (LAs), invoices and respective fiscal receipts, in order to determine whether procurement was in conformity with the Public Procurement Regulations (PPR), PSMC, applicable Finance Circulars and relevant agreements.

During the year under review, PSC made use of one vehicle for general-use purposes. Testing of the respective logbook and verifications with relative sections of the PSMC were carried out. Additionally, fuel consumption of a fully-expensed car, was verified and ensured there was compliance with limits set by MFC Circular No. 5/98 – 'Purchase and Use of Official Cars'.

Inventory

The electronic Inventory Database and 10 Room Lists forwarded for verification were checked to ensure conformity with MF Circular No. 14/99 – 'Government Accrual Accounting: Revised Inventory Control Regulations'. A physical inspection of four selected rooms was carried out by the National Audit Office (NAO).

Personal Emoluments

Emoluments in favour of 10 employees, in addition to all five Commission members[1], were selected for testing. Factors considered for sample selection included, employees in various grades, others on a reduced work schedule, as well as employees who commenced or terminated their employment during 2015.

Testing was focused on ensuring the accuracy of salaries paid to the sampled employees and Commission members, including officers' entitlement to allowances. An analysis of the daily reports extracted from the electronic Attendance Verification System (AVS) was conducted to assess whether time records, Sick Leave (SL) and Vacation Leave (VL) records, were being adequately maintained, properly authorised and that the information held was correct and reliable.

Good Practice

During testing it was noted that PSC abided by Contracts Circular No. 4/2015 – 'New Regulations regarding the Award of Services Contracts within the Public Administration', which specifies the minimum rates payable to office cleaners employed by service providers. In correspondence between PSC and a company providing cleaning services, the former drew attention to the fact that the office cleaner employed by said company was being underpaid. Following PSC's request, the cleaner's hourly rate of pay was correctly adjusted.

In addition, PSC requested the company to provide a Statement on Conditions of Employment, which was signed in February 2015. The service provider agreed to ensure good working conditions for employees working on the standing agreement with PSC and to follow pertinent employment and other legislation.

Control Issues – Expenditure

Misallocation of Expenditure

During audit testing, three Payment Vouchers (PVs) were verified under Account 2130 – 'Utilities – Electricity' and five PVs were verified under Account 2410 – 'Rent of Property'. Out of these, two payments, relating to condominium expenses, were noted to have been erroneously accounted for in these accounts, on the basis that expenses did not relate in their entirety to the nature of the aforementioned accounts.

[1] Annual salary of the Commission members, as stipulated in the Schedule to Article 3 of LN 6 of 2013, was complied with.

Other Shortcomings

Whilst conducting audit testing, NAO noted the following:

a. In 25 of the payments tested, the alignment of the printed PV was not correct, and as a consequence, the date indicating when the document was issued was left out. However, PVs were still being signed and dated manually by the respective officer.

b. Another LA in respect of rent for the period ranging from August to October 2015, and amounting to €15,000, was not signed by the respective officer.

Logbook lacking necessary Details regarding Fuel Intake

Trips carried out by the only general-use vehicle in use during the year under review, were recorded on a logbook and forwarded for verification. NAO noted that all the trips were certified.

However, no details as regards fuel intake were recorded on the logbook as required by the PSMC. Certain information, such as amount of litres taken and the respective fuel requisition note numbers, were missing.

Compliance Issues – Expenditure

Shortcomings related to Inventory

a. Items not included in Inventory Database and/or Room Lists

Details regarding computer sets (laptops, monitors and central processing units) were analysed against information featuring in the Inventory Database and respective Room Lists. It was noted that the Inventory Database did not feature any of these computer sets.

Moreover, while carrying out the physical inspection, seven computer sets which were located in different rooms, were not traced to the respective Room Lists. This was brought to the attention of the officer in charge of inventory, who confirmed that since these assets were recorded in Malta Information Technology Agency's inventory and bore its identification numbers, PSC did not consider it necessary to record them in their inventory. However, NAO was informed that action has been taken to rectify the matter.

b. Discrepancies related to Assets traced on Site

While conducting the physical verification, various discrepancies were noted, between information as *per* Room List and what was actually traced on site, such as different Asset Identification Number, no physical marking on asset and an asset with a different brand name.

c. Differences between Inventory Database, Room Lists and Assets traced on Site

Other differences were noted between the information according to the Inventory Database against Room Lists and assets traced on site. Typical examples included an asset traced in a different location and the asset number quoted on the Room List and affixed to the asset differing from that as *per* database.

Non-submission of VAT Defaulters Quarterly Returns

During the course of the audit, NAO noted that all PVs verified in the audit sample, were duly accompanied by the respective fiscal receipt. However, 'Nil' Returns were not being submitted to the Value Added Tax (VAT) Department on a quarterly basis, as required by MF Circular No. 5/2002 – 'Submission of Fiscal Receipts to Government Departments' and subsequent update MFEI Circular No. 2/2012. This was brought to the attention of PSC and immediate action was taken, whereby Management contacted the VAT Department in order to start complying with the respective MF Circular as from 2016.

Control Issues – Personal Emoluments

Background

The employees at PSC make use of an AVS in order to record their daily time records. The system in use only records attendances. Therefore, absenteeism in respect of VL, SL, Time Off *In Lieu* or similar, is still recorded manually. In fact, the Commission still makes use of VL and SL record forms, with daily reports being certified by a responsible officer.

Weaknesses related to the upkeep of the Daily Reports

a. Discrepancies between Vacation Leave Record Forms and Daily Reports

Out of the sample tested, VL record forms of seven officers, did not always tally with the daily reports extracted from AVS. Nonetheless, the majority of these daily reports were endorsed by the officer in charge.

b. 'Day Off' not recorded on Daily Reports

The daily reports relating to one pay period of an employee on a reduced timetable, spread on four working days, were verified to ascertain that such officer's 'day off' was duly recorded on these reports. However, on three instances, no remarks were noted on the respective daily reports indicating that this particular officer was not on duty.

c. Uncertified and/or Undated Daily Reports

Since the daily reports issued through AVS are amended manually in order to reflect absenteeism and other staff movement, all these reports pertaining to 2015 were verified so as to ensure that these have been checked and certified by the responsible officer.

While conducting this testing, it was noted that, on various instances, the daily reports were either not signed and/or not dated.

Shortcomings in the Vacation Leave Record Forms

a. Approval of Vacation Leave not dated

- All VL utilised by three officers during 2015, was duly authorised by a superior official, however such authorisation was not dated.
- Thirty-three hours of VL relating to one employee, availed of between July and December 2015, were duly authorised, however they lacked the date of such approval.
- Similarly, five hours VL (equivalent to one working day) utilised by a different officer were also authorised but not dated. On another instance, even though two hours VL availed of on another day by the employee in question was properly authorised, such approval lacked the date.

b. Unauthorised Vacation Leave

No evidence of authorisation was traced on the VL record form of one employee in respect of a total of 24 hours VL which was utilised during September 2015.

c. Incorrect Computation of Vacation Leave

Following the review of VL utilised during 2015 by an officer, it transpired that the balance as at year-end was inaccurately calculated. This employee had a remaining balance of 143.5 hours, however 64.5 hours were erroneously forwarded to the year 2016.

According to PSMC Section 4.2.4, such officer was entitled to carry forward 50% of her leave entitlement. Therefore, the correct amount of hours carried forward to 2016, should have been 96, thus leading to an understatement of 31.5 hours.

Sick Leave Record Form not updated

While verifying that all SL taken by an employee during 2015 was substantiated with the respective medical certificates, it transpired that on two days, the officer was on SL and presented the relevant medical certificate. Notwithstanding that the daily reports pertaining to the aforementioned dates reflected such absenteeism, these two days were not duly recorded on the SL record form.

Recommendations

Control Issues – Expenditure

Misallocation of Expenditure

The PSC is recommended to allocate payments in the appropriate account, which is most related to the expense concerned, so that the actual expenditure reported will reflect a more realistic portrayal of costs. The PSC may consider opening a new account relating to condominium expenses, if need be.

Other Shortcomings

Management is to ensure that no information is missing from the PVs and all the necessary details are clearly shown, thus ensuring a proper audit trail. All PVs and LPOs/LAs should always be clearly endorsed by means of a signature accompanied by a date, in order to indicate the responsible officer authorising the purchase and payment accordingly.

Logbook lacking necessary Details regarding Fuel Intake

Full details regarding fuel intake are to be clearly recorded on the logbook as required by PSMC Appendix 8.I, as a means to verify the vehicle's fuel consumption.

Compliance Issues – Expenditure

Shortcomings related to Inventory

As stated in MF Circular No. 14/99, "*Each item shall be physically marked with a consecutive identification number*." This procedure is expected to be adhered to, and items are to be physically marked with a permanent identification number, as far as it is practicable.

All assets are to be recorded accurately within the Inventory Database. These are to be adequately identifiable and traced to the respective location. Room Lists are also to be updated to reflect latest movements. Both the Inventory Database and Room Lists should contain the same information, and any discrepancies resolved.

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

Non-submission of VAT Defaulters Quarterly Returns

Returns with details of defaulters, including any 'Nil' Returns, are to be submitted to the VAT Department on a quarterly basis, as required by the respective circular.

Control Issues – Personal Emoluments

Weaknesses related to the upkeep of the Daily Reports

Adequate regular reconciliations between the daily reports and the related records, should be carried out to ensure correctness of details. This enables any variations to be tackled in a timely manner. Moreover, PSC is to ensure that all employees clock in and out every time they leave/return to the place of work, for whatever reason.

When endorsing attendance records, Management is assuming responsibility that these are correct in every detail, and that all officers falling under its responsibility have been duly accounted for. Furthermore, since the daily reports are being used in order to reflect the actual attendance of the employees, these should be certified to ensure completeness and accuracy of the reported timings. Certification should bear a date in order to ascertain that this has been carried out in a timely manner.

Shortcomings in the Vacation Leave Record Forms

It is recommended that for control purposes, all VL approvals should carry the date of such approval. Moreover, Management is encouraged to maintain accurate VL records by carrying out regular checks, in order to avoid as many discrepancies as possible.

Sick Leave Record Form not updated

Since SL record form is updated manually, more care is to be placed when recording such information.

Management Comments

In its reply, Management fully concurred with NAO's reviews and comments and confirmed that all recommendations have been fully considered and adopted.

Management also highlighted the facts that:

- PSC had moved to its new offices in November 2014. The relocation brought about a meticulous and concerted process where procurement and the upkeep of the inventory mattered; and
- AVS was introduced in year 2015 and that during the first couple of weeks they encountered some difficulties, which however, were resolved later on.

Ministry for Education and Employment

Free Childcare Scheme

Background

The Free Childcare Scheme is a measure introduced by Government in April 2014, aimed at facilitating women's return to employment by providing children aged between three months and three years with good quality childcare. Thus, it is specifically intended for those children whose parents[1] are either both in employment and paying social security contributions, or are in education, following a course leading to a recognised diploma or degree.

Free childcare services, covered by public-private partnership agreements between the Government and childcare centres, are offered at both public and private childcare centres, comprising 92 registered bodies as at March 2016.

For 2014 and 2015, Government paid the childcare service providers the rate of €3 per hour per child, to cover all staff costs and consumables, including stationery; as from 1 January 2016 this rate was increased to €3.05.

Entitlement to free childcare is based on the monthly working hours of the mother, and includes an additional 10% of the same hours for unforeseen exigencies as well as another 20 hours per month for commuting. Parents in education are entitled to 20 and 40 hours per week for part-time and full-time courses respectively. If parents consume more hours than those entitled to, they will be personally liable to pay the childcare centres for the extra hours at the service provider's rate.

The applicable terms and conditions stipulate that Government will automatically pay the childcare centres all of the booked hours for the month if a child attends between 90% and 110% of the said hours. If attendance is less than 90%, the booked hours will still be paid in full, but the difference will be deducted from the child's absence entitlement, calculated as 15% of the annual booked hours. Once the yearly absence entitlement is exhausted, the centre will only be paid for the actual attendance of that child. Childcare centres are not paid for those hours, in respect of which they are informed by parents, at least one month in advance, that they will not be making use of the service.

[1] 'Parents' throughout the Report represents parents and/or guardians.

Systems Overview

From its inception, *i.e.* April 2014, up to 31 December 2015, the administration of the Scheme was manually based, supported by the use of spreadsheets created specifically for this purpose by the Malta Information Technology Agency (MITA). The only data reflecting the attendance was inputted manually by the childcare centres, in spreadsheets, which were then forwarded to the Ministry for Education and Employment (MEDE). No other documentation was available at the Ministry to confirm, or otherwise, the correctness of the said hours. Payments were computed by MEDE through formulae embedded in the spreadsheet, on the basis of the times inputted therein. The vetting of applications and changes in booked hours as notified by the respective childcare centre, verifications of the monthly records submitted by the latter, as well as the computation of payments to the service provider, amongst others, fell under the responsibility of the Department of School Resources within MEDE.

As from 1 January 2016, following a public call for tender, a fully automated system, referred to as the Childcare Information System (CIS), was implemented, intended to strengthen the internal controls and curb the possibility of abuse prevailing under the manual system. The CIS, which went live in all the childcare centres with effect from January 2016, enables electronic fobbing, providing a log of the child's name, as well as the time of arrival and departure, allowing the database to automatically calculate the attendance and duration of children at the centres, together with the related payment.

Application and Attendance Records

Completed application forms, together with the requested documentation, are presented by the parents to their preferred childcare centre. Up to 30 November 2015, the latter forwarded hard or scanned copies of these records to MEDE for the relevant approval. Once the application was accepted, the centres submitted, on a monthly basis, the respective spreadsheet indicating the daily time-in and time-out of children, filled in by the same centres.

Since 1 December 2015, the data on the applications is being keyed into CIS by the centres, with the other supporting documentation, such as employment declarations and payslips being uploaded, allowing MEDE to vet and approve the applications online, for services commencing from January 2016. Following acceptance of the application, the centre provides the parents of the child with two key fobs, and records the latter's unique numbers in CIS, immediately reflecting them as 'In Use'. All accepted applications will be activated during the automatic End-of-Month (EoM) procedure, and will come into force as from the indicated start date. The daily time-in and time-out scans are saved in the database and will only be converted into proper attendance records during the EoM run. Centres can, prior to the said procedure, go through the scans and correct any erroneous records by manual input or by marking the entries as 'ignored'. In the latter case, such entries will not be included in the EoM report. Every EoM run also generates the respective payment for each childcare centre, creating a specific payment file, which file is then downloaded by MEDE and transmitted to the Central Bank of Malta through secure email.

Payments

Payments to childcare centres are issued on a monthly basis. These are based on the number of booked hours for the month, except for the two instances highlighted earlier on under 'Background', *i.e.* where the child attends more than the booked hours (up to 10% more), or where the absence entitlement is exhausted, in which cases payment is based on actual attendance.

Changes to Booked Hours

According to standing policies, changes to booked hours are to be communicated by the parents to the childcare centres at least one month in advance. The centre will then inform MEDE of the requested change and hours will be increased or decreased accordingly. During 2015, the latter were being informed through an email, but since the official introduction of the CIS, a Change Request for Booked Hours is generated. Once approved by MEDE, the change is reflected in the EoM run, wherein the amended hours are activated. The parents are not required to provide any confirmation of such a request to MEDE.

Financial Information

The Scheme started with a budgeted provision of €3.8 million in 2014, increasing to €8 million in 2015 and €11 million in 2016.

Tables 1 and *2* show the budget and expenditure incurred over the said period, as well as the average number of children who took up the Scheme, and the average number of service providers.

Table 1: Financial Analysis

Period	Original Budget for the Year	Warrant	Virement	Total Funds available	Amount paid during the Period	Difference between Amount paid and Budgeted Expenditure
	€	€	€	€	€	
2014 Apr-Dec	3,800,000	1,582,000	540	5,382,540	5,316,778	40%
2015 Jan-Dec	8,000,000	3,162,771	–	11,162,771	11,152,442	39%
2016 Jan-Dec	11,000,000	–	–	–	Data not yet available	

An exercise carried out by the National Audit Office (NAO) with respect to account 57045703, namely 'Grants - To Non-Government Institutions – Childcare for All', revealed that in 2015, out of the net expenditure of €11,087,662, the direct cost related to the children's attendance amounted to €9,987,830, covering a total of 3,329,277 hours. The remaining balance mainly relates to the cash injection paid out to every childcare centre as per clause 4 of the terms and conditions but which was still being advanced on a yearly basis, the payments to the system provider and to MITA, as well as adjustments related to the previous year.

Service Users and Service Providers

Both children and childcare centres have been on the increase since the inception of the Scheme, as shown in *Table 2*.

Table 2: Average Number of Children enrolled in the Scheme

	2014 Apr-Dec	2015 Jan-Dec	2016 Jan-Apr
Average number of children	2,337	2,700	2,842
Average number of childcare centres	72	83	91
Total booked hours	1,874,008	3,433,382	1,279,973
Average number of booked hours per child per month	89.10	105.97	112.59

Audit Scope and Methodology

The aim of the audit was to assess the level of internal controls prevailing in the implementation of the Scheme, and to determine whether day-to-day operations reflect efficient administration of public funds, in line with standing terms, conditions and regulations. Another objective of the audit was to obtain reasonable assurance that payments effected are accurate, duly covered by supporting documentation enabling verification, and in line with the set terms and conditions.

The audit was originally intended to cover financial year 2015. However, in view of the implementation of the new system, as indicated above, testing was extended to cover also the first four months of 2016, in order to assess whether the risks associated with the manual system have been addressed.

A total of 10 childcare centres were selected for audit purposes, as indicated in *Table 3*.

Table 3: Audit Testing

Name of Childcare Centre	Reviewed Applications	Carried Out Physical Inspection
A	Yes	Yes
B	No	Yes
C	Yes	Yes
D	No	Yes
E	No	Yes
F	Yes	Yes
G	No	Yes
H	Yes	Yes
I	Yes	No
J	Yes	No

Limitation on Scope of Audit

Payments to childcare centres were based on attendance records provided by the same centres (2015) and fob records (2016). Given the lack of supporting documentation, the former could not be independently verified by NAO auditors. Moreover, due to the serious shortcomings detected with respect to the fob records, as explained further down, NAO feels that the present system still does not give the comfort that records cannot be manipulated. In view of this, correctness of payments could not be verified.

Copies of the demand for payment, raised by the centres to parents in respect of invoiced absence, were not available at MEDE. As a result, it could not be ascertained that the centres are not billing parents for hours that they have been paid for by the Ministry.

Despite the parents' signature on the application forms, instances were encountered where the hours required were often compiled by the childcare centre representative. In such cases, it could not be ascertained that the hours applied for truly reflect the needs of the beneficiaries.

Similarly, given that no evidence originating from the parents was traced with respect to changes in the monthly booked hours, it could not be determined whether such requests actually originated from the respective parents.

Disclaimer

Since no audit procedures could be performed to assess the correctness and reliability of attendance as recorded for 2015, and also because of the way such data was captured, certain testing was only based on the entries recorded in CIS for the period January to April 2016. However, even in this case, despite being automated, the data provided could still not be sorted on the basis of the time. As a result, the auditors had to scan the entries one by one to carry out audit testing. Thus, given the vast amount of records, it cannot be ascertained that the observations identified are exhaustive.

Furthermore, it was not possible to carry out audit testing across all entities to identify duplication of the children's name under different centres during the same periods. This was due to the voluminous data in the form of individual password protected spreadsheets used for the recording of 2015 attendance by childcare centres, as well as time constraints. As a result, instances highlighted under Key Issues observation 'Full Reliance on Information provided by Service Providers – Transfers' were only identified incidentally, and the risk that these were not isolated cases cannot be ignored.

Key Issues

Inadequate Internal Controls

Testing carried out revealed that MEDE was relying completely on information provided by the childcare centres and payments were issued solely based on such information, without having in place effective safeguards. The weak control environment was also evident in the absence of communication between MEDE and the Department for Social Welfare Standards (DSWS), the latter being the responsible regulatory body, whose functions include the issuance of the compliance certificates to the childcare centres. Another area evidencing lack of control was the non-observance of the pre-established terms and conditions. These observations will be discussed in more detail further down in the Report.

Budget versus Actual Expenditure

a. Since the Scheme involves free childcare for all, there can be no capping in place on the number of children who could participate. As a result, the budget is presumably based on estimates of expected demand. To this effect, during both 2014 and 2015, the actual expenditure incurred exceeded the original budgets by 40% and 39% respectively as already indicated in *Table 1*.

b. The average number of children taking up the Scheme between April and December[2] 2015 increased by 20% over the same period in the prior year. On the other hand, a relatively higher increase of

[2] The period April to December 2015 was selected for comparison purposes.

43%[3] was registered in the booked hours for the same nine-months. *Table 4* refers. This escalation in booked hours, partly influenced by the lack of control measures by MEDE, contributed significantly to the increase of €5,835,664 in the net expenditure. Moreover, since booked hours, are not covered by independent records, as highlighted under 'Limitation on Scope of Audit', and explained further below, under Key Issues observation titled 'Full Reliance on Information provided by Service Providers – Changes to Booked Hours', the validity of such increases, and hence correctness of related payments, could not be verified and confirmed.

Table 4: Statistics

	2014 Apr-Dec	2015 Apr-Dec	Difference
Average number of childcare centres	72	85	18%
Average number of total children per month	2,337	2,800	20%
Total booked hours as collated from MEDE's manual spreadsheets[3]	1,874,008	2,687,687	43%

Lack of Human Resources

Despite the magnitude of the Scheme, with an average of 83 childcare centres and 2,700 children per month, in 2015, only one officer was dedicated full-time to the management of the childcare system, with the other two having other duties, in addition to those related to the Scheme.

Lack of human resources in the early implementation stages of such a challenging project may have long-term consequences upon its overall effectiveness and sustainability.

Full Reliance on Information provided by Service Providers

Due to the limited human resources involved in the administration of the Scheme, no independent checks were being carried out to ensure that information submitted by the childcare centres is correct, or that the intended controls associated with the key fobs were effective. As a result, payments were based entirely on attendance records as drawn up and fob records, with various shortcomings being detected during the audit, particularly related to the latter. In addition to the limitations highlighted under 'Limitation on Scope of Audit', the following concerns were also noted:

a. Applications

Regular instances were encountered where the number of hours of childcare required were either recorded on the application by the childcare centres' representatives themselves or amended by the latter. Despite that this was very evident in two particular childcare centres in the audit sample, no questions were raised to this effect by MEDE up to time of audit. Instances were also noted where correction fluid was used to amend the required hours on the applications. Independent confirmation was not obtained from the parents about the actual number of hours required; thus, NAO auditors were not in a position to validate the said hours.

b. Changes to Booked Hours

Up to December 2015, changes to booked hours, which at times involved significant increases, were only covered by an email from the childcare centre to MEDE. As from January 2016, an online change

[3] Given that MEDE did not have readily available totals of the number of booked and actual hours utilised in 2014 and 2015, the booked hours, collected by NAO from the manual spreadsheets, were used.

request started being generated by the centres. However, still no other evidence was available to confirm that such demands were actually emanating from the parents.

c. Terminations and Temporary Breaks

According to the terms and conditions, service providers will not be paid for days for which parents advise at least one month in advance that they will not be making use of the service. However, the parents inform just the centres of such intention. Thus, MEDE will only stop the payment if the centres relay the message.

Similarly, the Ministry is not informed directly by the parents in case of early termination, but the notification is received from the service provider. Furthermore, there is no supporting documentation to corroborate such occurrence in order to ensure that the respective payments are correct. Should the centres fail to inform MEDE, payments will still be issued, as highlighted in the observation hereafter.

d. Transfers

From the sample reviewed, it transpired that for the period November 2015 to January 2016, a childcare centre was paid by MEDE the total sum of €2,534 for two siblings who were, during the same period, being recorded as present at two different centres. Hence, the Ministry was paying both centres for the same children and for the same period.

Another centre was also paid the total amount of €4,380 over the period July to December 2015, in respect of two separate children who were recorded with two different childcare centres during the period in question.

This latter case was eventually detected by MEDE in December 2015 during the installation phase of the fob readers. To this effect, January payment was withheld from the centre concerned. However, although MEDE was considering further action to recoup the money overpaid, messages left on the social media indicate that the owner, who is a foreigner, has since left the island.

The above indicate a shift of control from MEDE to the centres. Thus, given that the accuracy of payments depends on the reliability and trustworthiness of the aforementioned records, their correctness could not be validated by NAO auditors.

Furthermore, since the service providers were enjoying significant control, evidence collected during the audit confirms that in certain cases records were being manipulated. This resulted in inflated payments since MEDE was relying completely on the records provided by the centres.

Ineffective Control through the New Fobbing System

CIS was specifically custom designed to cater for the particular needs of the Free Childcare Scheme. This system, which cost €246,706, excluding other modification costs, was intended to provide an electronic attendance of the children, which is recorded by the parents through a device on arrival on the premises and respective departure. For this reason, childcare centres were provided with a number of key fobs, based on the registered children as at November 2015, to hand out two free fobs to the parents of each child. Additional fobs may be acquired by the centres from MEDE, at the same trivial price paid by the latter for their acquisition. These are then sold to the parents at the same price. Once a fob is handed out to parents, the centre records its unique number in CIS.

a. The only records kept by MEDE in relation to the extra fobs were the requests by the centres and the respective payments. Since centre representatives were not obliged to keep any evidence of the actual requests, NAO auditors could not ascertain that any additional fobs 'in use' were actually requested by the parents, and were really being used by them.

b. Surprise inspections carried out by NAO auditors at eight childcare centres, revealed that at least in two centres, fobs 'in use' were being kept by the respective centre. When asked for an explanation as to why such fob was not retained by the parent, auditors were verbally told that it was the parents who opted to leave the fob there, to be used in case theirs was forgotten. However, auditors could not establish whether this fob was one of the two fobs handed to the parents, or any other fob which the centre was keeping. Moreover, it could not be ascertained who is actually using the fobs to record the attendance.

c. Verifications showed that the number of active fobs linked to each child ranged from one to seven. In the case of 33 children with one fob, this is in breach of the provisions of the respective manual.

d. Extra fobs were being sold to childcare centres at the same price that MEDE had purchased them. However, despite the intention to have a uniform price set for all centres, MEDE could not ensure that parents were actually being charged the same price.

e. Daily fob scans are only converted into actual attendance records, showing in and out times, when the EoM procedure is run. Prior to the said procedure, childcare centres may simulate part of this run, in order to see how the final records will be reflected and they can also amend such records through corresponding manual entries. Although the system provides an audit trail, including the reason for the manual entry, justification for such entries could not be independently verified. Amongst others, reasons for such manual entries included 'forgot to fob' and 'mother didn't know she had to fob'.

The lack of control over the key fobs, as well as the easy access to purchase such device in view of its cheap cost, hinders the effectiveness of the overall control element embedded in the system, and consequently the reliability of records and validity of the respective payments.

Abuse of the System and Tampering of Records by Childcare Centres

While the introduction of the fobbing system was meant to cater for all the risks mentioned above, especially the tampering of records, because of MEDE's lack of control over the fobs, coupled with an inadequate risk assessment, the intended controls were significantly impaired. The following relate:

a. 'Ignored' Entries

The system allows centre representatives to mark entries as 'ignored'. Such records will have their status changed and will be excluded from the attendance in the EoM procedure. This feature was intended to enable centres to correct erroneous records arising particularly from multiple scans, mainly due to prolonged contact of the fob with the fob reader[4].

On analysing all the 8,631 'ignored' entries recorded by the centres, in the two sampled periods, namely 4 to 15 January and 18 to 29 April 2016, the following issues were revealed:

i. In 87 instances spread over 28 centres, particularly in the period 4 to 15 January 2016, entries were marked as 'ignored' and replaced by another record. In 29% of such cases the new entries were recorded with a different fob number, which increased the duration and consequently the payment. Given the prevailing issues as already highlighted, no practicable audit procedures could be performed to ascertain correctness of the entries recorded, as well as the respective payments, and to confirm that no abuse was taking place.

[4] Refer to observation under Control Issues 'No Effective Checks by the Ministry on the Data submitted – Incorrect Fob Records'.

ii. During the sampled period, on 23 instances, 11 centres recorded manual entries, highlighting amongst other reasons that parents forgot to fob. However, such entries were very often followed or preceded by a fob record, eventually leading to one of the entries being marked as 'ignored'. This highlights the possibility that entries were being recorded manually, without using the fob, before the child actually turned up at the centre. Moreover, there is the risk that the reason indicated to justify the manual records is fabricated.

iii. Thirty-two anomalous instances pertaining to 13 childcare centres were noted in the reviewed period, whereby all the fob entries for the day were marked as 'ignored' without any explanation.

b. Physical Inspections by NAO Officers at Childcare Centres

Physical inspections carried out by NAO auditors at eight different childcare centres confirmed that, despite the introduction of the electronic system, attendance records were still being tampered with by certain centres, resulting in overpayments. The on-site visits revealed that a number of childcare centres were using the fobs themselves to record the children's attendance. However, it could not be confirmed whether the fob used was one of the two that should have been forwarded to the parents, or any other extra fobs kept by the centre. The following relate:

Childcare Centre 'A' - 2 February 2016 at 14:15 hrs

During the inspection, carried out at 14:15 hours, 13 children were present, of which four were not part of the Scheme. The centre's manager indicated the names of the children, and stated that only one fob was provided to the parents, confirming that the other one was kept by the centre.

On 3 February 2016, *i.e.* the day following the visit, NAO obtained from MEDE, a copy of the attendance record issued from CIS for the previous day. It transpired that:

i. Between 14:21 and 14:26, *i.e.*, as soon as the audit visit was concluded, a total of 11 children were fobbed out. None of these 11 children were present at the centre when the visit took place. This implies that the fob held by the centre's manager was used to fob out these children.

ii. In the case of eight children from the 11 indicated above, the fob used to record the 'Out' entry was the same one used for the 'In' fob. Since the device used to fob 'In' was not the one held by the parents but the one that was retained by the centre, this could imply that the said children did not turn up at all on the respective date.

iii. *Table 5* indicates four children, included in the attendance sheet provided on 3 February 2016 for the previous day, one of which, namely Child 1, was present during the on-the-spot inspection while the others were not. However, records for these children only show the 'In' time for 2 February 2016, without a corresponding 'Out' time.

Table 5: Attendance shows Children's Time 'In' but not 'Out'

Name	Time-In
Child 1	06:47
Child 2	08:15
Child 3	08:25
Child 4	08:25

As a result, none of these entries were included in the final attendance record for the month, following the EoM run, provided by MEDE on 14 April 2016.

iv. Two other children were marked as 'Out' at 11:13 and 12:34 respectively. However, both were still present at time of visit, *i.e.* 14:15.

Childcare Centre 'B' - 25 January 2016 between 10:45 hrs – 11:15 hrs

During the inspection 38 children were present, of which one was not part of the Scheme.

i. Two children were both included as present in the EoM attendance record. However, none of the children were traced during the physical inspection carried out by NAO auditors, despite that according to the time recorded, as shown in *Table 6*, they should have been present at the centre.

Table 6: Children not present during Inspection but featured as present in Attendance Records

Name	Time-In	Time-Out
Child 1	08:27	16:34
Child 2[5]	08:32	14:51

ii. In contrast to the above, a child was present at the centre during the inspection. However, on the attendance records he was marked as 07:51 'In' and 08:31 'Out'. On the other hand, the timings of another child were not included in the attendance records obtained on the day, despite that she was at the centre, but only featured in the final record.

iii. A difference between the timings included in the attendance record obtained from MEDE after the visit, and the final record generated after the EoM run, was noted with respect to five other children. Although all, except for one (Child 2 in *Tables 6* and *7*), were present during the inspection, the records provided could not be validated due to their inconsistency. *Table 7* refers.

Table 7: Difference in Timings between Attendance on Day of Inspection and End-of-Month Attendance Report

Name	Fobbing as per Attendance Record obtained on 25 Jan 2016	Fobbing as per Final Attendance following End-of-Month run
Child 1	08:32 – 11:14	08:32 – 14:51
Child 2	08:32 – 11:14	08:32 – 14:51
Child 3	08:27 – 09:43	08:27 – 14:10
Child 4	08:26 – 08:39	08:26 – 15:40
Child 5	08:27 – 09:48	08:27 – 15:03

iv. Three different fob timings, namely 08:32, 09:52 and 11:14, were traced for another child in the attendance for the day of the inspection, which the system automatically allocated as 'In', 'Out' and 'Error'. However, when verifying with the EoM final record, it transpired that the 'In' and 'Out' timings were shown as 11:14 and 17:18 respectively, despite that the child was present during the audit visit, *i.e.* at 10:45.

[5] On the attendance report issued for 25 January 2016, the time-out was marked as 11:14.

Childcare Centre 'C' - 26 January 2016 at 10:30 hrs

During the inspection 37 children were present, of which three were not part of the Scheme.

i. The centre had the fobs with the children's names on display. When asked as to why the centre kept such fobs, the representative verbally claimed that parents opted to leave them there to be used in case they forgot their own. In view of this, it could not be ascertained whether the parents are themselves actually fobbing the 'In' and 'Out' times of their children.

ii. One child, was traced in the final attendance record on which payment was based, but she was not listed in the record provided by the centre's representative during the visit.

Childcare Centre 'D' - 27 January 2016 at 10:15 hrs

During the inspection 87 children were present, of which 19 were not part of the Scheme.

Two children, who according to the attendance record should have been at the centre at the time of the visit, were not present.

Childcare Centre 'E' - 19 February 2016 at 09:45 hrs

During the inspection 52 children were present, of which five were not part of the Scheme.

i. One child was included in the attendance sheet, reportedly being at the centre between 07:45 and 14:51. However, as at the time of the visit, the said child was not present.

ii. In contrast, another child was present at the centre, but she was not included in the attendance record.

Childcare Centre 'F' - 19 February 2016 at 10:15 hrs

During the inspection 54 children were present, of which five were not part of the Scheme.

i. A child marked as present in the final attendance record, with 'In' and 'Out' timings of 07:35 and 14:10, was not present at the centre during the visit.

ii. An attendance extract, provided by the centre's representatives during the visit, did not reflect all the children who were actually present. It transpired that four children, who arrived at the centre between 06:28 and 08:45, were not included in this list but were included in the final attendance record which presumably was adjusted later. *Table 8* refers.

Childcare Centre 'G' - 19 February 2016 at 11:30 hrs

During the inspection 43 children were present, of which five were not part of the Scheme.

i. Two children, who were present at the centre during the visit, were traced in the final attendance record, but not in the attendance for the day of the inspection as provided by MEDE on 22 February 2016.

ii. Further testing revealed that whilst the time 'In' of Child 2 was inputted manually, the other child's arrival time was recorded by means of a fob as highlighted in *Table 9*.

Table 8: Children found on Attendance Report but not on the Records provided by Centre

Name	Scan Date	Scan Time	Scan Source[6]	Scan Type
Child 1	19.02.2016	06:28	Fob	In
		18:20	Manual	Out
Child 2		07:40	Manual	In
		18:50	Fob	Out
Child 3		08:20	Manual	In
		13:54	Fob	Error
		13:54	Fob	Out
Child 4		08:45	Manual	In
		13:10	Fob	Out

Table 9: Abstract from Fob Scans Report

Name	Scan Date	Scan Time	Scan Source	Scan Type	Manual Reason
Child 1	19.02.2016	08:45	Fob	In	
		14:30	Manual	Out	Forgot
Child 2		08:30	Manual	In	Forgot
		16:43	Fob	Out	

The above show that the system has not eliminated the risks prevailing under the manual system, but rather resulted in a new set of risks which still impinge upon the reliability of records kept by the childcare centres, as well as on the correctness of payments issued thereon. The above shortcomings also question the reliability of records for the previous period/s and the correctness of the respective payments.

Divergence from the set Terms and Conditions and the Applicable Contract Provisions

According to clause 4 of the terms and conditions for childcare service providers "*a onetime initial cash injection will be made available for centres to avoid cash flow related problems*". However, in contrast, the agreements entered into with the service providers indicate that apart from the initial cash injection upon the signing of the agreement, a yearly cash injection based on the number of booked hours in November of the previous year shall be paid to the respective centres. This amount is then to be set-off against any outstanding amounts due to the latter towards the end of every year.

In addition to the fact that this annual payment is not in line with the applicable terms and conditions, it is also increasing the workload of the officers employed in the administration of the Scheme, where the human resources are already inadequate for a Scheme of such magnitude. Moreover, although such payment is recouped at the end of the year, it is tying up funds that could be used more beneficially for other projects, rather than providing cash flow to service providers, when payments to the latter are being effected regularly and in a timely manner.

Eligibility Provisions overlooked by the Ministry

A main eligibility criterion stipulated in the information leaflet, as well as in the terms and conditions for service users, is that in order to benefit from the service, parents have to be both employed and paying social security contributions. However, there was no system in place to ensure that beneficiaries were actually paying the said contributions.

[6] No reason provided for the manual entries.

Lack of enforcement of these established eligibility criteria defeats the purpose of the whole Scheme whilst negatively impinging on the collection of revenue, namely the social security contributions and tax due to Government.

Control Issues

No Effective Checks by the Ministry on the Data submitted

As already highlighted, shortcomings concerning the reliability of data, and consequently the accuracy of the respective payments, were noted both in 2015, when the system was still manual, as well as in 2016 after the introduction of the fully automated CIS. The following concerns relate to the period January to April 2016.

a. Inconsistent Recording in Manual Entries

i. Instances were noted, predominantly in two childcare centres, whereby the time inputted manually by the centre's representative, erroneously or otherwise, was not in the 24-hour format. As a result, records showing the attendance, captured timings such as 00:00, 01:00 and 02:00. This distorted all the records, as in such instances the time-in was swapped with time-out and *vice versa*.

ii. In other instances, manual timings were noted in addition to fob scans for the day concerned. This also mixed up the records for the entire date, with the attendance captured being the incorrect manual entry and time-in fob, while the time-out fob was taken as an error.

iii. Due to the above, payments effected were incorrect. However, since NAO auditors were not in a position to determine the correct timings, the extent of such variance could not be quantified.

b. Public Holidays and Closed Days

i. Despite that centres run by the Foundation for Educational Services (FES) are closed on weekends and public holidays, three centres managed by the Foundation, as indicated in *Table 10*, recorded manual attendance for 1 January and 10 February (being the sampled period). Moreover, despite that the centres run by FES are closed on 4 January, as declared in the application, three centres also recorded manual entries for the said day, while in contrast indicating that the reason for such entries was that the centre was closed. Notwithstanding this, all these records were accepted by the system and payments, in aggregate amounting to €2,507, were issued for these hours.

Table 10: Payments on Days when the Childcare Centre was closed

Centre	Date	Reason recorded for Manual Entry	Number of Children	Hours of Service	Amount Overpaid
					€
1	1/1/2016	Public Holiday	10	62:20	189.71
	4/1/2016	Shutdown	10	62:20	189.71
	10/2/2016	Public Holiday	1	3:00	9.15
2	1/1/2016	Public Holiday	26	146:30	446.22
	4/1/2016	Centre Closed	26	147:15	448.81
	10/2/2016	Public Holiday	23	143:30	437.68
3	1/1/2016	Public Holiday	17	99:15	302.41
	10/2/2016		11	77:15	235.31
4	4/1/2016	Shutdown	13	81:30	247.97
Total					**2,506.97**

ii. Despite that the dates when centres are closed are recorded in the CIS, entries pertaining to those days were still accepted by the system and paid for. In the circumstances, it cannot be ascertained that the highlighted instances are isolated cases.

c. Incorrect Fob Records

i. Since January 2016, attendance was mainly captured through the fobs. However, an analysis of the entries recorded during the three-month period reviewed, *i.e.* January to March 2016, revealed a significant number of erroneous entries, arising from incorrect use of the fob, prevailing generally in January. As highlighted under Key Issues 'Abuse of the System and Tampering of Records by Childcare Centres – 'Ignored' Entries', prolonged contact of the fob with the reader was resulting in the recording of two or more entries. While no serious repercussions were noted with respect to entries reflecting the arrival of children on the premises, when this happened on their departure, the system automatically classified the two entries as 'Out' and 'In' again, with the following day's 'In' record captured in the system as an 'Out' fob. As a result, the recorded entries wrongly reflected an overnight stay at the childcare centre. While acknowledging that January was the first month of implementation, it is a major concern that such entries were neither corrected by the centres, despite the ability to do so, nor were they detected by MEDE, with the result that payments were issued on the basis of these hours.

ii. In contrast, other instances were noted whereby such erroneous entries resulted in a minimal duration of a few minutes, and the eventual payment thereof.

d. Applications and Entitlement

i. A test carried out on the applications related to the sampled centres involved the checking of the monthly entitlement as recorded in the CIS for January 2016. This was compared against the mother's working hours, as declared in the application. Queries to MEDE pertaining to the same centre, revealed that:

- in 13 out of the 17 cases queried, the entitlement recorded in the system was overstated;
- in three cases, of which two were terminated with effect from 31 January 2016, the booked hours exceeded the actual entitlement; and
- in another instance, the mother's working hours were not specified on the application, which only indicated that "*mother employed as a maid on part time basis flexible hours*", to substantiate a claim for 217 hours of service per month which translates to an average of 50 hours per week.

ii. According to MEDE, "*when the data was uploaded from the old spreadsheets to the new CIS there was no information regarding employment hours and therefore entitled hours. To this effect it was decided that employment hours would be made equal to the booked hours as per December 2016 [sic]. Entitlement hours were calculated accordingly*". This implies that the entitled hours were not checked for accuracy at application stage. Thus, compliance with the applicable formula establishing the entitlement cannot be ensured.

Standing Policy for Payments

a. The standing payment policy as per the applicable terms and conditions is that centres will be paid in full for the booked hours, provided that the absence entitlement is not exhausted. Verifications carried out for audit purposes, on attendance recorded by all childcare centres between January and April 2016, revealed that during the said period, 60 centres were paid an aggregate total of €90,140, covering 29,554 booked hours, for which the respective children failed to attend, or because they attended a different centre.

b. Twenty-one children, with an aggregate total of 11,910 hours recorded as booked with the centres, of which 75% were booked at a particular centre, did not attend for four consecutive months. Another 20, booking an aggregate of 4,950 hours, 24% of which were also on the records of this particular centre, did not show up for three consecutive months. All these children exhausted their annual absence entitlement without attending the respective centre.

c. The system only stops the payments once the absence entitlement goes down to zero. Thus, where the entitlement balance is almost exhausted, with only a few hours outstanding at the beginning of a particular month, the respective centre is still paid for the full booked hours at the end of the month.

Despite that the children in question failed to turn up at the respective centres for months in a row, exhausting all the absence entitlement, no action was taken by MEDE to determine the parents' intentions. While acknowledging that the timing of absence cannot be predicted, cases highlighted above clearly indicate that this policy can result in significant cash outflows, to the benefit of the centres only, and limiting the places available for other service-users. Moreover, the possibility of other cases where children are transferred from one centre to the other, thus featuring on multiple centres, without any communication with MEDE, as highlighted in the case example under Key Issues observation 'Full Reliance on Information provided by Service Providers – Transfers', cannot be excluded.

No Enforcement of Capacity Restrictions

The maximum number of children a centre may accommodate at any point in time is based on the area of the respective property, taking into consideration a space allowance of five square metres per child, as stipulated in the National Standards for Child Day Care Facilities.

a. While all the centres indicated their maximum capacity, in the applications submitted to MEDE to register for the Scheme, only 45% registered centres were supported by documentation from DSWS to confirm the said capacity. In the other cases, the certificate issued by the latter did not indicate the number of children that the respective centre can hold. While acknowledging that this is not within the control of MEDE, one cannot ignore the fact that no attempts were made to acquire evidence of the approved capacity.

b. Checks carried out by NAO auditors, after obtaining the information from DSWS on the maximum capacity, revealed discrepancies between the number as indicated by the centres in the applications submitted to MEDE, and the information held by DSWS.

c. Despite that centres may also accommodate children who are not part of the Scheme, and thus, MEDE would be unaware of, no surprise inspections were being carried out by the latter to ensure that the centres were respecting the capacity limit. NAO auditors were informed that this aspect fell under the responsibility of DSWS, however following its assessments, there was no communication with MEDE.

d. During 2015, only 29 visits were carried out by DSWS, covering 26 out of the 91 centres, as at December 2015. Moreover, only four visits, which were carried out in December while the audit was in progress, were unannounced. In all the remaining 25 visits, the respective centres were informed beforehand that an inspection would be taking place.

e. Independent verifications carried out by NAO auditors, at eight centres, revealed that in four cases, the capacity was in their majority substantially exceeded. In one particular centre, visited on 27 January 2016, the capacity of 15 children established by DSWS was exceeded by 72 kids at the time of visit, with the number of children present being more than four times the officially allowed capacity. In addition to breaching the applicable standards, potential abuse could expose the children to serious risk should an accident take place. *Table 11* refers.

Table 11: Children in Centres exceeding Capacity

Centre	Date of Visit	Time of Visit	Capacity as per DSWS	Capacity indicated by Centre on Application	Number of Children present at time of Audit Visit
1	27/1/2016	10:15	15	35	87
2	19/2/2016	11:30-12:00	15	31	43
3	25/1/2016	10:45-11:15	20	21	38
4	19/2/2016	10:15-10:30	50	50	54

f. Despite NAO recommendations made in a separate Report in 2010, encouraging the Government to accelerate the introduction of regulatory legislation, providing DSWS with the legal backing to enforce the National Standards for Child Day Care Facilities, to-date such standards, established in 2006, still do not have any legal backing. Although this is not a direct responsibility of MEDE, it still limits any actions the latter may adopt in cases of non-compliance.

Lack of Awareness by Parents about the Scheme's Operational Aspect

MEDE published a self-explanatory leaflet regarding the Scheme, which is also available online; however, no information sessions were ever held for service-users. Comments on social media and also personal encounters during the audit revealed that there is a general lack of awareness amongst parents on how the system actually works. Given that the latter's main contact point are the childcare centres, beneficiaries tend to get the information from the said centres or else from other parents, which, in certain cases, was not always in line with the set guidelines. While acknowledging that MEDE is trying to address this issue by keeping parents updated through regular mobile messages, as well as providing access to records of attendance, a basic understanding upon registration, together with the importance of the fobs, is still lacking.

Parents are one of the main elements of control. However, if they fail to understand how the system operates, the importance of the fob records, as well as that of confirming their child's attendance or otherwise, such control is lost.

Recommendations

Key Issues

Inadequate Internal Controls

In order to be effective and promote operational efficiency, controls are to be embedded in the operations and form part of the overall culture. It is thus recommended that a proper assessment is undertaken, wherein the current processes and procedures in place are reviewed in detail in order to identify potential risks and take the appropriate measures in a timely manner. Controls should also be capable of responding quickly to evolving risks, and include procedures for reporting immediately to appropriate levels, identified weaknesses and significant control failings. Moreover, to remain valid over time, such measures have to be reviewed on a regular basis.

However, sound internal controls cannot eliminate the possibility of processes being deliberately circumvented. Thus, staff and operations should be supervised by competent officers who are fully conversant with the standing processes, and who are ready to query such procedures and decisions, if and when necessary, taking appropriate measures to address any shortcomings in a timely manner.

Budget versus Actual Expenditure

As far as possible, detailed planning is to be undertaken when preparing budgetary estimates, in order to avoid having to resort to supplementary estimates, and keep such additional amounts to the barest minimum, thus limiting disruptions to other projects.

It is recommended that a continuous and thorough review of the processes in place is undertaken, in order to identify potential areas of abuse.

Lack of Human Resources

Given the significant funds involved, it is recommended that adequate human resources are allocated to manage the Scheme in order to strengthen the internal control structure.

Full Reliance on Information provided by Service Providers

In order to ensure effective use of public funds, regular checks and inspections are imperative to ensure that controls are functioning as intended, the system is not being abused of, and records provided by the centres are reliable. The outcome of such checks is to be documented. A sample of parents may also be selected randomly on a regular basis to confirm the child's attendance for the respective month.

Moreover, MEDE needs to regain control of the system without being too bureaucratic. Thus, one may consider requesting parents to submit both the application, as well as changes to booked hours, directly to the Ministry. Following the latter's approval, communication can then be made with the respective centre.

A standard Change Request form could also be drawn up, which may be either downloaded, available on the e-id portal, or collected in hard copy from the childcare centres and/or MEDE. While acknowledging that this may, up to a certain extent, increase the administrative work for the Ministry, it reduces significantly the possibilities of abuse, at the same time providing a reliable system at a lower cost.

Ineffective Control through the New Fobbing System

In order to ensure that the intended controls through the introduction of the fobbing system are effectively in place, MEDE must ensure that there is adequate control over the fobs themselves. A reconciliation exercise is to be undertaken to ensure that all fobs already issued are accounted for, including confirmation of receipt from the parents' end. For this reason, it would be ideal that henceforth, fobs are provided directly by the Ministry to the parents.

The Ministry may also consider the introduction of a Request for Fobs form, which could be filled in by the parents to order additional fobs, and which shall be submitted to MEDE and approved accordingly prior to the acquisition. Such form is to clearly indicate the number of fobs held by the parents, together with their unique number/s. Furthermore, it is recommended that audit trails are checked on a regular basis, enabling any irregularities to be identified at once so that corrective action could be taken in a timely manner.

Abuse of the System and Tampering of Records by Childcare Centres

The control element lies with the use of fobs. It is thus recommended that stricter controls are exercised over both their distribution and usage. This can only be achieved if the Ministry ascertains that the devices are actually held by the parents. On the other hand, the latter are to be made aware of the importance of such fobs and the related time-keeping. In addition, in order to monitor and ensure their effective use, regular inspections are to be held to confirm or otherwise the correctness of recorded information. For this reason, communication with DSWS is to be ongoing. Exchange of information obtained during such inspections is also recommended. In addition, the Ministry is encouraged to enhance the system, ensuring that any record

marked as 'ignored', for reasons other than multiple scans within a specified timeframe, is accompanied by a valid justification, and ideally approved by MEDE after being verified accordingly.

Divergence from the set Terms and Conditions and the Applicable Contract Provisions

Cash injection payments are to be made as stipulated in the applicable terms and conditions, *i.e.* as a one-off payment intended to ease initial cash flow related problems.

Eligibility Provisions overlooked by the Ministry

While positively noting that the Ministry is discussing the way forward on this matter, it is recommended that such checks be incorporated in the vetting process of the applications prior to their acceptance.

Control Issues

No Effective Checks by the Ministry on the Data submitted

While acknowledging that the Ministry is already taking action on certain concerns which were brought to its attention during the audit, it is recommended that a comprehensive assessment is carried out to identify the possible risks associated with the Scheme. A plan should then be set up to include detailed checks which can be performed on a monthly basis on centres on rotational basis to address those risks.

Standing Policy for Payments

It is recommended that if children fail to turn up for a whole month, MEDE contacts the parents in order to determine their future intentions. Necessary action can then be taken in a timely manner. In addition, as already suggested, as far as possible the Ministry is to get the information from the parents rather than centres. To this effect, another standard form may be circulated for transfers and terminations, for parents to fill in and submit to MEDE, either through email or post. The latter will then inform the centre of the change and process the respective payments accordingly.

No Enforcement of Capacity Restrictions

Although DSWS carries out checks to ensure compliance with the national standards, these inspections are not limited to the childcare centres. Thus, in view of the limited resources at both entities, and in order to avoid duplication of work, it is recommended that information concerning the childcare inspections, including the planned visits, is shared between the two entities. This will enable better planning, aimed at covering a larger number of centres each year. Once the high-risk centres are identified, more frequent visits can be scheduled to such locations.

Further to the above, it would be ideal if a joint framework of corrective measures is drawn up, backed up by the appropriate legislation. Financial penalties could initially be imposed by MEDE on those entities breaching the applicable conditions. Withdrawal of the DSWS certificate, and consequently suspension and eventually expulsion from the Scheme, is also to be considered in case of persistent defaulters.

Lack of Awareness by Parents about the Scheme's Operational Aspect

It is recommended that, on a regular basis, an obligatory information session is held for service-users. Parents are also to be informed that it is their responsibility to fob in and out for their child, and to check correctness of such timings recorded through any of the available mediums.

Management Comments

Management expressed its reservations on the timing of the audit, claiming that "*... the period (December 2015 – February/March 2016) was a crucial period in relation to the changeover from a manual system to the online system*".

The following comments and reservations were also submitted:

Limitation on Scope of Audit

MEDE is a 3rd party in relation to the invoices issued by the childcare centres to the parents. Parents know the attendance and non attendance of their respective child, and therefore any bills reflect such difference. Parents have resorted to the Unit to request assistance to verify the bills which was of course duly given.

Disclaimer

Action has been taken so that the system is enhanced so that data can be sorted on the basis of time.

Inadequate Internal Controls

Since June 2016, the regulatory role of childcare has been shifted from DSWS to the Ministry for Education and Employment.

Budget versus Actual Expenditure

On an annual basis, the Unit submits its budgetary proposal to the Ministry of Finance regarding the expected expenditure of the scheme. In the 2 years of operations, the budget submitted by the Unit was almost accurate to the actual estimate given. The Unit submits a detailed budget regarding this line vote.

Full Reliance on Information provided by Service Providers

It is to be clarified that payments are based on recorded fob records. All manual entries are audit trailed.

The Unit is in discussion with the Child Care Centres to introduce a verification system for change requests by parents.

Ineffective Control through the New Fobbing System

It is to be pointed out that to date the Unit has received 19 requests for additional fobs from the Centres. These requests totalled 335 fobs. When one considers that there are 10,105 fobs that are used or have been used (as at 19th September 2016), the issue of additional fobs is a minor one.

When Centres present a request for new 'free' fobs, the Unit reconciles the amount of fobs already taken up by the Centre with the amount in use or used in order to ascertain that the request is justified.

Audit trails of the system are matched with the manual entries. Both the centres and the parents who regularly forget the fobs, are being officially notified and reprimanded for this non-compliance.

Abuse of the System and Tampering of Records by Childcare Centres

Regarding the 'ignored' entries it should be pointed out that the majority of 'ignored' entries were picked up during the 4th to 15th January 2016, i.e. two weeks into the commencement of the new CIS. It would be understandable that the start-up period for a new system would inevitably have teething problems for the Centres, parents and also MEDE. The second sampled period, 18th to 29th April 2016, shows a significant drop in numbers.

Action was taken against Centres who had defaulted regarding capacity and all Centres were instructed that they should not retain any fobs at their end.

MEDE has also incorporated in the application process, a letter to be sent to parents whose application has been accepted, emphasising their responsibility to pick up the two fobs that they are entitled to from the respective Centre. An information leaflet explaining the Scheme is being included with the letter.

Divergence from the set Terms and Conditions and the Applicable Contract Provisions

Cash injection is a one-off payment. It is retained for the duration of the contract. The recommendation given by NAO will be considered in the new contract to be drawn up with the child-care providers.

No Effective Checks by the Ministry on the Data submitted

Inconsistent Recording in Manual Entries

MEDE has included a validation in the CIS on manual entries that warns the user if the time In or Out of a fob-scan is between 21:00 and 06:00.

Public Holidays and Closed Days

MEDE has included a new validation in the CIS regarding closed days. The new rule does not permit Centres to change 'Closed Day' entries that have occurred in the past. If Centres try to fob in or out using a manual entry on a 'Closed day' or a 'Sunday' the system will alert the user that the entry is not permitted.

Standing Policy for Payments

The cases need to be looked into on an individual basis. ... MEDE has recouped the €24,104.24[7]*.*

It must be pointed out that in most cases, this is the data that was migrated from the old spreadsheets.

[7] Being part of the €90,140 indicated in the Report, where the respective children failed to attend the childcare.

Foundation for Educational Services

Background

The Foundation for Educational Services (FES) is a public entity within the Ministry for Education and Employment (MEDE). It was created as a mechanism that works hand-in-hand with the Education Directorates to provide a range of innovative educational initiatives.

FES was constituted by a deed of foundation in May 2001 whilst its statute regulates its mission, objectives, functions and powers. It is a body corporate having a distinct legal personality. The powers and functions of the Foundation are entrusted to the Board which is responsible for the management and administration of FES affairs. The legal and judicial representation of FES is vested in the Chairperson of the Board.

Audit Scope and Methodology

FES management accounts for the year 2015 show an overall payroll expenditure of €5,374,224, paid to approximately 110 full-time employees, 350 part-timers and 1,400 temporary summer workers. In view of the significance of this expense, the main audit objective was to verify that the level of internal controls in the payroll process was adequate. Eleven employees spread among various grades were selected for testing on the basis of materiality of remuneration paid under the respective category. The aggregate payment to these employees during the year under review amounted to €123,141.

Contractual and Professional Services amounted to €245,806 during 2015. In this regard, the objective of the audit was to verify that the respective purchases were duly authorised and properly accounted for, and that the Public Procurement Regulations (PPR) S.L. 174.04, as well as other relevant circulars, were followed. The sample, selected on the basis of materiality, consisted of 45 payments in aggregate amounting to €65,774.

Limitation on Scope of Audit

Salaries

During 2015, FES payroll depended totally on manual attendance records and the National Audit Office (NAO) did not obtain sufficient comfort that such records were reliable. Internal control of records supporting the payroll function was also deemed lacking as explained further down in the Report under the pertinent observations.

Key Issues

Shortcomings in the Financial System

A report drawn up in April 2015, following a financial governance review exercise commissioned by the Chief Executive Officer (CEO)[1], identified various weaknesses in the financial management at FES. As a general overview, financial governance was found to be extremely weak. CEO 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. Management was also not aware that an accounting system was in place and financial information was only being retained on spreadsheets.

It was further remarked that neither the CEO nor the Accountant were aware whether a management letter was issued following the 2012 audit by the external auditors. The 2013 audited financial statements had not yet been approved by the Board when the report in question was concluded.

Only the bare minimum of financial documentation was retained and this was mostly scattered in unfiled piles of paper. Payroll files were found to lack a proper audit trail and not all employment contracts were available.

Payroll, creditors and expenses paid on behalf of other entities were being handled by two FES employees. All other accounting functions were under the responsibility of an outsourced Accountant, whose contract had just expired in March 2015. During January 2015, amounts due to the Inland Revenue Department for social security contributions and final settlement tax collected on behalf of FES employees, covering six months of the previous year and amounting in excess of €600,000, were settled directly by MEDE. Such amount had not been previously accounted for by the Foundation.

Various internal control measures were implemented following the conclusion of the above-mentioned report. A Financial Controller was engaged on a contract for service basis until 30 December 2015, following which, the same person was appointed as Head Business Support. However, given the shortcomings ingrained in the finance and human resources functions over the previous years, NAO still highlighted various observations, which will be discussed separately under the pertinent headings in this Report, such as:

a. inadequate attendance records and verification;
b. weaknesses in contracts of employment;
c. shortcomings in overtime approval; and
d. inadequate filing of documents leading to a lack of audit trail.

Inadequate Attendance Records and Payroll Verification

As already noted under 'Limitation on Scope of Audit', records provided were not considered reliable. During 2015, FES relied solely on manual records for registering the attendance of its employees as automated devices had not yet been 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.

Control Issues

Prior Approvals to perform Overtime not official

Section 15 of FES collective agreement 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

[1] The CEO was appointed in December 2014.

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.

Shortcomings in Personal Files

Files not updated

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 the basic pay awarded could not be confirmed with accuracy.

Documentation supporting Qualification Allowance not available

The qualification allowance awarded to two employees in the audit sample, was not supported by a copy of the respective certificates in the personal file. Moreover, it transpired that in one of these cases, the qualification allowance for a Masters Degree was granted when the incumbent was still attending lectures related to the respective course.

Payroll Discrepancies and Anomalies

Payroll testing of the 11 sampled officers revealed various shortcomings which warrant separate mention. The following concerns relate:

Anomalies related to the Appointment of Programme Coordinator

Retrospective Approval

An Officer's deployment to assume the position of Programme Coordinator with FES on 'grounds of public policy', was only approved on 27 February 2015 with effect from 19 September 2014, following the current CEO's appointment at FES. No explanation was available for this retrospective approval.

A contract stipulating the terms and conditions regulating the position in question was still not available by the time such deployment was revoked on 14 September 2015.

Salary awarded in excess of Official Approval

The starting annual salary commensurate with the Programme Coordinator's post was €21,260, as per FES pay structures in 2014[2]. However, the Officer was paid at the maximum of salary scale 6 applicable to the Public Service which, in 2014, was equivalent to €25,846. No documentation was made available to justify the additional emoluments.

Overtime

Section 3.2.1.3 of the Public Service Management Code states that overtime pay may only be paid to officers in salary scale 7 and below, while the maximum rate of overtime is to be invariably pegged to the maximum of salary scale 10. However, hourly overtime rate paid to the Programme Coordinator was still computed at 1.5 times the maximum of scale 6.

[2] Comparison made to 2014 rates. The FES collective agreement was only signed on 31 July 2015.

Anomalies relating to the Appointment of Senior Executive

Personal File not updated

The personal file only contained correspondence sent by FES to notify the then Employment and Training Corporation that the Officer was promoted to Senior Executive as from 1 March 2009. Official documentation was also not provided to confirm that the Officer was later deployed with the National Literacy Agency (NLA). The employment contract, which was subsequently obtained, had expired in 2012.

Basic Pay not in line with the Public Service Collective Agreement

The employment contract pegged the Senior Executive's salary to scale 5 of the Public Service collective agreement. However, her actual pay did not correspond to any of the steps within such scale for 2015. Following our observation, in view that the Officer occupied a number of posts with FES since the year 2006, the Head Business Support had to analyse the changes to her basic pay over the years and rectify the matter.

Payroll Shortcomings within NWAR Programme

Background

Approval dated September 2014 from the Office of the Prime Minister outlined FES salary structure for staff not covered by the collective agreement, for the years 2014 to 2016. This document included, amongst others, the hourly rates and conditions in respect of part-time personnel, such as tutors and coordinators, recruited for after-school hours, as well as for summer and NWAR[3] programmes.

NAO was informed that in 2014, services related to NWAR programme were absorbed by NLA. However, the latter was still not equipped with an administrative structure to take over the payroll process. Thus, in agreement with MEDE, FES continued to issue payroll during 2015 and charge back the Ministry. The Foundation confirmed that no verification was being performed at its end. The management accounts show total reimbursements of €201,925 in relation to approximately 70 officers engaged with NLA, mostly on a part-time basis. Shortcomings related to the three sampled employees falling under this category are highlighted hereafter.

Centre Coordinator

Compensation for Work not recorded as performed

As per section 6 of the Centre Coordinator's contract "*the Officer is expected to work 5.5 hours on-site per week and 1.5 hours off-site to carry out the necessary research, reports and preparation to ensure the smooth running of the centre*", for a weekly remuneration of €105. Although the Officer was still paid the weekly remuneration in its entirety, no record was available to cover the off-site hours that she was required to perform.

Family Literacy Tutor

Duration of the Contract not indicated

The contract of the Family Literacy Tutor (NWAR programme) was effective from 19 October 2009. Although its renewal was subject to a number of conditions as stipulated in section 3.2, the document did not specify the expiry date of the contract, thus rendering it open-ended.

[3] NWAR is the name of a literacy programme.

Contract for New Roles not available

Although the Officer was also paid the hourly rates for Homework Tutors and Coordinators, agreements regulating these positions were not available.

Overpayment

Audit queries revealed that the Officer was remunerated twice for the same two weeks work performed in August, as the respective timesheets were also presented twice.

Tutor

Expired Contract

A contract of service for the position of NWAR Tutor expired on 30 September 2015. However, testing confirmed that the individual received compensation for services rendered until 10 December 2015.

Irregular Services for the running of Programmes

Employees not paid through the Payroll

Payments made to three part-time employees, amounting in aggregate to €4,817, were not processed through payroll.

Services not covered by Contract

Two of the above-mentioned officers were not covered by employment contracts. This matter was regularised in the last quarter of 2015.

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[4] per hour, were signed retrospectively on 16 February 2015 with effect from 1 January 2015. The collective value of such 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.

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.

[4] Tender rate per hour was €5.80 amended to €6.29, both exclusive of Value Added Tax (VAT), in accordance with Contracts Circular No. 4/2015.

Shortcomings in the Procurement of Temping Services

The supplier for the provision of temping services was selected on the basis of the cheapest rate per hour, following quotations obtained directly from three service providers. Initially, these services were required for a three-month period from mid-November 2014 to mid-February 2015. Subsequently, a request to extend the agreement for an additional four weeks was approved by the Ministry on 29 January 2015.

However, the aggregate amount of €11,140 was disbursed on temping services during the year under review; thus, procurement of the foregoing required a departmental call for tenders or the publishing of a call for quotations in the Government Gazette.

Quality Assurance Services Timesheets not available

Five payments effected for quality assurance services in aggregate amounted to €4,280. Although all the relative documents were endorsed by FES officers prior to obtaining CEO approval for payment, these were not supported by timesheets substantiating the hours claimed.

Central Filing System not in place

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

Compliance Issues

Lists of Direct Orders and Departmental Contracts not published

PPR Article 20(2) stipulates that lists of departmental contracts awarded, as well as cases involving variations of more than 5%, are to be published in the Government Gazette every six months. As per MFEI Circular No. 11/2011, this list is to include also those purchases effected through direct orders procedure.

FES confirmed that this requirement was not met and thus the three departmental tenders and a direct order in the sample, amounting to an aggregate value of €224,930, were not published in the Government Gazette.

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, 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.

Financial Accountability

a. As per Section 10 of the statute attached to the Foundation's deed, the audit report and financial statements of the previous year are to be submitted to the Minister responsible for Education, by not later than the end of March each year. Notwithstanding this requirement, the audit for the year 2015 had not been finalised by the time NAO's review was concluded in September 2016.

b. The previous year's audited accounts had also been submitted late. The audit report and financial statements for the year ending 2014 were only finalised in November 2015 and these were only sent to the Minister on 12 August 2016, following NAO's query by email two days earlier.

c. The statute also requires the submission of the business plan for the following three financial years, together with an estimated budget of income and expenditure for the following year, to the Minister responsible for Education, by the end of May each year. Due to major restructuring within FES, in agreement with the Chairperson of the Board, for the current year, these were to be submitted by end October 2016.

Recommendations

Key Issues

Shortcomings in the Financial System

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

Inadequate Attendance Records and Payroll Verification

Given the substantial amount paid on salaries, NAO recommends 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 are to be incorporated within the payroll process where the introduction of such devices is not considered feasible by FES.

Control Issues

Prior Approvals to perform Overtime not official

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.

Shortcomings in Personal Files

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.

The entitlement to qualification allowances is to be confirmed through a copy of supporting certificates prior to effecting the respective payments.

Payroll Discrepancies and Anomalies

Contracts of employment regulate the relationship between an organisation and the respective employee. Thus, these should always be in place prior to the commencement of employment to avoid undue misunderstanding.

The financial package given to employees is not to exceed official approval. Management is also to ensure that, as far as possible, applicable regulations are followed to adopt good practice, fairness and transparency, thus leading to a positive and motivational climate in the workplace based on teamwork and collaboration.

Payroll Shortcomings within NWAR Programme

Measures are to be implemented to ensure that the administration and payment of amounts in relation to this service is adequately certified and controlled. Thus, an officer, accountable for such claims is to be identified. The respective officer's responsibility is to include corroboration of claims prior to settlement and filing of backing documentation for verification purposes.

Irregular Services for the running of Programmes

NAO reiterates that contracts of service are to be in place from the outset in order to regulate the employer and employee relationship. The amounts earned are to be invariably processed through the payroll system and taxed at the applicable income tax rates. This will assist the Inland Revenue Department in collecting the correct amount of tax dues in a timely manner and eliminate the possibility of tax evasion.

Cleaning Services

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.

Shortcomings in the Procurement of Temping Services

FES is to strive to ensure that the method of procurement is in line with the applicable regulations, thus ascertaining transparency and fairness. All service providers are to be given equal opportunity to submit their quote.

Quality Assurance Services Timesheets not available

The absence of timesheets leads to a lack of control over the hours worked and ultimately on the respective payment. Thus, invoices are to be invariably passed for payment, only if the relevant supporting documentation is provided and duly verified.

Central Filing System not in place

FES is 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.

Compliance Issues

Lists of Direct Orders and Departmental Contracts not published

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.

VAT Receipts not submitted

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

Management is to regularise its position by complying with the relevant circulars and report VAT defaulters accordingly.

Financial Accountability

Once the necessary set-up is in place for the smooth running of finance operations, Management is to ensure that the audited financial statements and other information, as required by the statute of FES, is submitted by the established deadlines.

Management Comments

Management concurred with the majority of the findings highlighted in the Report and action was taken to comply with a number of NAO's recommendations, whilst others were to be taken on board in due course. The following comments and reservations were also submitted:

Limitation on Scope of Audit

Should sufficient funding be forthcoming, FES plans to embark on a project to introduce card/palm readers in each of its 76 centres, such that attendance sheets are cross checked with pre-set rosters and actual clocking recorded and posted in the payroll system.

Shortcomings in the Financial System

Following the financial governance review exercise, FES Management has spent most of its valuable time completely reorganising employment contracts, financial information, archiving and ensuring proper funding for operations.

The utmost is being done to ensure that all employees have correct and current employment contracts, a proper personal file and correct data in the payroll system. Reconciliations are also being performed against Jobsplus records. It is to be noted however that the Human Resources Manager had resigned in July 2015 and a replacement was only in place in May 2016. This function was taken over by the CEO and Head of Business throughout this period.

Inadequate Attendance Records and Payroll Verification

Management has taken note of the recommendations and it is positive to note that although manual attendance sheets are still being processed, all timesheets are now being mathematically checked and approved against rosters before these are inputted in payroll. Checks are also being effected on leave and sick claimed and that all claims have supporting documentation and certification.

As defined in the section 'Limitation of Scope' above, FES wishes to install automated systems in all centres, however one needs to appreciate the financial and technical constraints that we experience. It is pertinent to note that half of our centres do not even have a personal computer in the office.

It is also pertinent to note that FES deals with a high number of part-timers with an extremely high turnover. Whilst this does not excuse any entity from retaining proper records, it is an administrative burden and requires adequate resources which are currently not in place.

Prior Approvals to perform Overtime not official

Recommendation has been noted and we are doing our best to obtain prior approvals before any overtime is carried out. Claims for additional hours without prior approval are not being considered or paid.

Shortcomings in Personal Files

Recommendation has been noted and stricter controls are in place with regard to the up keeping of personal files and what correspondence is entered into each. It is FES's objective to have these files properly indexed (red), however this would entail yet another administrative burden for which currently not enough resources are in place. In this regard, we have over the past year archived and registered more than 250 boxes of files and documentation such that the most recent files are properly retained and indexed.

All current qualification allowances being paid are supported with copies of certificates. With regard to the two samples taken, it is to be noted that we have requested a copy of the Diploma from the employee still working for the FES and ongoing correspondence is in place with the other employee (now terminated) to recover any payments made and approved in error.

Payroll Discrepancies and Anomalies

The FES is fully aware of the payroll processing procedures used in 2015 and notifies that a substantial number of issues have already been rectified. However, Management is of the opinion that the small sample taken is not representative of the thousands of transactions processed.

Anomalies related to the Appointment of Programme Coordinator

The FES is already in contact with its ex-employee who was deployed to the entity in September 2014, such that we recover payments made in excess if no documentation/approvals are found. If approvals are in place for his payment of Scale 6 basic salary, then his overtime needs to be refunded. If not, then the overtime and basic rate are to be adjusted to reflect that of the approval as Programme Coordinator.

Anomalies relating to the Appointment of Senior Executive

The salary paid to the Officer reconciled with Scale 5 until 2013. It is in 2014 and 2015 that adjustments (in the employee's favour) need to be effected. Failure by the FES management to extend the contract in 2012 resulted in the fact that the employment contract became one of an indefinite nature.

Management will obtain documentation confirming the Officer's deployment with NLA.

It is pertinent to note that FES today ensures that all employment contracts have the necessary approvals in place prior to any payroll payments being effected. Moreover, salary scales are in line with approvals obtained by MFIN[5], PACBU[6] and Collective Agreement.

Payroll Shortcomings within NWAR Programme

During year 2015, FES continuously insisted that the payment of the NWAR payroll moves to NLA or MEDE, as it felt that we were out of control of what was being approved and paid. The service (NWAR programme) is no longer under FES remit and moreover the processing of payroll stopped from 1 January 2016.

Irregular Services for the running of Programmes

Recommendation noted and already in place. FES does not engage personnel for its services unless through a regularised employment contract. Two of these persons still work for FES and have a valid employment contract in place with Tax and National Insurance deducted as applicable.

[5] MFIN – Ministry for Finance.
[6] PACBU – Public Administration Collective Bargaining Unit.

Cleaning Services

FES agrees that not enough control and thorough checking was implemented on the cleaning contract, which was terminated at the end of December 2015. It is pertinent to note that the contractor was not one of experience in the field and lacked integrity with regard to payment to his employees. FES was aware of a substantial turnover in the contractor's staff due to non-payment of wages. Therefore this placed enormous difficulties in the management of this contractor who was engaged to clean on a daily basis all of our centres. It is to be noted that FES had reported this Contractor to the Department of Industrial and Employment Relations.

Should FES manage similar contracts in the future, NAO recommendations would certainly be taken onboard.

Shortcomings in the Procurement of Temping Services

This recommendation is being noted and FES can confirm that all procurement is now being carried out in line with regulations. This applies to the adherence to procurement thresholds, calls for quotations, tenders and direct orders. This agreement with the service provider was concluded by the previous CEO and contract was terminated as soon as possible, due to it exceeding the tendering thresholds.

Quality Assurance Services Timesheets not available

Recommendation is being noted and will be taken on board for future similar contracts.

Central Filing System not in place

During 2015, FES Management embarked on an exercise to archive more than 200 boxes of files and documentation which FES never archived since its inception in 2001. Up to date, all archived files are recorded on computer spreadsheets, however current files' movements are not registered. This is mainly due to lack of resources of both a registry system and personnel to maintain it. This task will be handled and managed by the Manager Corporate Services once employed.

Lists of Direct Orders and Departmental Contracts not published

Lists of Tenders, Calls for Quotations and Direct Orders are being published in the Government Gazette in line with circular and copied to the Compliance Unit at DOC[7].

VAT Receipts not submitted

Vat Receipts will be requested for those suppliers not providing a fiscal invoice with EXO number. VAT defaulters will be reported in line with directives.

Financial Accountability

Audit for 2015 has been concluded and targeted for Board presentation by end of November 2016. The 2016 audit will be conducted in February 2017 such that financial statements are submitted to the Minister in line with Statute requirements. Same applied for Business Plans and Financial Budget.

[7] DOC – Department of Contracts.

Ministry for Sustainable Development, the Environment and Climate Change

Agriculture Support Scheme

Background

The approved budget allocation for the Agriculture Support Scheme, out of which the subsidy payments under the Special Market Policy Programme for Maltese Agriculture (SMPPMA) were effected, stood at €2,200,000 for financial year 2015. This allocation was reduced by €112,287 during the year, resulting in a revised budget of €2,087,713.

Apart from fully utilising the allocated revised budget, a further €12,005 was expensed from the Below-the-Line (BTL) Account – SMPPMA Funds, held by the Ministry for Sustainable Development, the Environment and Climate Change (MSDEC).

The SMPPMA for crop producers ran for a period of 11 years effective from Malta's accession to the European Union (*i.e.* 1 May 2004). Therefore, 2014 marked the final year of subsidies paid to beneficiaries of crop producers under this Programme.

Audit Scope and Methodology

The scope of the audit was to ensure that subsidies paid in 2015 from Line Item 5014 – Agriculture Support Scheme, under Programmes and Initiatives, and the BTL Account relating to SMPPMA Funds, were appropriately recorded and processed according to pertinent regulations and circulars. Furthermore, the audit sought to verify whether internal controls, intended to ensure the complete and accurate recording of expenditure, were in place and that these were satisfactory.

Given that the largest subsidy payments related to fruit and vegetables[1], and the majority of farmers unloaded their produce at one or more of the 16 private *Pitkala*[2] stationed at the *Pitkali* Markets Centre, the audit sample was selected from amongst these beneficiaries. Audit testing was carried out on the subsidy payments effected in 2015 to nine beneficiaries exceeding a threshold established by the National Audit Office (NAO). This covered a total payment of €71,532, representing approximately nine *per cent* of the fruit and vegetables subsidies paid. The testing performed also served as a follow-up to the audit carried out by NAO on the same Scheme for financial year 2008.

[1] Payments for fruit and vegetables subsidies totalled €807,446, of which, €545,565 related to amounts due for 2013 and €261,881 for 2014.

[2] Fruit and vegetables unloaded by the farmers at the *Pitkali* Markets Centre are sold through middlemen, referred to as *Pitkala*.

Furthermore, the audit included a review of transactions posted in the BTL account, as well as obtaining an explanation on expenditure, other than subsidy payments, charged to the Agriculture Support Scheme.

The *Pitkali* Markets held a current account with a local commercial bank, which account was closed on 31 December 2015. Amongst other functions, this account was utilised for effecting subsidy payments to beneficiaries. NAO requested clarifications on the maintenance of the bank account, as well as the payment system in general. Explanations were also obtained on the new payment system that came into force during 2015.

Overview of Fruit and Vegetables Subsidy Calculation

In the case of farmers unloading their produce at any of the 16 private *Pitkala*, the data is recorded by the respective *Pitkal* through a computerised system. Information noted includes, but is not limited to, the type of crop unloaded, number of crates or weight in kilograms (kg), selling price, quantities sold and name of buyer. A report holding this information is subsequently forwarded to the *Pitkali* Markets, where officers input the data in the *Pitkali* Markets Management System (PMMS). The subsidy payments are calculated on the produce weights as shown in the PMMS and pre-established rates determined in accordance with Annex XI of the Act of Accession: Malta.

Key Issues

Limitation on Scope of Audit

Uncertainty on Basis for determining Subsidies due to Beneficiaries

During audit testing, NAO noted that the subsidy payments for 2013 and 2014 were at times calculated on the quantities of produce sold by the private *Pitkala*, while on other occasions, subsidies were based on quantities unloaded by farmers.

In fact, out of the total weight of 6,969 kg recorded as having 'Nil' value[3] in the *Pitkala*'s reports made available for audit purposes, 6,339 kg were not recorded in the PMMS, thus excluded from the subsidy entitlement calculation. On the other hand, 630 kg were input in the *Pitkali* Markets system, and subsidies were paid to the beneficiaries accordingly.

Following a clarification requested by NAO, a senior official within the *Pitkali* Markets confirmed that SMPPMA was payable on the actual quantities sold. On the other hand, the explanation on subsidy entitlements to fruit and vegetables producers forwarded by the Agricultural Directorate within the Rural Development Department refers to "... *production data from deliveries reported by the Pitkali Markets* ...".

Since the method for calculating the 2013 and 2014 subsidies was inconsistent and not in line with information obtained, NAO requested further clarifications from MSDEC, as well as any official documentation identifying the basis on which the subsidy payments were supposed to be calculated. However, no such documentation was made available up to time of audit testing.

In view of the conflicting information on which quantities (*i.e.* unloaded by farmers or sold by *Pitkala*) were to form the basis of subsidy payments, it cannot be ensured that the beneficiaries were paid the correct amount to which they were entitled. Thus, the scope of audit was limited in this respect.

[3] Implying that the sale did not take place.

Required Information not made available for Audit Purposes

During the audit, MSDEC was requested to provide an itemised list of the 1.75% commission supplement paid to *Pitkala* (totalling €100,333) and payments relating to wine analysis (amounting to €9,016), both charged to the Agriculture Support Scheme.

Despite various reminders sent, the requested information was not made available by conclusion of the audit, hindering NAO from conducting the necessary testing. Additional information on the wine analysis expenditure was submitted to NAO's satisfaction together with the Management Comments. However, only monthly aggregate figures were submitted in support of the 1.75% commission supplement paid.

Source Documentation not forwarded by all *Pitkala*

In order to conduct testing on the sample of subsidy payments for 2013 and 2014, source documentation was requested from 11 and 10 private *Pitkala* respectively. However, the 2013 sales reports were made available by only eight *Pitkala*, while one *Pitkal* failed to forward documentation in support of deliveries by the sampled farmers during 2014.

Consequently, no testing could be performed by NAO on 12% and 6% of the sampled weight for 2013 and 2014 respectively, thus hindering verification on the accuracy of the respective subsidy entitlements.

'Nil' Value Transactions featuring in Pitkala Reports

Upon reviewing source documentation made available by the private *Pitkala*, NAO came across several instances where, although the respective weights or quantities of produce were inputted in the *Pitkala*'s systems, 'Nil' values were assigned to these transactions. Furthermore, the buyers' codes and names for these transactions, where available, stood out when compared to the remaining entries within the same reports[4]. The *Pitkala*'s sales reports forwarded to NAO in support of subsidies paid to the beneficiaries selected in the audit sample featured crops weighing a total of 13,514 kg recorded at 'Nil' value.

Since the weight of produce forms the basis of subsidy payments to farmers, NAO requested the *Pitkali* Markets to explain the nature and reasoning behind such transactions. In its reply, the latter made specific reference to the six transactions for a total of 2,075 kg of watermelons, featuring at 'Nil' value in the sales report of a particular *Pitkal*, which NAO used as an example in its query. A *Pitkali* Markets officer claimed that in the mentioned case, all sales of watermelons effected on the day were returned to the *Pitkal* and therefore, the respective weights still featured in the system. Furthermore, another *Pitkali* Markets officer claimed that "*... articles were returned back and once inputted in system items cannot be erased*".

In view of the fact that the *Pitkali* Markets' explanation was exclusive to one particular case, NAO was not in a position to establish whether transactions with a 'Nil' value were supposed to be taken into consideration in determining the subsidies entitlement to farmers. Neither could it be ascertained that all 'Nil' value transactions featuring in the *Pitkala* reports represent returns of crops to the same *Pitkala*. The inconsistent treatment of these transactions by the *Pitkali* Markets when calculating subsidy payments also shed doubt on the reliability of the explanation given to NAO.

On the other hand, if the explanation provided is valid for all the remaining 'Nil' value transactions featuring in the *Pitkala* reports, considering that NAO identified instances where such transactions were recorded in the PMMS and subsidy paid accordingly, double-counting of weights, and therefore, overpayment of subsidies, cannot be excluded.

[4] This included buyer codes commencing with '6' and '7' when all the other codes started with '0' to '2'; five-digit codes instead of the usual four-digits used to identify the different buyers; and codes bearing repetitive digits, such as '111111'.

Control Issues

Subsidy Payments

No Source Documentation retained by the *Pitkali* Markets

Documentation supporting the data entered in the PMMS was not retained by the *Pitkali* Markets. Therefore, the original documents had to be requested from the private *Pitkala* in order for NAO to have access to details forming the basis of subsidy payments and to conduct its audit testing.

Consequently, the verification of the correctness of subsidy payments depended entirely on the availability of the information submitted by the *Pitkala*.

Produce Weights as recorded in the *Pitkali* Markets Management System not in agreement with Source Documentation

In order to verify whether the correct quantities of produce were input in the PMMS, NAO requested the source documentation, held by the private *Pitkala*, for a sample of 129 transactions, with records actually made available for 113 of these transactions.

Testing performed revealed discrepancies in 14 transactions between the produce weight as recorded in the PMMS (and on which subsidy payments were calculated) and the *Pitkala*'s documentation. In fact, in each case, the quantities recorded in the PMMS were overstated, resulting in the beneficiaries being paid more subsidies than they were actually entitled to.

NAO felt it should remark on the seriousness of the shortcoming, even though excess subsidy was not material by amount.

Pitkali Personnel not present during the unloading and sale of Products at the *Pitkali* Sheds

During the 2008 audit, NAO had observed that *Pitkali* personnel were not present during the unloading and sale of products at the *Pitkali* sheds. In its reply to NAO's Management Letter, the then Ministry for Resources and Rural Affairs had committed itself to review its clerical deployment in this area. Furthermore, it had claimed that "*Action has already been taken with the Management and Personnel Office to have a new human resource structure and complement in line with current reform being undertaken at the Pitkali market*".

When queried on the matter during the current audit, a senior official at the *Pitkali* Markets confirmed that the unloading and sale of produce at the sheds operated by the private *Pitkala* was not being monitored.

The lack of independent verification of data recorded by the private *Pitkala* (at unloading and selling stages) sheds doubt on the accuracy of the weights forming the basis of subsidy payments.

Bank Account held with a Local Commercial Bank

Shortcomings in the Maintenance of the Bank Account

No Bank Reconciliation

The bank account which was closed on 31 December 2015, was not being reconciled on a regular basis by the *Pitkali* Markets. In fact, when queried on the matter, *Pitkali* Markets officials commented that the payment system was fully administered by the local commercial bank.

Substantial Amount of Accumulated Bank Charges

In the process of closing the above-mentioned current account, MSDEC was requested by the commercial bank to settle a long outstanding debt balance of €26,344.

By mid-2015, the commercial bank had reviewed entries in the Ministry's account and listed bank charges, which were debited automatically once the payments to the farmers were processed. According to this list, charges incurred by MSDEC totalled €54,462, and had been accumulating since July 2002, *i.e.* for almost 13 years. The commercial bank had in fact utilised funds available in MSDEC's bank account to offset part of these bank charges, and the amount of €26,344 was the remaining outstanding balance.

When queried on the untimely settlement of the bank charges, *Pitkali* Markets officials stated that these were only brought to their attention once the commercial bank initiated proceedings to terminate its contract with the Ministry. The officials further claimed that over the past 15 years, previous *Pitkali* Markets Management and SMPPMA Fund Administrators were responsible for administering these charges.

Unreconciled Differences

Although €54,462 was due to the commercial bank in respect of accumulated charges, payments by MSDEC to this effect amounted to €45,290. Nonetheless, the charges were settled in full, resulting in untraced payments of €9,172. Out of this amount, €6,690 were unaccounted for, with the remaining €2,482 relating to a difference on the amount due to a particular *Pitkal*.

Recommendations

Key Issues

Limitation on Scope of Audit

Uncertainty on Basis for determining Subsidies due to Beneficiaries

MSDEC is to ensure that calculations of amounts due to beneficiaries are consistent from one year to another and supported by official documentation. Such documentation is to be retained for future reference.

Required Information not made available for Audit Purposes

Auditees are expected to maintain records in a way that enables timely forwarding of all information and explanations upon request, hence facilitating the performance of the audit.

Source Documentation not forwarded by all Pitkala

Pitkali Markets is to ensure that it is in possession of all source documentation, thus avoiding having to revert to the private *Pitkala* in the event of independent verification by third parties.

Control Issues

Subsidy Payments

No Source Documentation retained by the Pitkali Markets

As mentioned previously, *Pitkali* Markets is to retain all source documentation, which is to be systematically filed, either physically or electronically, and held for future reference.

Produce Weights as recorded in the Pitkali Markets Management System not in agreement with Source Documentation

Pitkali Markets is to place more care when data is input in its system, so as to avoid similar errors from occurring. Requesting refunds for the excess subsidy given is also to be considered.

Pitkali Personnel not present during the unloading and sale of Products at the Pitkali Sheds

Whilst the Ministry is urged to improve its current operations, it is to refrain from effecting payments based solely on unverified third party information.

Bank Account held with a Local Commercial Bank

MSDEC is to refrain from placing reliance on the commercial bank for the administration of its accounts. It is also to ensure that all bank accounts are monitored and reconciled on a regular basis. By maintaining full control, the possibility of being faced with accumulated charges and unreconciled amounts is minimised.

Management Comments

In its, at times, non-exhaustive reply, Management stated that the subsidy amounts paid to farmers was based on "... *the produce delivered and sold at the Pitkalija*" and that the subsidies were "... *calculated on the sales inputted by the Pitkali Clerks in the said PMMS*". NAO was forwarded with exchange of correspondence between MSDEC and PMMS' software developer, but the audit issue still holds. Furthermore, MSDEC failed to offer an explanation for the instances noted during the audit, whereby subsidies were based on the quantities unloaded by farmers. NAO's observation regarding the inconsistent treatment of produce that was assigned a 'Nil' value by the individual *Pitkala* was also not properly addressed.

On the fact that not all the private *Pitkala* made source documentation available for audit purposes, Management commented that the data held in this documentation was recorded in the PMMS and it "... *is considered to be reliable especially in the light of the fact that once cycle is completed and closed no changes can be affected*". Furthermore, the Ministry was adamant that source documentation was "*irrelevant to keep*" at their end, since the data entered in the PMMS would have already been reconciled with the data provided by the *Pitkal*. MSDEC also claimed that "*In case of discrepancies these would be noted by the farmers*".

Management pointed out that the *Pitkali* Administration was working on implementing a new Information Technology System, in order to ensure better control and transparency in relation to produce bought and sold at the *Pitkali* Markets. It is being planned that the proposed system is expected to include real time recording and monitoring of all deliveries and sales of produce.

As regards the unreconciled amounts on the bank account, MSDEC pointed out that these "... *were accepted by the Bank and regarded as reasonable, given that the sum of 447€ per annum was involved for transaction varying between €1 to 1.5 million monthly*". Management also confirmed that through the new banking system introduced as from March 2015, reconciliations, as well as updates of bank charges, were being carried out on a monthly basis. Among the benefits of the new banking system, MSDEC highlighted the reasonable cost of the system, well-managed overdraft facilities and that farmers were assured of receiving their payments, due to a bank guarantee system that was imposed on the individual *Pitkala*. At the same time, Management also stated that the banking system is self-financed by stakeholders themselves.

Management concluded by pointing out that "... *the difficulties and flaws of the Pitkali Payments system were largely inherent to the old Banking system which was very difficult to control and reconcile*".

Ministry for Transport and Infrastructure

Ministry for Transport and Infrastructure

Expenditure

Background

The Ministry for Transport and Infrastructure (MTI) had an approved budget allocation for 2015 of €82,802,000. Of this, €30,720,000 was allocated to Personal Emoluments, €4,102,000 to Operational and Maintenance Expenses, €47,210,000 to Programmes and Initiatives and €770,000 were intended to be used as Contributions to Government Entities.

Warrants amounting to €2,234,996 were granted to MTI during the year under review, increasing the available Recurrent Vote budget to €85,036,996. Actual expenditure for 2015 totalled €84,548,962, of which €30,771,191 related to Personal Emoluments, €5,276,046 to Operational and Maintenance expenses, €47,736,386 to Programmes and Initiatives, and €765,339 to Contributions to Government Entities.

The discrepancy between the budgeted funds and the actual amounts spent resulted in unutilised funds on MTI's recurrent vote of €488,034.

Audit Scope and Methodology

The main scope of the audit was to assess the level of existing internal controls over the procurement and payment of selected items of expenditure incurred by MTI during 2015. The audit also aimed to ascertain the efficient administration of public funds in line with existing regulations, policies and procedures, including the prudent use of public resources.

Audit work performed covered a sample of transactions charged to a number of accounts falling under Operational and Maintenance Expenses. A total of 30 items, in aggregate amounting to €289,303 were selected from these accounts. A further 10 transactions, totalling €239,799, were also selected from Programmes and Initiatives and other control accounts pertaining to the same types of expenditure. When selecting the audit sample, particular consideration was given to the materiality of amounts and the nature of the expenses.

Selected Payment Vouchers were traced to Local Purchase Orders or Letters of Acceptance, invoices and fiscal receipts, in order to determine whether authorisation was duly obtained before the purchase, that the amount due was correctly computed, and that MTI was invariably issued with a fiscal receipt, whenever applicable. Reference was also made to contract agreements, quotations or tender documentation, supporting the procurement procedures being followed.

Five locations from an inventory list provided by MTI were also selected to ascertain the correctness of inventory held by the Ministry, in line with the provisions of MF Circular No. 14/99 – 'Government Accrual Accounting: Revised Inventory Control Regulations'.

Testing was also conducted in relation to the maintenance of logbooks of nine general-use vehicles. Each logbook was verified by randomly selecting a particular month and assessing its adherence to the relevant sections of the Public Service Management Code (PSMC). The fuel consumption of three fully-expensed vehicles was also assessed against provisions within MF Circular No. 5/98 – 'Purchase and Use of Official Cars'. The same Circular was referred to when testing the purchase of two new fully-expensed vehicles during 2015.

Moreover, transactions relating to six official visits, with a total value of €43,743, were checked to assess whether travel arrangements including flight cost, hotel accommodation and other expenses, as well as the subsistence allowance entitlement were in accordance to the relevant PSMC requirements.

Control Issues

Irregularities in relation to Direct Order approvals

Services provided by a Cleaning Company

A Direct Order (DO) request for the procurement of cleaning services was made by MTI in October 2015. The request quoted the fact that the selected supplier had already offered such services to the Ministry, as well as that the payment terms and rates had already been agreed with an MTI Director, as reasons for resorting to a DO. The relevant approval was granted by the Ministry for Finance (MFIN).

A payment of €11,293 was made for cleaning services performed during the period May to October 2015. The Ministry confirmed that such payments were covered by the above-mentioned DO, implying that this approval was granted retroactively and that the amount approved by MFIN was used to pay for work, which, in its majority had already been carried out by the service provider.

In total, the cleaning company received €21,419 in payments during 2015, and €20,047 up to June 2016, with a further €6,236 funds committed up to August 2016.

Services provided by an Architect

A request for approval to obtain the services of an Architect to oversee projects falling under MTI's remit, was made by the Ministry in May 2015. The DO for €32,239 was approved by MFIN on the day following MTI's request.

Nevertheless, testing revealed that a 12-month Service Contract Agreement between MTI and the proposed Architect was entered into in April 2015, which was more than one month before the DO was requested and approved. Furthermore, testing of payments totalling €11,682, and relating to three invoices for the months of April to June 2015, also showed that the amount of circa €5,527 was not covered by the pertinent DO approval.

Services provided by an Information Technology Company

An approval for the engagement of an Information Technology company for the online promotion of a National Campaign, for a total value of €74,022, was requested from MFIN in August 2014 and approved on the same day, on the basis of the Ministry's claim of urgency.

However, the National Audit Office (NAO) noted that a Letter of Intent was sent to the service provider four months later, in December 2014. Moreover, since no agreement was traced in file, NAO could not verify the terms of engagement, as well as the official date when such services were to commence.

An invoice from the same company, dated September 2014, was also traced as part of the vetting process. Part of this bill related to domain name registrations for the period of one year to July 2015, showing that

such registrations were already in place before the DO approval was even requested in August 2014.

Services procured without the Necessary Approvals

Service provided by a Consultancy Company

In June 2015, additional funds were requested by MTI in relation to an investigation into the New Parliament's project cost overruns. A company was appointed to conduct this work, at a cost of €74,692 and the relevant report was presented in October 2014.

a. The approval for additional funds by Budget Office was given in August 2015, 10 months after the report was submitted by the said company. Furthermore, no information was traced in file showing the rationale behind the appointment of this service provider and a DO approval was never sought from MFIN. The Ministry also confirmed that no approvals for the appointment of the service provider were available.

b. No contract agreement was traced for the services provided by the company for the above-mentioned amount. Therefore, NAO was not in a position to assess whether the amount paid was justified and correct.

c. The relative invoice included fees[1] payable to three individuals for work conducted during August and September 2014. Information showing the nature of the work and when it was conducted was not traced in the files provided. Following NAO queries in this regard, MTI confirmed that no supporting documents were available.

   An additional amount of €6,724 included in same invoice, pertained to flights, taxis, hiring of cars and fuel, accommodation, car park fees and in one instance, a reimbursement for a meal. MTI confirmed that, even in this case, no supporting documents were made available, detailing the expenses paid for by the Ministry.

Other Works

Two payments, amounting to €7,762 and €2,370, made to two companies, were selected for audit testing. MTI stated that one of the suppliers was chosen through a tender for Framework Contract for the supply and delivery of ready mix concrete, whilst the other company had been awarded a period contract for the hire of hydraulic excavators.

Nevertheless, in both instances, the respective files, as well as replies to NAO queries in relation to the procurement of such services, did not contain sufficient information for this Office to assess the relevant procurement procedures.

Compliance Issues

Lack of compliance with Standing Travel Regulations

Flight Documentation not available

In the case of a delegation trip, NAO was not in a position to verify whether air travel was properly procured after obtaining three quotations since the only quotations traced were from two local travel agents.

[1] Fees *per* hour in relation to one of these individuals amounted to €320, whilst a fee of €130 *per* hour was payable to the other two (VAT excl.).

Errors in the Calculation of Subsistence Allowance

Deductions from subsistence allowance in relation to lunches/dinners were not duly made in relation to seven officers, who participated in three separate visits abroad.

Travel Reports not available

A report containing the purpose and benefits achieved from visits abroad on official Government business, as required by Ministry of Finance, the Economy and Investment (MFEI) Circular No. 5/2012 – 'Travel on Official Duty', was lacking in the case of two of the selected visits.

Shortcomings in relation to General-Use Vehicles

No Logbooks being kept

During testing, MTI confirmed that no logbooks were being kept to record the journeys made by four general-use vehicles during 2015. Nevertheless, in the case of three of these vehicles, NAO was presented with the 2016 logbooks, which were duly scrutinised instead.

Shortcomings in the compilation of Logbooks

Testing revealed that none of the logbooks tested was fully compliant to the relevant PSMC provisions. In the majority of cases, the following information was missing:

- Odometer details
- Duration time
- Purpose of the journey
- Issues of fuel
- Signature of the officer making the journey

Furthermore, the monthly certification required by Section 8.2.5 of PSMC was not available in all the sampled logbooks.

Shortcomings related to Inventory

Inventory Lists not updated

NAO noted a number of discrepancies between the list provided by MTI and the inventory on site. In fact, testing showed that a number of items present at the three locations tested, were not traced to the Inventory List. Furthermore, a number of items listed in the aforementioned list, were also not traced on site, while no Asset ID was affixed to seven assets tested. Additionally, a vehicle procured during the year under review was not included in the Inventory Database.

Non-compliance with Fiscal Obligations

Missing Fiscal Documentation

Fiscal receipts were not traced in relation to eight transactions selected for audit purposes, which related to disbursements of €152,200.

Non-submission of VAT Quarterly Returns

Upon NAO enquiry, MTI confirmed that it did not forward the quarterly Returns reporting fiscal receipt defaulters, which it should be submitting to the Value Added Tax (VAT) Department in accordance with MFEI Circular No. 2/2012. Nevertheless, the Ministry confirmed that steps are being taken to ensure that the submissions are sent when due.

Recommendations

Control Issues

Irregularities in relation to Direct Order approvals

As emphasised in MFIN Circular No. 3/2013 – 'Public Procurement Regulations – Direct Orders', DOs should be limited to the barest minimum. Moreover, commitments should not be entered into with the service provider before obtaining the necessary MFIN approval, which instances are to be resorted to on an exceptional basis.

Additionally, each major assignment handled by the Ministry should be formalised through a Contract Agreement to ensure that all the necessary details are understood by both parties and that billing is done according to the plans and relevant approvals.

Services procured without the Necessary Approvals

It is recommended that MTI adheres fully to the requirements of the Public Procurement Regulations, to ensure fairness, and provide equal opportunity to all interested parties in the provision of services.

Compliance Issues

Lack of compliance with Standing Travel Regulations

As required by the relative provisions of the PSMC, whenever the services of Air Malta are not used for some permissible reason, alternative air travel arrangements should only be authorised on the presentation of three quotes, one of which must always be from Air Malta.

Reports on the visit should also be prepared by the travelling officers and be submitted to MTI accordingly.

Shortcomings in relation to General-Use Vehicles

The Ministry is to ensure that a logbook is maintained for each of its general-use vehicles, detailing all the trips made, as well as the signatures of the officer making the journey.

In line with standing regulations, each logbook is also to be certified by the officer in charge of transport at the end of each month, to ensure that the trips recorded in the logbook were made on official duty and that fuel consumption is reasonable and justifiable.

Shortcomings related to Inventory

It is recommended that periodic checks are carried out on inventory items to ensure that any discrepancies are recognised.

Moreover, as stated in MF Circular No. 14/99, "... *Each item shall be physically marked with a consecutive identification number* ..." It is recommended that this procedure is adhered to, and that, as far as is practicable, items are physically marked with a permanent identification number.

Fixed asset additions are also to be forwarded to the officer in charge of inventory for eventual recording in the respective records, to ensure the safeguarding of assets owned by Government.

Non-compliance with Fiscal Obligations

Every effort is to be made to enforce the principle that VAT receipts are invariably obtained from suppliers for every purchase of goods and/or services.

Additionally, defaulting suppliers are to be reported in the quarterly VAT defaulters lists, required to be submitted to VAT Department as per MFEI Circular No. 2/2012, for appropriate action to be taken. 'Nil' Returns are also to be forwarded accordingly.

Management Comments

In its reply, Management concurred with most of the observations and recommendations put forward by NAO. In its feedback, the Ministry outlined its clarifications and actions that will be taken, as follows:

Irregularities in relation to Direct Order approvals and Services procured without the Necessary Approvals

With regards to services provided by a cleaning company, the Ministry stated that "*The present process is a stopgap measure since currently a number of alternative solutions are being considered and discussed with OPM*".

In relation to NAO's finding about Information Technology services, MTI remarked that it "... *will make sure that for future projects a contract is duly signed by both parties*". Furthermore, the Ministry stated that "... *the performance guarantee was furnished and the service provided ... ... was satisfactory*". Additionally, the Contracts and Procurement Section within the Ministry "... *is ensuring that performance guarantees are submitted with the contract*".

When commenting about the procurement of the Architect's services, the Ministry claimed that it "... *was implementing a major project of national interest and which was being funded through EU Funding. The implementation period of the project was to expire by the end of 2015* ...". The projects in question "... *were subject to delays which could not have been anticipated due to the nature of the works, and resources were required to supplement the capacity in order to meet the deadlines* ...". Therefore a decision had to be taken by the Ministry and the request for the Architect's services was finalised. Nevertheless, the Ministry reiterated that "... *This was a one time event especially when the project had to be closed within the same year* ...".

Similarly, with regards to services provided by a consultancy company, MTI remarked that "... *Due to the nature of the project and the urgency of the investigation, immediate action had to be taken to get the process ongoing*. ..."

The Ministry also stated that it "... *will make sure that in the future Direct Order approvals are kept to a minimum, resorted to only in cases which are justified by the circumstances and requested in a timely manner*. *This will be enforced through the issuance of an internal circular delineating the process in relation to Direct Orders which will be disseminated amongst MTI staff*".

With reference to other works, although Management provided the original tender documents and relative contracts in relation to both suppliers, these were insufficient for NAO to assess the procurement process.

Lack of compliance with Standing Travel Regulations

The Ministry noted NAO's comments with regards to errors in the calculation of subsistence allowance forwarded to five officers and *"... will take the necessary action to recover funds ..."*. However, in the case of the remaining two officers, MTI claimed that *"... they did not opt for the lunch during the conference"*. Nevertheless, NAO disputes this comment since it was noted that both individuals did in fact avail themselves of a dinner during the conference.

The Ministry will also *"... issue a Circular in line with the PSMC that a travel report on each visit is to be submitted by the delegate to the Director responsible for Corporate Services by not later than one (1) month after the visit"*.

Shortcomings in relation to General-Use Vehicles

Management also confirmed that a memo in connection with the maintenance of logbooks was issued, *"... whereby every official travel, should be recorded according to section 8.2.4 of the PSMC. The logbook should contain the date, the destination and arrival of each trip, the duration of the trip, description of travel and the mileage. The officer in charge of the vehicle has to maintain a proper logbook and sign for each trip. Fuel will not be given if the logbook is not properly filled in"*.

Shortcomings related to Inventory

The Ministry is also *"... taking action to consolidate the inventory, particularly in anticipation of the Fixed Asset Register module for the accrual accounting (IPSAS). This exercise has already started in the summer of 2016"*.

Non-compliance with Fiscal Obligations

With regards to its fiscal obligations, MTI maintained that it *"... will chase suppliers to submit the fiscal receipts."*, and that "*Action is being taken so that quarterly or 'nil' returns are submitted on time*".

Transport Malta

Ex-Gratia Grant Scheme

Background

In pursuit of the implementation of one of the measures identified in the Budget 2014, the Government allocated the sum of €3.5 million to an *Ex-Gratia* Grant Scheme, managed by Transport Malta (TM). A further €2.3 million were then voted for same in the Budgetary Estimates for 2015. The aim of this Scheme is to refund the full amount of Value Added Tax (VAT) to vehicle owners who paid registration tax on vehicles registered and licensed for personal use, between 1 May 2004[1] and 31 December 2008[2].

The Scheme covers a seven-year period with separate calls for application being issued each year. Following an internal exercise, TM traced a total of 42,001 vehicles which were potentially eligible under this Scheme. A total of 29,154 eligible applications were received by TM in 2014, and a first instalment of €110 or €55, depending on the type of vehicle they applied for, was paid to these applicants. In aggregate, first instalments amounting to €3,136,540 were paid in 2014.

In 2015, TM issued separate applications and settled the remaining balances for vehicles registered and licensed for personal use between 1 May and 31 December 2004. Payments made in 2015 in full refund of the VAT due on vehicles purchased during this period, amounted to €2,316,241. These payments related to 3,366 applicants, 70 of whom applied for the first time during 2015, and hence received the full payment due to them during the same year.

The Authority will adopt the same process in the coming years until all payments for the eligible applicants up to 31 December 2008 are settled.

Eligibility under the Grant Scheme required applicants to be Maltese residents and at least 18 years of age. Additionally, the applicant had to be the first licensed owner of the vehicle, irrespective of whether the vehicle was still in his/her possession at the time of the application. Vehicles that were registered and licensed by motor car dealers or by companies were not eligible, although in these instances, the next or subsequent licensed owner who was not a dealer, was eligible.

Application from heirs of deceased persons were also eligible for the grant, as long as the former submitted a notary declaration together with the application.

[1] Malta's accession to the European Union (EU).

[2] The date when VAT was last charged on registration tax.

Furthermore, vehicles had to be registered for personal use under categories M1[3], N1[4], Motorcycles or Quad Bikes, during the intervening period, and each applicant was only entitled to refunds on a maximum of three vehicles. Vehicles used for hire and reward, or used for commercial purposes, were not eligible under this Scheme[5].

Audit Scope and Methodology

The scope of the National Audit Office (NAO) audit was to evaluate the level of controls in relation to payments made by TM with respect to the *Ex-Gratia* Grant Scheme during the financial year 2015 and the level of adherence to criteria related to eligibility.

In view of the fact that an internal audit[6] on the initial part of the Scheme had already been carried out by external private auditors appointed by TM, and any administrative issues were duly brought to light, it was decided that the NAO audit was to be carried out when the first payments in relation to cars registered in 2004 were effected.

NAO also conducted a thorough analysis of the data provided by TM. Specifically, the payments made in 2014, as well as the list of ineligible vehicles, were checked against the list of all potential applicants extracted by TM from its Vehicle Registration and Administration System (VERA). The scope of these tests was to ascertain whether the related vehicles were part of the full population, and in exceptional cases, the reasons for their inclusion and/or exclusion.

An assessment of the 2014 applications in dispute was also conducted. These applications were either deemed to be eligible or ineligible following a decision by a Board of Appeal, which was set up with the aim of considering dismissed claims. From information provided, a total of 729 applications were disputed following the 2014 application process. In 370 of these cases, the original decision was reversed on appeal, making the applicant eligible. NAO assessed the application pertinent to particular vehicles against the payments made by TM in 2014 and 2015, to ascertain whether such payments were indeed made in the case of eligible applications, or withheld if the application was ineligible.

A total of 30 payments, amounting to €119,385, were also randomly selected and testing was carried out to check whether the respective applicants fitted the pertinent eligibility criteria, as well as to ascertain the correctness of the amounts disbursed.

The registration tax for each of the selected payments was recalculated in line with the provisions of the Motor Vehicles Registration and Licensing Act, 1994 (Cap. 368), as amended by the Budget Implementation Act, 2004 (Act II of 2004). Such taxes were calculated as a percentage of the cost, insurance and freight value[7] of each vehicle, which was available from VERA. NAO feels it pertinent to point out that this value had to be taken as given, as this information was inputted in TM's system upon the initial registration of the vehicle.

Attention was also given to those second-hand vehicles that were imported from a non-EU country, since a minimum registration tax applied in these cases.

Additionally, from the list of ineligible individuals who applied in 2015, as provided by the auditee, three instances were selected, and testing was carried out to re-assess the reasons given for their ineligibility.

---

[3] Category M1 – passenger cars up to nine seats.

[4] Category N1 – goods-carrying vehicles with a mass not exceeding 3,500 kilograms.

[5] Vehicles bearing registration numbers *HQ, *QZ, **K, **Y, HRS, GV* were not eligible.

[6] The scope of the internal audit was to verify that the Scheme provisions were adhered to at the application processing stage, including the assessment of the eligibility criteria; and to check that the payment of grants was of €110 for vehicle categories M1 and N1, and €55 for motorcycles and quad bikes.

[7] Commonly referred to as the 'CIF' value.

Moreover, since the eligibility criteria stated that any one individual was only entitled to refunds on a maximum of three vehicles, the full population provided by TM was analysed to assess adherence to this requirement.

Good Practice

NAO was satisfied that procedures in relation to the *Ex-Gratia* Grant Scheme were in place and correctly followed by TM.

Furthermore, all relevant documentation was held in an organised manner and was made available for the audit upon request.

In more detail, NAO satisfactorily noted that for the sample tested:

- application forms were traced and duly filled in;
- the eligibility criteria in relation to payments were met;
- registration taxes and the pertinent VAT thereon, on the respective vehicles, were in line with the relevant standing regulations;
- minimum amounts of registration tax in relation to selected second-hand vehicles imported from a non-EU country, were correctly applied;
- the correct amounts were disbursed to applicants during 2015;
- the reasons for ineligibility, where applicable, were considered valid; and
- no individual was in receipt of more than three payments in 2015.

Management Comments

In its reply, Management fully concurred with NAO's reviews and comments, while expressing its satisfaction on the audit methodology adopted.

Ministry for the Economy, Investment and Small Business

Ministry for the Economy, Investment and Small Business

Expenditure

Background

The Ministry for the Economy, Investment and Small Business' (MEIB's)[1] initial approved budget allocation for 2015 amounted to €36,154,000, apportioned as follows: Personal Emoluments – €2,765,000; Operational and Maintenance Expenses – €890,000; Programmes and Initiatives – €23,425,000; and Contributions to Government Entities – €9,074,000.

During the year, MEIB's Recurrent Vote was increased to €36,527,538. However, payments as recorded in the Departmental Accounting System totalled €34,552,366, resulting in unutilised funds of almost €2 million. Major savings were registered in the Contributions to Government Entities, with €923,423 of unutilised funds, as well as Programmes and Initiatives, which closed the financial year with a positive balance of €834,501.

Audit Scope and Methodology

The main scope of the audit was to ensure that expenditure incurred by MEIB during the year under review, was appropriately recorded and processed, in accordance with pertinent regulations and circulars. The audit also sought to determine the level of existing internal controls over procurement and payments, as well as to establish whether Government resources were used prudently and in a judicious manner.

Audit work performed covered a sample of 20 Payment Vouchers (PVs), for a total value of €252,953, and covering over 22% of the amount paid by MEIB in operational and maintenance expenditure. A further 21 PVs, charged to Item 5752 – EXPO Milan 2015 (under Programmes and Initiatives) were also included in the audit sample. These transactions totalled €1,510,809, representing almost 96% of the total payments effected from this Item. The transactions included in the audit sample were mainly selected on a random basis, although the materiality and nature of the expense were also taken into consideration.

Since the largest expense charged to Operational and Maintenance Expenses related to travel (€241,698), audit testing was also performed on 10 visits abroad. These trips covered approximately 26% of the total cost of travelling abroad, as indicated on the list of overseas travel during 2015 compiled by MEIB and forwarded to the National Audit Office (NAO) for audit purposes. Verification performed by NAO included ensuring that travel arrangements met the requirements of the Public Service Management Code (PSMC), and that advances granted to officers travelling abroad were accurate and in accordance with standing regulations. Any refunds due by the travelling officers were also checked for timeliness, accuracy and completeness.

[1] During 2015, the Parliamentary Secretariat for Competitiveness and Economic Growth was attached to MEIB. This Secretariat ceased to form part of the Ministry as from 29 April 2016, following a Cabinet reshuffle.

NAO also performed random spot checks at the Millennia Building (Marsa) and Palazzo Zondadari (Valletta), to verify whether the Ministry's Inventory Database included the items selected for inspection, as well as to ensure that inventory items recorded in the database were actually located on site.

Key Issue

Contract Value exceeded and other Shortcomings

Following the approval 'in principle' granted on 14 March 2014, the Ministry for Finance (MFIN) issued its definite approval for the procurement of cleaning services at MEIB offices on 28 March 2014. The service was to be provided for a period of four months, at an hourly rate of €6.33 (Value Added Tax (VAT) excl.). The approval was granted on condition that the total amount of €12,000 (VAT excl.) was not exceeded.

The contract for the provision of cleaning services between MEIB and the service provider was dated 27 March 2014, *i.e.* the day before MEIB obtained the definite approval from MFIN. Whilst specifying the maximum contract price, the agreement did not indicate the duration of the engagement, *i.e.* the four months noted in MFIN's approval.

Audit testing revealed the following:

a. Although MFIN's definite approval covered a four-month period, payments were issued to the service provider for cleaning carried out between April 2014 and March 2015. No documentation was traced in the Ministerial file reviewed evidencing that this cleaning service was formally extended.

b. Since its engagement on 27 March 2014 till 29 April 2015 (*i.e.* the date on which the last payment was effected by MEIB), the service provider was paid a total of €70,017[2], thus exceeding the limit imposed in MFIN's definite approval, as transposed in the contract, by €55,857. In the absence of documentation to prove otherwise, payments effected to this service provider over the prescribed threshold were neither covered by Finance authority nor by a binding agreement between the contracting parties.

c. The Performance Guarantee submitted by the service provider covered only a three-month period, effective from 7 April 2014. For the remaining nine-month period to March 2015, no Performance Guarantee was in place, resulting in the Ministry not being legally covered.

Control Issues

Procurement, Agreements and related Payments

Back-dated Contract entered into with the Malta Information Technology Agency

a. An agreement between MEIB and the Malta Information Technology Agency (MITA) indicated the contract effective date as being 1 January 2015. However, it was only officially endorsed on 25 January 2015. Furthermore, through an amendment made on 27 February 2015, both parties agreed that the provisions of this contract were to be effective as from 1 January 2014. This resulted in the provisions of the contract being applicable almost 13 months prior to the date of signing of the same agreement.

   In fact, according to the log of hours supporting the first claim for payment by MITA, work on the project had already commenced in August 2014, implying that the provisions of the contract had already come into effect when MEIB endorsed the agreement.

[2] As from 1 January 2015, MEIB was charged at the hourly rate of €6.35 (VAT excl.) instead of the contracted rate of €6.33 (VAT excl.).

b. Although MEIB was to be charged on a time and material basis as *per* hourly rates stipulated in the agreement, the value of the project was capped at €47,400. Nonetheless, payments effected to MITA in relation to this project totalled €47,788, *i.e.* €388 over and above the capping laid down in the agreement.

Inconsistencies in obtaining Quotations for the Lease of a High-end Vehicle

a. In August 2013, MEIB requested quotations from three car rental companies for the lease of a high-end vehicle, for official use. Whereas in two requests for quotations, MEIB indicated that the rental charge was not to exceed a fixed daily rate, in the third instance, the car rental company was given the option to quote at a higher rate. One of the former two service providers stated that the suggested rate was too low for a high-end car and opted not to submit a quotation. On the other hand, the service provider who was given the option to quote at a higher rate, offered a choice of three vehicles at different rates. The vehicle was eventually rented from this latter service provider at a total cost of €45,650 (VAT excl.). The agreement, backed up by a direct order approval from MFIN, covered a five-year period commencing on 1 January 2014.

b. The vehicle leased by MEIB cost an additional €4.50 *per* day than the pre-established threshold in the request for quotations which it sent to the selected service provider.

c. An email requesting further details on the type of vehicle required, sent by one of the service providers the day following MEIB's request for quotations, was answered by the latter almost two months later. In fact, MEIB replied to this service provider on 2 October 2013, *i.e.* the same day it obtained the direct order approval from MFIN to enter into a five-year agreement with the successful bidder. Therefore, the options eventually presented by the above-mentioned service provider were futile, since the Ministry's selection had already taken place.

Overtime not charged in accordance with Tender Document

On 1 August 2015, a service provider invoiced MEIB a total of €2,955, for cleaning performed during the previous month. The same invoice included a charge for eight hours of overtime at 1½ times the contracted hourly rate. Timesheets attached to the respective invoice indicated that the overtime in question was performed on a weekday.

Since the contract signed between the two parties failed to indicate the applicable procedures in case of additional hours, reference had to be made to the Tender Document issued for the provision of cleaning services, which specified that overtime was only chargeable for services provided on Saturdays, Sundays and Public Holidays.

Therefore, the above-mentioned overtime charge was not in accordance with the Tender Document.

Sponsorship not covered by an Agreement

a. According to an undated Letter of Intent, MEIB confirmed its intention to enter into an agreement with an association to sponsor a television campaign through the reimbursement of up to €10,000 to cover part of the respective costs. The parties were to enter into a formal agreement "... *ideally by and in any event before the 10th of December of 2015*". However, no such agreement was traced to the departmental file reviewed. Following NAO's query on the matter, MEIB stated that since it had already effected the reimbursement of €10,000 on 14 December and there was no further obligation by either party towards each other, it was no longer deemed necessary to enter into an agreement. On the other

hand, the conditions and obligations set out by both parties did not have a legal basis since, as stated in the document itself, the Letter of Intent was not meant to be legally binding.

b. Furthermore, although according to the Letter of Intent, the reimbursements of costs were to be made against the submission of fiscal receipts compliant to VAT obligations, none were traced to the departmental file reviewed.

Documentation

Transfer of Vehicles not appropriately documented

During audit testing, NAO encountered monthly payments for the lease of two vehicles, one in official use and the other for general-use purposes. Apart from an undated minute in each of the two files held by the Ministry for Tourism, indicating that "*vehicle is being transferred to MEIB*", no further documentation supporting this claim was traced to the departmental files of the respective vehicles held by MEIB.

In reply to NAO's request for documentation relating to these transfers, MEIB stated that it took over the two vehicles, originally leased by the Ministry for Tourism, following a Cabinet reshuffle in April 2014. In fact, the lease agreements in place indicate the 'Ministry of Tourism' as the lessee.

Since no formal documentation evidencing the transfer of these vehicles was made available for audit purposes, it could not be ascertained that the said transfers were duly authorised by both Ministries.

Expo Milan 2015

The 2015 Expo was held in Milan between 1 May and 31 October, with Malta's participation being coordinated by Malta Enterprise (ME), as the national agency responsible for promoting and facilitating international investments in the Maltese Islands. A total of €2,000,000 was allocated for this Programme and Initiative, with actual payments amounting to €1,574,954.

All procurement relating to Malta's participation in the Expo Milan 2015 was carried out by ME, with the entity being invoiced for the respective goods and services purchased. The main invoices, once approved by ME, were forwarded to MEIB for payment to be effected. However, for practicality's sake, ME paid for certain invoices itself and subsequently claimed reimbursement from the Ministry. Therefore, MEIB's role in relation to Malta's participation in the Expo Milan 2015 was that of effecting payments on behalf of ME.

Lack of Supporting Documentation for Expenditure relating to the organisation of the Malta Day Concert

As part of the Malta Day celebrations on 16 July 2015, the Malta Philharmonic Orchestra held a concert in the Expo Auditorium. Although the Orchestra's services were delivered free of charge, it was not responsible for any additional costs that were incurred in conjunction with this concert. In fact, on 13 November 2015, the Malta Philharmonic Orchestra was paid €11,050, as a reimbursement of expenses incurred, consisting of production and subsistence allowances paid to musicians, the engagement of self-employed musicians, purchase of music, hire of musical instruments, as well as insurances and flight tickets.

In conducting audit testing, NAO noted the following:

a. In a reply to NAO's request for any contractual agreement entered into between ME and the Orchestra in relation to the Malta Day Concert, ME stated that no formal agreement was signed by the parties "*... since despite reminders, the MPO[3] never complied*".

[3] *i.e.* the Malta Philharmonic Orchestra.

b. Given the absence of a formal agreement, NAO queried on why ME was responsible for the payment of the production and subsistence allowances to musicians, which totalled €6,825, as well as how the rates of these allowances and the charge of €1,619 for the engagement of the self-employed musicians were established. Although various correspondence relating to the above-mentioned concert was forwarded to NAO, none of the documents made available provided the required information. As a final reply to NAO's query, ME stated that apart from accommodation and flights, for which it paid directly, and travel insurance, which was reimbursed to the Malta Philharmonic Orchestra, the other payments were "... *based on agreement with* ..." a high-ranking administrator of the Orchestra.

   Without the necessary documentation supporting the reimbursement claimed by the Malta Philharmonic Orchestra, it could not be ensured that the expenses relating to the Malta Day concert, paid for by MEIB, were accurate and justifiable.

Audit concern about Approval obtained from the Ministry for Finance

When NAO requested documentation, including approvals, supporting the payment of a number of expenses falling in the audit sample, which totalled €80,949, ME stated that these were all related to the Malta Day concert, an event which was discussed and approved by MFIN's Permanent Secretary.

In support of this latter statement, ME forwarded an email sent to MFIN's Permanent Secretary on 18 June 2015, in which it made reference to the organisation of activities for the Malta Day at the Expo Milan 2015 and for which, the Permanent Secretary had given "... *verbal agreement during our meeting in February of this year*". Furthermore, through the same correspondence, ME sought MFIN's approval for "... *an additional €16K over and above the DO verbal approval of €70K which cover other arrangements for the MPO[3] such as flight, internal transport, accommodation, rehearsal hall in Milan, insurance and per diem*".

On 27 June 2016, *i.e.* during the audit, ME notified Permanent Secretary – MFIN of NAO's request for documentary evidence to substantiate the above-mentioned verbal approvals, to which the Permanent Secretary replied "*Approved*". Therefore, since written approval from MFIN was only obtained upon NAO's request, it could not be ascertained that the payments selected in the audit sample were duly authorised. NAO questions whether payments should be made on the basis of verbal approvals.

Permanent Secretary Approval sought subsequent to Payments

Audit testing revealed three instances where the authorisation for payment was sought on the same day or subsequent to the issue of the respective payment, thus rendering the eventual granting of MEIB's Permanent Secretary's approval superfluous:

a. On 11 June 2015, the Director Corporate Services MEIB requested the Permanent Secretary to endorse a payment of €34,800 for managing services at the Malta Pavilion, with the approval being granted on the same day. However, both the Telegraphic Transfer and the Funds Transfer Form, were issued on 10 June.

b. Similarly, the Permanent Secretary's approval for the payment of €29,000 for the renting of equipment, was requested on 9 July 2015, the same day as the issue of the Telegraphic Transfer and the Funds Transfer Form. The approval was granted on 13 July 2015.

c. In another instance, the Permanent Secretary approved a payment on 16 July 2015, when the payment, amounting to €10,899, had already been made by Telegraphic Transfer on 14 July 2015.

No Agreement for the Provision of Video Production and Photography

In December 2014, MEIB requested the Public Broadcasting Services (PBS) to submit a quotation for the provision of video production and photography for the Malta Pavilion at the Expo Milan 2015. Two invoices

were issued by PBS, dated June and September 2015, for services rendered in relation to the Expo, for a total value of €100,300.

Various attempts, both written and verbal, were made by MEIB to PBS for the latter to propose a draft contract in relation to the above-mentioned services. However, PBS did not accede to their request, and consequently, the services rendered were not backed by a formal agreement.

Shortcomings in Reimbursements effected to Malta Enterprise

a. Included in one of ME's claims for reimbursement was a transaction of €22,000 relating to the construction of a stand. When NAO queried on this expense, ME confirmed that, although the expense was in connection with an event which also took place in Milan, it was not related to the Expo. Therefore, the transaction was erroneously included in the claim forwarded to MEIB and incorrectly charged to the Programme and Initiative – EXPO Milan 2015. ME further stated that action was to be taken to reverse this payment.

b. Claims for reimbursement by ME included expenditure relating to equipment, such as laptops, a personal computer and a printer, presumably purchased for utilisation during the Expo Milan 2015. The Ministry's Director stated that after the conclusion of the Expo, the equipment was retained by ME and registered in the latter's inventory, even though these items were ultimately paid for by MEIB.

c. On 1 October 2015, MEIB's Director requested documentation from ME in support of a sample of transactions selected by MEIB itself, totalling €22,392 and claimed for reimbursement, with the requested documentation reaching MEIB the following day. However, the Ministry had already refunded the respective expenditure on 30 July 2015, *i.e.* two months earlier. It is unclear whether MEIB intended to carry out verifications on the sample of invoices or if the documentation was requested for record-keeping purposes.

Travel

Overpayment to Travelling Officer

In the Statement of Expenses compiled following a trip to Ukraine between 19 and 24 June 2015, the accommodation expenses equivalent to €1,190 were included under both 'Hotel Bill' and 'Other receipts'. As a result of this error, the travelling officer was refunded €327, when he should have reimbursed the Ministry €863.

The air tickets for this trip had already been purchased three days before the Permanent Secretary's approval.

Purchases not considered as relating to Official Business claimed as Travel Expenditure

a. Included with supporting documentation for expenditure claimed as 'Other Receipts' in the Statement of Expenses for the Ukraine trip mentioned above, was a receipt for the purchase of personal items. It follows that these items, worth the equivalent of €296, were paid out of the contingency money granted to the travelling officer.

b. The hotel bill for a visit to Dubai by a Ministerial Delegation between 16 and 19 September 2015, included charges for alcoholic beverages in the region of €756, approximately €318 of which were from a mini-bar.

Advances forwarded in Cash

During audit testing, NAO noted that advances to a politically-exposed person, for use during visits abroad, were forwarded in cash. The Ministry confirmed that advances in cash were only made to this person, whilst other travelling officers received theirs by means of a credit transfer.

Nature of Expenses not identifiable from Supporting Documentation presented by Travelling Officers

A review of documentation supporting the expenditure incurred on the trips selected in the audit sample revealed that in the following instances, the nature of the purchase made was either difficult to identify or not identifiable at all. Thus, NAO could not ascertain that the inclusion of these expenses in the respective Statement of Expenses, and the eventual reimbursement out of public funds, was in conformity with the provisions of the PSMC:

a. Although the Statement of Expenses following the Dubai trip included a claim for 'Other Receipts' equivalent to €584, receipts traced to file only totalled the equivalent of €491. Therefore, it could not be established what the remaining expenditure of approximately €93 related to.

b. Documentation supporting expenses claimed by the travelling officer following the trip to Ukraine indicated the nature of the respective purchases in the country's native language. Furthermore, the Statement of Expenses also failed to provide information on the type of purchases made, since all expenses, totalling the equivalent of €1,637, were classified as 'Other Receipts'.

c. Similarly, documentation supporting most of the expenses claimed by the delegation following a trip to Xiamen, China, indicated the nature of the respective purchases in the country's native language. Apart from receipts which could be identified as relating to transport expenditure, the remaining receipts, totalling the equivalent of €775, were classified as 'Other Receipts' in the Statement of Expenses.

   Furthermore, out of this amount, expenditure of approximately €653 was not covered by fiscal receipts but by point-of-sale chits, which provided no information on the items purchased.

d. Only the last page of the hotel invoice for a visit to Monaco between 22 and 25 May 2015, indicating a total charge of €2,003, was traced to the respective file. Since the accommodation charge (breakfast included) was paid by Telegraphic Transfer on 14 May, the complete invoice was requested by NAO in order to verify the nature of these additional charges. However, MEIB stated that the full documentation was not available, and was "*probably misplaced*".

e. The hotel invoice for the Ukraine trip traced to the respective file also just showed the total charge, equivalent to €1,190. When NAO requested the full invoice, MEIB once again stated that this was not available, as it was probably misplaced.

Errors noted in the Travel Documentation and other Shortcomings

The following errors and shortcomings were noted by NAO while performing testing on documentation relating to the 10 trips abroad selected in the audit sample:

a. In nine out of the 10 Visits Abroad on Official Duties (referred to as GA27) and Visits Abroad on Official Duties (Ministerial Delegations) (GA27A) forms reviewed, the 'Breakdown of Estimated Expenditure' failed to include the travelling expenses (air fares) which totalled €29,606.

   Furthermore, apart from the air fare, the GA27A form for the Monaco trip also failed to include the accommodation expenses of €8,000 in the 'Breakdown of Estimated Expenditure' section. Thus, figures on the GA27 and GA27A forms, did not give a true indication of the visits' total cost prior to their approval.

b. As specified on the form itself, Section C of the GA27 is to be completed before departure of the delegation. However, in the case of the Singapore visit between 28 February and 14 March 2015, the travelling officer endorsed this Section on 2 March 2015, *i.e.* during the duration of the visit!

c. Although an information brochure of the Course on Developing e-Government Strategies held in Singapore was available, a detailed programme, as *per* Section 8.9.1.1(c) of the PSMC, was not traced to the respective file.

d. No reports following the attendance to the above-mentioned course held in Singapore and the participation in the Global Conference on Cyberspace 2015 held in The Hague, Netherlands, were traced to the respective files.

e. According to an invitation letter dated 25 September 2015, the Forum of Marine Cooperation between China and South European Countries was to be held in Xiamen, China between 7 and 8 November 2015. Since only the event programme for 7 November was traced to file, NAO requested MEIB to indicate the exact duration of the forum. Although the Ministry confirmed that the programme for both days was available, it failed to forward that for 8 November, despite being specifically requested by NAO.

f. The Post-Travel Submission Form for the Monaco trip was not traced to file. When queried on the matter, MEIB stated that the form had been compiled, but was only filed at the time of audit. The Ministry failed to produce a copy of the form when requested by NAO.

Inventory

Discrepancies noted during Physical Inspections

Physical inspections performed by NAO on a sample of entries in the Inventory Database, recording items located at Palazzo Zondadari and the Millennia Building, revealed the following shortcomings:

a. In five instances, the quantity of assets as recorded in the Inventory Database differed from the actual quantities found on site.

b. Four items were found in a different location than that indicated in the Inventory Database, and a few others were not included in the Inventory Database of Palazzo Zondadari.

c. Three paintings were not found in the location as indicated in the Inventory Database. Although a number of paintings were found in a store within the same premises, in the absence of further details, it could not be ascertained that these were the ones supposed to be found in the location as *per* Inventory Database.

Recommendations

Key Issue

Contract Value exceeded and other Shortcomings

The Ministry is to ensure that all the conditions laid out in Finance approvals are abided with. Where it is envisaged that the service will be required for a longer period than catered for in the original approval granted, guidance is to be sought from MFIN accordingly. Moreover, the agreement and Performance Guarantee are to cover the full period for which the service is needed.

Control Issues

Procurement, Agreements and related Payments

Back-dated Contract entered into with the Malta Information Technology Agency

Agreements with service providers are to be endorsed by all parties prior to their effective date, or as close to it as possible. Additionally, contracts with third parties are to be continuously monitored in order to ensure that all the clauses, including payment terms, are fully respected and complied with.

Inconsistencies in obtaining Quotations for the Lease of a High-end Vehicle

Whilst all requests for quotations for the procurement of a particular good or service sent to prospective suppliers are to contain identical information, any queries raised by these suppliers are to be answered in a timely manner. This will enable the Ministry to have sufficient comparable information for the selection of the best option from the ones made available. MEIB is also to ensure that only bids that satisfy the pre-established requirements are ultimately chosen.

Overtime not charged in accordance with Tender Document

The Ministry is to ensure that invoicing by service providers is in accordance with the rates and conditions stipulated in both the Service Contract, as well as the respective Tender Document.

Sponsorship not covered by an Agreement

A policy decision has already been taken by MEIB whereby, in future, similar reimbursements falling over such a short transaction period will be immediately provided for through an agreement without the prerequisite of a Letter of Intent, thus simplifying bureaucratic procedures.

Documentation

Transfer of Vehicles not appropriately documented

Any transfer of vehicles from one Ministry to another is to be duly authorised and backed by supporting documentation. This is to be retained and appropriately filed for future reference.

Furthermore, since the agreements for the above-mentioned leases were entered into by the 'Ministry of Tourism', one is to consider whether to revise such contracts to reflect the current lessee of the said vehicles, or to enter into new lease agreements.

Expo Milan 2015

Lack of Supporting Documentation for Expenditure relating to the organisation of the Malta Day Concert

Similar procurement of services is to be consolidated by an agreement, clearly indicating each of the contracting parties' financial responsibilities. This agreement is to be duly endorsed and retained for future reference.

Audit concern about Approval obtained from the Ministry for Finance

Requests for direct order approvals are to clearly indicate the expenses for which MFIN authorisation is being sought.

Furthermore, whilst verbal approvals are to be avoided, if circumstances necessitate that authorisations are obtained in this manner, MEIB is to ensure that such direct order approvals are ultimately backed by official ones.

Permanent Secretary Approval sought subsequent to Payments

Expenditure warranting approval prior to being paid is to be duly and timely authorised by the right level of authority, as *per* standing procurement regulations.

No Agreement for the Provision of Video Production and Photography

The Ministry is to persist in its requests for agreements to be in place and duly endorsed by the contracting parties before the respective services are carried out.

Shortcomings in Reimbursements effected to Malta Enterprise

Although ultimately both MEIB and ME obtain their finances from the Consolidated Fund, for better accountability, it is to be ensured that expenses are borne from the appropriate Vote or Item.

Travel

Overpayment to Travelling Officer

All statements of expenses, together with the supporting receipts, are to be thoroughly checked. Calculations are also to be recomputed to ensure that amounts claimed and refunded are accurate.

Furthermore, the above-mentioned situation is to be rectified and the amount of €1,190 recouped by MEIB.

Purchases not considered as relating to Official Business claimed as Travel Expenditure

The Ministry is to ensure that only justified incidental expenses and purchases incurred on official business are expensed out of contingencies. Furthermore, statements of expenses submitted by travelling officers are to be duly verified to ascertain that expenses claimed are in line with the requirements of the PSMC.

Claiming reimbursement for presumably personal purchases is also to be considered by MEIB.

Advances forwarded in Cash

For security reasons, the Ministry is to consider limiting the amount of cash advances and apply the procedure utilised in the case of other Ministerial and Private Secretariat travelling officers.

Nature of Expenses not identifiable from Supporting Documentation presented by Travelling Officers

Statements of expenses following official travel are not to be processed by MEIB, unless all purchases claimed as refundable expenditure are supported by adequate documentation. In the event that the receipts are in a language other than English, the travelling officer is expected to state the nature of the purchases made.

Errors noted in the Travel Documentation and other Shortcomings

The Ministry is expected to be fully compliant with all the relevant provisions of the PSMC as regards visits abroad.

Inventory

Discrepancies noted during Physical Inspections

Whilst MEIB is to continue in its exercise of keeping the Inventory Database up-to-date, periodic physical verification of records is also encouraged, to ensure that inventory records truly reflect the description, quantity and location of items. Any transfer of assets, both permanent and temporary, is also to be duly recorded.

Management Comments

Management took note of the majority of observations and recommendations put forward by NAO, and explained that these will be integrated into MEIB's Financial Management, Monitoring and Reporting Policy. This Policy, which came into effect in January 2016, provides a comprehensive overview of the main principles of modern management and serves as a day-to-day guide for officers involved in financial management and control. In its reply, Management also confirmed that it will be taking all necessary actions recommended by NAO to continue adhering to the Financial Regulations and good practice.

Furthermore, the following comments on a number of NAO's observations were forwarded:

- Management stated that "... *the lack of request for a definite approval for the extension of this* [cleaning services] *contract was due to an oversight* ...", whilst confirming that, in future, all necessary approvals will be obtained and properly filed.

- Management took note of NAO's observations in relation to Expo Milan 2015, together with the corresponding recommendations, which were duly communicated to ME to ensure that these are implemented and continuously monitored. Moreover, MEIB will ascertain that any future similar programmes/projects, will be coordinated and monitored as *per* NAO's recommendations.

- In reply to NAO's observations on travel abroad on official duties, Management stated that it:

  - will be taking the necessary actions to recoup the overpayment made to the person travelling to Ukraine;
  - "... *will try to limit the amount of cash advances*"; and
  - will take the necessary actions to ensure that bills for expenditure incurred on official business are itemised and in the English language, as well as that proper documentation is provided.

Management however did not properly address NAO's observation on purchases not considered as relating to official business claimed as Travel Expenditure.

In its concluding remarks, MEIB recognised that NAO's Report raises issues which need to be addressed. The Ministry remarked that "... *over the past months a number of actions have already been implemented to address certain issues raised in this report. In the immediate future Management will address the remaining issues by developing an action plan, where the ultimate goal will be to have the necessary change in structures, policies and standards of procedures that will ensure the full abidance with relevant governing rules and regulations*".

Commerce Department

Trading Licences Revenue

Background

The Commerce Department (CD) was set up towards the end of 2000, to assist business and facilitate trade, whilst providing the necessary infrastructure to encourage the securing, utilisation and respect of intellectual property rights.

As detailed in Article 2 of the Trading Licences Act, 2002 (Cap. 441) (TLA), a '*commercial activity*' in Malta refers to the exercise of any trading or economic activity, including the sale of goods and the provision of any services, as may be prescribed, irrespective of whether such commercial activity is exercised from commercial premises or otherwise. This excludes any commercial activity regulated under any other law.

According to Article 10(1) of the same Act, "*No commercial activity shall be carried out in Malta without a licence from the regulatory authority*." Article 4 of S.L. 441.07 of 2006 – 'Trading Licences Regulations' (TLR), designates the Trade Licencing Unit within CD as the regulatory authority responsible to issue trading licences in respect of commercial and other activities as established in TLA and TLR.

A person who wishes to carry out a commercial activity listed under Part 1 of the First Schedule of TLR, is thus required to submit an application for a trading licence with CD. The applicant must not commence any commercial activity before a formal licence is issued. On the other hand, a person who wishes to carry out a commercial activity listed under Part 2 of the First Schedule of TLR, is required to submit a notification to CD within 30 days from the commencement date of such activity. Once the notification is submitted, the person is deemed to be licensed.

Commerce Department caters for six types of licences, being premises-based, non-premises based, busker[1], street hawker, market hawker and marketing agent. The application for these type of licences is to be submitted to CD and shall be filled in appropriately, including all required details, supporting documentation and relative payment, depending on the type of activity.

[1] A person who produces on site and sells a work of art.

Audit Scope and Methodology

The scope of the audit was to assess revenue from trade licences during the year under review and to evaluate the level of existing controls and procedures in place, in relation to the collection of arrears of revenue.

The introductory meeting was followed by a walkthrough, whereby the application process, renewals, cancellations, deposits and arrears were discussed and analysed in further detail.

Licences registered under TLA as at end 2015 was 18,030, for a total value of €1,609,951. This comprised 17,526 active licences with a total of €1,529,006, and 504 temporary pending licences amounting to €80,945. Out of the full list of active licences, 1,616 related to new licences issued during the year under review, totalling €85,449.

Initial testing conducted by the National Audit Office (NAO) comprised a thorough analysis of the data provided by CD. A sample of 40 trade licences, amounting to €13,191, was selected randomly to verify the procedures in place with respect to trade licence revenue, from the application stage to the deposit of funds into the Public Account held at the Central Bank of Malta. Particular consideration was given to the materiality of the licence fee and the date of issuance.

Further testing was conducted by NAO to verify the procedures in place with respect to the Department's reported arrears of revenue. Another sample of 20 trade licences, with outstanding arrears of €38,769 was selected for testing purposes. Such licences were classified as Active[2], Temporary Pending[3] and Withdrawn[4] in the Licensing Management System (LMS).

NAO also verified the correctness of total revenue for the year under review as reported in the LMS *vis-à-vis* the Departmental Accounting System (DAS). Reconciliation between the two figures was conducted by the Department upon NAO enquiry and discrepancies were analysed accordingly.

Key Issue

Insufficient Verification of Application Detail Requirements

An application for a trading licence submitted to CD contains details, such as name and address of the applicant carrying out the commercial activity, proof of identification, details of the legal entity (where applicable), Value Added Tax (VAT) registration number, permit(s) issued by the then Malta Environment and Planning Authority (MEPA) and other requirements as deemed necessary.

Although the Business Care Unit within CD checks that each application form has been filled in appropriately and that all required documents have been submitted, NAO did not trace any evidence in file that information listed in the application form, such as the area of the premises (in square metres) used for the commercial activity, MEPA permit number and VAT registration number, were verified for their correctness, either with the respective authorities or through physical inspection of the premises. CD verbally stated that in case of trading licences issued in recent years, the Department relies on the information submitted by the respective applicant and this is considered correct unless proven otherwise.

Furthermore, NAO did not trace any evidence in file that CD confirmed that, prior to date of application, the applicant(s) would have not commenced operations.

[2] Active licences during 2015.
[3] Licences awaiting cancellation, having arrears accumulating on a yearly basis.
[4] Withdrawn licences with an outstanding balance in arrears to be paid.

Control Issues

Discrepancies between the Department's Reporting Systems

The Department records all transactions in relation to trade licences using LMS, which captures all information on any trade licences administered by the Department. The Accounts Section within CD makes use of DAS to record all related monetary transactions.

Whilst examining LMS and DAS reports provided by CD, pertaining to revenue from trade licences for the year ended 31 December 2015, it transpired that the closing figure as reported in DAS (€1,752,734) was not in agreement with that reported in LMS (€1,633,092). Upon further enquiry, CD provided additional information to reconcile both figures, and confirmed through correspondence that such discrepancy mostly related to timing differences. However, after examining such reconciliations, NAO noted that a resulting difference of €9,283 remained unexplained.

Shortcomings in relation to the Collection of Arrears of Revenue

The Department confirmed that, as from 2013, action was taken to control the high amounts of arrears due[5]. To this effect, a number of Official Letters were issued to defaulters, stating the full amount of arrears due to Government, whilst simultaneously, an exercise was conducted to categorise properly the full list of arrears as reported to the Treasury Department.

Accumulation of Arrears due to Delayed Action by the Department

Testing revealed that in a number of cases, revenue in arrears was accumulated to significant high amounts over a considerable period, due to untimely or insufficient action taken by the Department. The following instances refer:

a. Active Licences

In eight[6] instances from the sample selected, a Judicial Letter or Notification was issued to the defaulters of the active licences in question, followed by an annual reminder generated automatically by LMS. However, no further evidence was traced in file with reference to other departmental action taken to control the increasing levels of uncollectable licences. Total arrears of revenue pertaining to these instances amounted to €240,252.

Three of these licences, totalling €182,051 in arrears, are outlined as follows:

i. From the sample selected for testing purposes, NAO noted that a licensee had two licences which were issued by CD, bearing €21,340 in arrears of revenue. Further enquiry revealed that an additional €57,521 were also due by the licensee, pertaining to other trading licences held by same, resulting in a total arrears of €78,861. It was confirmed from LMS that in 2013, a Notification was sent to the defaulter, to pay the amounts due in question, followed by a Judicial Letter in relation to amounts relating to 2008 and the previous years.

   During the audit, NAO noted that an on-site visit was held, upon CD's initiative, by the Department's officials in the beginning of 2016. Meanwhile, NAO traced in file, correspondence between CD and the licensee, where the Department asked for additional information to be able to proceed with the cancellation of seven trade licences which were not active anymore.

[5] Arrears are triggered following the first year when the trading licence is issued and paid.
[6] Two of such instances included more than one licence pertaining to the same individual, having arrears of revenue as at end of year.

ii. Another licensee had a total of €56,808 in outstanding licences due to Government as at end 2015. It transpired that arrears accumulated annually since 2002. As evidenced by information held in LMS, CD resorted only to the issuing of renewal notices on an annual basis. However, the applicant did not settle the outstanding balance. NAO noted that in 2013, a Judicial Letter was issued to the defaulter to regulate his position within seven days. Nonetheless, the licensee did not settle the pending amounts. Up to the conclusion of audit testing, the Department was still in the process of finalising licence cancellation proceedings, which initiated in April 2014.

iii. NAO confirmed against information available in LMS that on another particular licence, the amount due in arrears from 2007 totalled €25,362. Further enquiry revealed that an additional €21,020, pertaining to other trading licences held by the same applicant, were also due by the licensee, bringing a total of €46,382 as outstanding to Government. In 2013, CD issued a Notification to the defaulter to settle dues, followed by a Judicial Letter, whilst further annual reminders were sent in the subsequent years up to date of testing. However, no payments were affected by the defaulter and no further action by CD was traced in file.

b. Temporary Pending Licences

From the sample selected, NAO noted that in five[7] temporary pending cases, with an aggregate amount of arrears totalling €151,999, unpaid licences were still accumulating annually, even after the initiation of licence cancellation proceedings, where applicable.

The following cases pertaining to two of the defaulters relate:

i. Review of a particular file revealed that the company which the licensee represented, ceased trading in 2001. This was confirmed by an extract from the Government Gazette and a Notice of Appointment of Liquidator by the Court, traced in file. Minutes in the latter showed reference to the case by CD commencing in 2011, where the Director requested the advice of the Attorney General regarding the way forward.

   It transpired that since the Department did not register its credits when requested to do so by the liquidator, CD was not in a position to make a claim to this effect. In fact, in 2015, the Department stated that given these circumstances, the fees were considered as not due. However, no further action was taken up to date of audit testing, with total arrears of revenue amounting to €41,442.

ii. Another file tested revealed that a particular licensee had aggregate arrears of revenue amounting to €26,666 pertaining to two trading licences. The respective file could not be traced at CD, since this licence was issued by the Police Department prior to 2002. In fact, in 2013 LMS was updated with information from the Common Database, which revealed that the licensee deceased in 2002, and the licence had originally been issued on behalf of a company. However, up to date of testing, no further action was taken by CD to verify the existence of the company in question.

c. Withdrawn Licences

NAO selected five cases having a withdrawn licence, following a Cancellation Form submitted by the licensee. Although the status of the licence was set as 'withdrawn' in LMS, the Department is still chasing the applicants in question to recoup the amounts due. A total of €22,387 in arrears of revenue related to such cases.

[7] Two of such instances included more than one licence pertaining to the same individual, having arrears of revenue as at end of year.

Accumulating Arrears of Revenue with no Guarantee of Recoupment

A total of 36 trade licences pertaining to selling of roses, hiring of sunbeds/umbrellas, cleaning of shoes and selling of tickets, were categorised as 'temporary pending'. These licences were originally issued by CD. However, CD confirmed that after issuing such licences, it opined that these should have never been issued in the first place. Thus, these were categorised as 'temporary pending'. Total arrears arising from such licence categories amounted to €8,005.

Upon enquiry, NAO noted that these licences were included with the list of arrears of revenue as at year-end, with the respective licence fee being charged annually in LMS. However, no Renewal Notices were ever served to such licensees due to their pending status. NAO is thus concerned that licences, so categorised, do not fall under the direct responsibility of a particular department. Therefore, Government revenue is essentially being forgone.

Compliance Issue

Remittances to Public Account not effected in a Timely Manner

During the year under review, the day-to-day work schedule was the responsibility of only one Accounts Officer. In view of the limited human resources, it transpired that bank remittances and reconciliations were not being performed on a daily basis. Moreover, all stages of collection, recording and depositing of monies were done by the same designate.

To this effect, NAO testing revealed that CD took long intervals to deposit revenue received as trade licences fees at the Central Bank of Malta. This was in contravention of Article 36 of S.L. 174.01 of the General Financial Regulations, 1966.

In seven instances, more than 31 days had elapsed for the deposit to take place. In two of such cases, NAO further noted that deposits were effected in the Public Account after more than 70 days. *Table 1* refers.

Table 1: Number of Days between Receipt Date and Remittance to Public Account

Number of days	Number of payments [8]	Amount
		€
On same day	6	2,211
Between two and five days	10	2,048
Between six and 10 days	2	1,798
Between 11 and 30 days	11	3,752
Between 31 and 60 days	4	1,126
More than 61 days	3	1,008
Totals	**36**	**11,943**

Recommendations

Key Issue

Insufficient Verification of Application Detail Requirements

NAO recommends that CD liaises with other entities, such as the then MEPA, the VAT Department and the then Employment and Training Corporation, to verify that trading activity commenced as declared in the application form, whilst 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.

Finally, NAO opines that the Department is to enforce penalties, as stipulated in TLA, to avoid situations where businesses without a trading licence commence operations without proper authorisation.

Control Issues

Discrepancies between the Department's Reporting Systems

NAO recommends that reconciliations are 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.

Shortcomings in relation to the Collection of Arrears of Revenue

Accumulation of Arrears due to Delayed Action by the Department

It is highly recommended that the Department increases its efforts to control arrears of revenue and reduce such amounts to an acceptable level. Timely and effective action is to be taken in all circumstances in order to safeguard the interests of the Department and collect what is due to Government.

In cases where Renewal Notices are issued to licensees but no payments are effected within the stipulated timeframe, CD must take note of such defaulters, and proceed with immediate action to recoup such amounts, thus enhancing the collection process. By immediately identifying payment delays, and taking corrective action in a timely manner, situations of legal prescription or misinformation will be minimised.

Furthermore, the Department ought to apply the penalties as stipulated in Article 18 of TLA, on those defaulters who repeatedly ignore Renewal Notices and do not settle the amounts due to the Department within a reasonable timeframe.

Accumulating Arrears of Revenue with no Guarantee of Recoupment

NAO recommends that this situation is to be resolved as soon as possible, so that arrears of revenue reported by the Department reflect the real position of outstanding amounts due to CD.

[8] Payments can be effected by cheque, cash or online.

Compliance Issue

Remittances to Public Account not effected in a Timely Manner

NAO opines that the strengthening of the Accounts Section will enable the Department to improve the internal control setup, as well as assist in reducing inherent risks. In line with best practice, 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.

Management Comments

In its reply, Management agreed with most of the observations and recommendations put forward by NAO. Moreover, apart from the comments mentioned hereafter, CD felt that the Report raised issues which need to be addressed.

The following comments were also forwarded:

Insufficient Verification of Application Detail Requirements

The Department stated that the absolute majority of commercial outlets in Malta (representing 89.26% as *per* LMS records) occupy less than 200 square metres. On the other hand, there are 141 outlets which occupy over 800 square metres. However, fees are capped at €1,000, irrespective of the outlet's footprint.

The Department noted that inspections on MEPA, VAT and Health issues are carried out regularly by the respective authorities. Enforcement on trading licences issues is carried out by the Police Department, and officers from the Trade Licensing Unit attend cases on a weekly basis. Fines charged by the Police Department were considerably more than those the business would have to pay to CD.

During 2015, the Trade Licensing Unit processed 1,402 Notifications/Applications, of which 76.96% were issued as a result of a Notification. The law permits such businesses to start their operations up to 30 days prior to notification. Meanwhile, 23.04% of licences in 2015 were secured by an Application and out of these, 94.74% were issued within one to five working days.

Accumulation of Arrears due to Delayed Action by the Department – Temporary Pending Licences

Although the Trade Licensing Unit has initiated cancellation procedures in respect of temporary pending licences, fees still have to be charged until the respective licences are formally withdrawn or cancelled. In fact, the arrears figures would not reflect the actual arrears due if such fees are not charged annually.

i. The liquidation of this licensee occurred in 2001, at the time when responsibility still laid with the Police Department. Since the licence was not cancelled, its responsibility was devolved to CD in 2002. These fees continued to accumulate arrears because the licensee did not cancel the licence after liquidation. The amount of €41,442 refers to fees payable as at date of devolution, and therefore in respect of renewals of the licence post-liquidation. Therefore, the Department could not register its credits with the liquidator, since the company ceased its operations in 2001 and these related to renewal obligations which came afterwards.

   Prior to 2013, the Department could not cancel the licence unless it went to Court, and fees had to be charged until cancellation took place. As a result of amendments in S.L. 441.07, it became possible for CD to cancel such fees, and to consider as never due, those fees accumulated after a business ceased operations. It was as a result of this action that arrears could be decreased by €41,442.

ii. Following a letter which was sent to the licensee's relative in his capacity as Director of the company in question, Cancellation Forms were received in April 2016, together with documented evidence showing that economic activity had ceased in 2004.

Accumulating Arrears of Revenue with no Guarantee of Recoupment

Management stated that, "*SL 441.07 provides that street hawker means any individual who is licensed under the Act to sell by retail from any street or render a service as the Minister may specify. According to advice secured from DG Office this means that for a street hawker to be issued with a licence to render a service such a service must be specified by the Minister. Neither the Act or any of its subsidiary legislation contain such a provision. The renting of umbrellas/sunbeds, the shining of shoes, the selling of a tour tickets are all services and thus it is being contended that these licences should not have been issued. Hence government revenue is not being forgone*.

It should also be noted that in the case of renting of umbrellas five licences are subject to a court case and as a result of direction given by the court the department has written in respect of the five licences involved requesting the licensee to make representations with the Director Trade Services why the licence should not be considered null and void and why it should be renewed given that the Trading Licences Regulations do not permit the issuing of a street hawker licence for the service of renting out umbrellas and given that the same regulations indicate that renewal of a licence obliges compliance with the requirements of the Trading licences Act and the Trading Licences Regulations. Depending on the outcome of these five cases the department will be proceeding with the rest".

Concluding Remarks

The Department noted that over the years, various steps have been taken to address the issues of arrears, by means of changes in the law and enhanced Information Technology systems. Furthermore, during the first half of 2015, a total of 16,192 Renewal Notices were issued, requesting arrears due, as well as 5,281 reminders to all licensees who failed to settle fees due for 2015. This was followed by letters from the Attorney General's Office.

Moreover, the Ministry and CD are currently reviewing the licensing system as a whole, including the issue of arrears of revenue, taking into due consideration observations raised in this Report and suggested actions.

Ministry for Home Affairs and National Security

Armed Forces of Malta

Expenditure

Background

The Armed Forces of Malta (AFM) is Malta's military organisation tasked with primary defence functions and safeguarding national sovereignty and interest, both in peacetime and in crisis. The military instrument, in the form of the operational capabilities delivered by AFM, is a major component of the Maltese island's national defence and security architecture. The Force is organised, trained and equipped to conduct military operations at a national level, as well as to contribute towards international crises management operations. The Financial Estimates for 2015 under Recurrent Vote 23 showed a total budget of €42,315,000 for AFM, out of which the amount of €6,982,000 was planned to be used as operational and maintenance expenditure. To this effect, the actual costs incurred as per the Departmental Accounting System (DAS) amounted to €6,866,551.

Audit Scope and Methodology

The main scope of the audit was to verify that operational and maintenance expenses incurred during financial year 2015 were duly authorised and properly accounted for, as well as that such expenditure was in line with the Public Procurement Regulations (PPR) and other relevant circulars.

Other objectives were to assess the reliability and adequacy of information recorded in the Fleet Management System (FMS), that the relevant sections of the Public Service Management Code (PSMC) regulating transport were complied with, and that inventory records were properly maintained.

A sample of 62 Payment Vouchers (PVs) for a total value of €1.787 million, *i.e.* 26% of the actual operational and maintenance expenditure, was selected for testing. This was based on materiality and covered a number of expenditure items.

Key Issues

Shortcomings in Public Procurement Procedures

Audit testing revealed a number of instances wherein procurement procedures within AFM were not entirely in line with standing regulations. The main areas of non-compliance, which will be discussed separately further down in the Report under the pertinent observations, include:

a. services or items procured directly from the open market without the necessary approvals;
b. bunkering services extended perpetually;
c. expired contracts still in use;

d. commitments to purchase from the open market made prior to the request and approval for direct orders from the Ministry for Finance (MFIN);
e. prior written approvals from the respective Permanent Secretary to purchase by direct orders not evidenced, or obtained retrospectively; and
f. calls for quotations not published.

Reimbursements of Medical Receipts

In 2015, as per DAS nominal account 3150 – 'Professional Services – Medical Services', at least an amount of €42,159 was paid to various members of the Force. The amount in question may not be exhaustive as similar expenses were also recorded in other accounts. 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.

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

Control Issues

Lack of Verifications

Audit testing revealed that adequate verification was not performed before invoices were approved for payment. The following shortcomings relate:

a. An invoice for the amount of €13,000 from a foreign entity, covering one-year subscription, and another invoice of €9,695 from another overseas supplier for technical assistance and procurement of spare parts, were not certified as correct and endorsed accordingly by an officer in charge, although these were processed for payment.

b. Besides telephone calls, a monthly fee of €665 was charged by a local company for satellite phone charges. Whilst the calls were substantiated, no agreement was provided to support the monthly fee. However, the relative invoice was still certified and processed for payment.

c. The unit price quoted for a particular seal purchased from a foreign entity was $96.50 but the amount invoiced was at $156.60 per unit. Given that quantity purchased amounted to 16, this resulted in an overcharge of $961.60. The respective invoice was still endorsed and payment effected on the amount invoiced without any explanation given.

d. Notwithstanding that the casting of an invoice for spare parts of motor vessels was incorrectly calculated, resulting in AFM being undercharged by €11,322, said invoice was endorsed and processed for payment.

e. An undated pro-forma invoice for tools and spare parts from a foreign supplier, amounting to €51,084, included an erroneous charge of €469, rather than €4,609 as quoted in the relevant correspondence. The respective email was still endorsed, stating that the pro-forma invoice is to be processed for payment.

f. On 1 December 2015, the Department of Contracts approved a variation of €2,297, in addition to the originally approved amount of €61,654, for overhaul of a rescue hoist from a foreign supplier. However, the pro-forma invoice on which payment was made amounted to €64,957, resulting in a difference of €1,006, which was not duly approved.

g. As per service level agreement for the Malta coastal radio station, payments to the contractor are to be made after receipt of a proper invoice and a progress report. However, such report was not available at AFM in support of the sampled invoice which was still endorsed and processed for payment.

Water and Electricity Bills charged by Gozo Channel Co Ltd

Gozo Channel Co Ltd charges the Force for consumption of water and electricity used by AFM Gozo Command on a periodical basis, in accordance to sub-meter readings. For 2015, such payments amounted collectively to €6,476. However, no formal agreement was in place between the respective parties.

Furthermore, proper verification of the amounts charged could not be performed since copies of the bills, issued by the service provider to Gozo Channel Co Ltd, were not available at AFM.

Misleading Information resulting in Excessive Mobile Phone Bill

Before an official trip to North Africa, a member of AFM was informed by an officer at the Communications and Information System Unit that, on paying an additional nominal fee per day whilst abroad, he could benefit from the use of wireless communication. However, following attendance to a course in the respective country, it transpired that such scheme applies only to countries within the European Union (EU) and consequently the total expense for usage whilst abroad during this four-day visit accumulated to €2,190.

Commitment of Funds subsequent to receipt of Invoice

In 13 out of 62 (21%) transactions tested, amounting collectively to €220,965, it was noted that Letters of Acceptance (LAs) or Local Purchase Orders (LPOs) were dated subsequent to the relative invoices, indicating that funds were not committed in DAS prior to procurement of items and/or provision of services. This may result in not having enough money to honour the actual expense.

Shortcomings in the Fleet Management System

Whilst scrutinising the FMS report, covering 217 vehicles, as well as 144 other fuel operating machines, such as generators, grass cutters and mowers, certain shortcomings that hinder inventory control management were noted:

a. Description of vehicle did not always correspond to the respective 'Make', 'Model' and 'Bodytype'. By way of example, four vehicles were described as boat, whereas 50 other fuel operating machines, such as generators, mowers and cutters, were marked as vehicles.

b. Data entries, namely 'Engine Number', 'Chassis Number', 'Colour', 'Make', 'Model', 'First Registration', 'Capacity', 'Bodytype' and 'Year of Manufacture', were left blank for six vehicles.

c. Details in the 'Description' were at times not properly recorded, since some referred to the body style of the vehicle, such as estate, instead of recording the type of transportation, *i.e.* whether it is a vehicle, aircraft or watercraft.

d. In 334 instances out of 361 entries (93%), details of 'Section' were broadly recorded as 'All Sections', without indication of the specific location.

e. Although two vehicles were marked as active in FMS, NAO was informed that during 2015 the respective vehicles were not utilised; one was garaged and the other was recommended for casting. In fact, the relative logbooks were not available.

Insufficient Monitoring over Fuel Consumption

A review of logbooks of 20 sampled vehicles, covering different months, was performed. It transpired that for the entire year under review, the logbooks of two vehicles were never endorsed as required in terms of PSMC section 8.2.5.1. The logbooks of November and December 2015, for a vehicle which started being utilised as from November 2015, were also not endorsed at the end of the month. This does not provide the comfort that adequate monitoring was being performed on fuel consumption.

Compliance Issues

Procurement without appropriate approval

Certain purchases falling within the audit sample 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 MFIN or the Department of Contracts, as applicable. The following relate:

a. During the year under review, €704,111 was paid to a local company for the provision of aviation fuel. However, no evidence was provided to indicate that formal approval was sought from MFIN to purchase by direct order.

b. As per DAS records, total payments made in 2015 in respect of satellite phone charges amounted to €31,857, covering the period from December 2014 to October 2015. Whilst claiming that the respective company is the only supplier of such service, AFM confirmed that a direct order approval to this effect was not obtained.

c. From the sample selected it was noted that AFM placed a direct order, amounting to €31,600, with a foreign company for training courses. MFIN approval to purchase such service from the open market was not sought.

d. Since 2009[1], AFM has been paying an annual renewal licence to a foreign company, to access an international data server that gives accurate winds and currents forecasts. AFM stated that due to its operational importance, such renewal is automatically effected. Up till the end of 2015, an aggregate payment of €50,200 was made, of which €13,000 was paid during the year under review. However, no evidence was found that approval for direct order was ever obtained from MFIN.

e. As per PPR Article 20(1)(b), expenditure ranging between €2,501 and €6,000 both excluding Value Added Tax (VAT) may be procured direct from the open market following the required approval, in this case being the Brigadier (Commander). Such requirement is also emphasised in section 72 clause 33 of AFM Standing Orders. However, although lubricants were being procured by direct order, it was confirmed that approval to this effect from the Brigadier was never sought. In 2015, lubricants were bought from two suppliers, which payments amounted to €3,685 and €5,720 (both VAT excl.) respectively.

[1] The data subscription for Year 1 (2009-2010) was covered by the US Coast Guard, as part of the bilateral project between the latter and AFM. According to AFM, no subscription was required for the years 2011 to 2013 since this system was used for a lower level of accuracy for training purposes.

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.

Other Competitive Suppliers not considered

MFEI Circular No. 9/2009 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[2]. During the year under review, payments for inland liquid fuel and marine bunkering service totalled €204,930 and €778,436 respectively.

Shortcomings in the Procurement of Petrol and Diesel

a. In 2015, a local company received €48,385 for the supply of petrol and diesel to vessels based at Mġarr, Gozo. In such circumstances, as per PPR, procurement was to be made after a departmental call for tenders or after publishing a call for quotations in the Government Gazette. However, from documentation made available, it transpired that quotes were only requested by emails from a list of selected suppliers, thus undermining the transparency of the procurement process.

b. The procurement for the said supply of petrol and diesel was to commence from date of receipt of letter of award and valid for a period of six months, with the possibility of extending the service by a further three months, by giving one-week written notice. Notwithstanding that the letters of award for the supply of petrol and diesel respectively were both dated 14 April 2014, payments also covered the subsequent six-month period, *i.e.* up to end of April 2015. However, such extensions were not covered by formal notices. The amounts[3] of €12,867 and €9,336 were paid for petrol and diesel respectively under an expired agreement, *i.e.* from mid-October 2014 up to end of April 2015.

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, 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

[2] The Government-owned company that took over Enemalta's Petroleum Division.

[3] Since the agreement expired in mid-October 2014, these figures also include a *pro rata* amount of €2,673 and €879 paid for petrol and diesel during October 2014.

market was endorsed by the Permanent Secretary subsequent to the relevant approval obtained from the Direct Orders Section within MFIN.

List of Awarded Tenders and Direct Orders published late

PPR and MFEI Circular No. 11/2011 state that 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.

Inadequate Details on Payment Vouchers

In breach of Article 52(2) of the General Financial Regulations, 16 PVs in the audit sample, amounting in aggregate to €349,060, either did not indicate the quantity procured to correspond with the respective invoices, or details recorded therein were not sufficient. Thus, proper checking cannot be performed without making reference to other related documents.

No Designated Officers in charge of VAT Issues

As per MF Circular No. 5/2002 and subsequent MFEI Circular No. 2/2012, one or more officers are to be designated with the responsibility to ensure compliance with the respective directives concerning VAT receipts. However, AFM confirmed that no particular person was responsible for such duties during 2015.

Tax Invoices not available

Whilst carrying out the necessary compliance verifications in line with the Twelfth Schedule of the VAT Act, Cap 406, on the invoices falling in the audit sample amounting to €1,786,595, it was noted that in 14 cases, a proper tax invoice for the aggregate amount of €716,462 (40%) was not provided.

List of Defaulters not compiled

Notwithstanding the preceding observation, AFM confirmed that defaulters were not being reported to the VAT Department, in line with MF Circular No. 5/2002 and MFEI Circular No. 2/2012.

Inventory Returns not submitted to the Auditor General

As per MF Circular No. 14/99, 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, at least up to the date of writing this Report, *i.e.* end August 2016.

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.

Recommendations

Key Issues

Shortcomings in Public Procurement Procedures

AFM is to ensure that the method of procurement is in line with PPR and the relevant authorisations are acquired. This would ascertain transparency and fairness, as well as ensures that, as far as possible, the most competitive prices are obtained. Additionally, all service providers and/or suppliers will be given equal opportunity.

Reimbursements of Medical Receipts

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

Control Issues

Lack of Verifications

All invoices are to be invariably verified and certified as correct by the officers in charge, in order to confirm their accuracy before processed for payment. Furthermore, in order 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.

Water and Electricity Bills charged by Gozo Channel Co Ltd

A bilateral agreement is to be in place to regulate the provision of the respective service. Furthermore, the amounts charged by the service provider are to be cross-checked with the original bills issued by the latter.

Misleading Information resulting in Excessive Mobile Phone Bill

Officers in charge of administrative matters, who are communicating information to travelling officials, are to be duly aware of the applicable roaming rates for different countries, to ensure cost efficiency.

Commitment of Funds subsequent to receipt of Invoice

Efforts are to be made by AFM in order to, whenever possible, issue LAs or LPOs when the actual commitment to purchase is made, ensuring that expenditure is duly authorised and adequate funds are available.

Shortcomings in the Fleet Management System

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

Insufficient Monitoring over Fuel Consumption

The relative provisions of PSMC covering logbooks are to be complied with, in order to enhance control over vehicle usage and fuel consumption.

Compliance Issues

Procurement without appropriate approval

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.

Before effecting payments, endorsing officers are invariably expected to verify that appropriate authorisation to purchase was obtained. In addition, officers entrusted with the authorisation of payments are to be held accountable in case they fail to carry out their duties properly.

Furthermore, whilst acknowledging that immediate instructions were issued to implement the applicable procurement procedures, and that demands for fuel, oils and lubricants are now to be endorsed by the Brigadier (Commander), it is to be ensured that such procedures are duly followed.

Bunkering Services extended perpetually

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.

Other Competitive Suppliers not considered

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.

Shortcomings in the Procurement of Petrol and Diesel

Calls for quotations or tenders, for purchases above the €6,000 (VAT excl.) threshold, are to be duly published in the Government Gazette, in order to give the opportunity to all potential suppliers to submit their quote.

Furthermore, purchases of fuel are to be invariably backed up by valid contracts. Timely planning to initiate the procurement process is also of utmost importance, so as to ensure that new calls for quotations or tenders, as applicable, are published and adjudicated before the agreement in force expires.

Direct Orders

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.

List of Awarded Tenders and Direct Orders published late

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. Whilst acknowledging that the lists with the names of the contractors and the details of the related contracts were eventually published, best practice suggests that the respective amounts are also indicated.

Inadequate Details on Payment Vouchers

Complete details, including quantities of items procured and period, where applicable, are to be invariably recorded on PVs in order to enable proper verification and also to be in line with standing regulations.

No Designated Officers in charge of VAT Issues

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

Tax Invoices not available

Officers in charge at AFM are to ascertain that they are furnished with proper tax invoices meeting the criteria set out in the VAT Act. Invalid tax invoices provided by the supplier and/or service provider are not to be accepted. In cases where sellers fail to adhere to VAT regulations, Management is to consider discontinuing purchasing from such defaulters until the situation is rectified.

List of Defaulters not compiled

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

Inventory Returns not submitted to the Auditor General

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

Shortcomings in the Inventory Database

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.

Management Comments

Management submitted an extensive reply concurring with most of NAO's findings. AFM stated that it has already implemented a number of measures to ensure transparency and good governance within its internal systems and procedures. The following comments and reservations were submitted:

Reimbursements of Medical Receipts

"*It has been Management's policy that no re-imbursement for medicine costs be processed unless the applicable receipts are authorised, signed and stamped by an AFM Medical Officer*".

According to the reply, "*AFM personnel are not given the option to procure the required medicines directly from their pharmacy*" except in two specific instances. A case in point is when the "*AFM Medical Officer recommends a prescription and the medicine is not available at a Government Dispensary while the second instance is when a member requires medical assistance after working hours and his private General Practitioner prescribes medicine which is not available at Mater Dei Hospital Pharmacy. An official AFM policy has been published in this regard, in 2016, in order to address this observation highlighted by NAO*".

"*Furthermore, not all registered local pharmacies issue itemised receipts, however verification is still carried out by the AFM Medical Officer prior to the reimbursement approval against the prescription issued by the latter or private General Practitioner*".

Lack of Verifications

The points under this title that were raised by the Auditors have been noted and in future such payments will not be effected without the appropriate approvals and checks.

Water and Electricity Bills charged by Gozo Channel Co Ltd

"*It is the intention of Management to initiate discussions with Gozo Channel Co Ltd to formulate a formal agreement for the use of Mġarr Harbour, as well as the provision of water and electricity bill readings*".

Misleading Information resulting in Excessive Mobile Phone Bill

"*The Report is referring to a single case when an officer travelled to Morocco and since he was not aware of the high mobile costs tariffs, he made frequent use of his mobile phone in connection with AFM related issues. The total bill amounted to €2,289*[4]*, however following discussions with the service provider, a discount of €547 was granted, bringing the actual cost down to €1,741. Given the high cost of this bill, prior to processing of payment, AFM's Finance Branch obtained the written approval from the Permanent Secretary at the Ministry for Home Affairs and National Security*".

Commitment of Funds subsequent to receipt of Invoice

"*The attention of Unit Quarter Masters will be drawn to this issue, since they perform such allocation and commitment of funds on DAS*".

Shortcomings in the Fleet Management System

These shortcomings were rectified accordingly.

Insufficient Monitoring over Fuel Consumption

"*Comments by the Auditors are noted and rectified. Further checks and balances will become more stringent with immediate effect by the respective Unit Motor Transport Officers. It must be highlighted that AFM does not fall within the PSMC but is regulated by the Malta Armed Forces Act. Also, internal Standing Orders regulate transportation and the use of work tickets (logbooks). Although AFM does not calculate the distance covered in each journey, but work tickets in use by AFM include speedometer readings prior and after each journey. Thus, one can calculate the distance covered during each journey. At the end of each month, the Unit Motor Transport Officer calculates the total distance covered during that particular month*".

[4] This amount includes a monthly service charge of €50, excise tax of €88.05 and a credit of €39.

Procurement without appropriate approval

All recommendations have been noted and action will be taken accordingly.

Bunkering Services extended perpetually

Management confirmed that the agreement of 2011 "*had to be extended until March 2015, since all attempts to issue tenders failed to reach execution*[5]*. In March 2015, an EU project was fulfilled when a fuel farm was commissioned at the Maritime Squadron and thus no bunkering service is further required*".

Other Competitive Suppliers not considered

"*Recommendation by the Auditors to go for a framework agreement has been noted and AFM will commence the process to implement it*".

Shortcomings in the Procurement of Petrol and Diesel

"*Recommendations as indicated by the Auditors have been executed and a public call for quotations was issued and was at its adjudication stage*" when the Management Comments were submitted.

Direct Orders

Management stated that it is normal procedure within AFM that funds are committed in DAS at planning stage and before final approval is granted. AFM also stated that "*no retrospective approvals were ever sought or approved from MFIN or the Permanent Secretary. There were instances where the approval from MFIN or Permanent Secretary was received a few minutes or hours in delay from each other since these are sent by email through Permanent Secretary*", which might be "*due to the backlog in emails at the Permanent Secretary's Office*"[6]. Nevertheless, "*authorities are now being requested sequentially in order not to have this time delay*".

List of Awarded Tenders and Direct Orders published late

"*Usually such publications are conducted twice annually in June and December*".

Inadequate Details on Payment Vouchers

"*Action will be taken to insert as much information as possible on PVs*".

No Designated Officers in charge of VAT Issues

"*A Major from the Finance Management Branch has been nominated*".

Tax Invoices not available

"*Action will be taken to ensure that in future, processed invoices will include all the details required*".

[5] The documents provided to NAO only confirmed AFM's intention to issue a call for quotation following Department of Contracts' instructions on 4 September 2014. Furthermore, no reply was given to the fact that there were extensions, which were approved retrospectively.

[6] NAO does not concur with Management's reply, as five sampled cases were encountered wherein the prior written approval from the respective Permanent Secretary was not obtained. Furthermore, there were other seven instances where the approval from Permanent Secretary was obtained days later than MFIN's approval.

List of Defaulters not compiled

"*Action has already been taken during 2016, with the first return submitted on 25 January 2016, covering the period July to September 2015*".

Inventory Returns not submitted to the Auditor General

"*Inventory returns are regularly submitted by AFM to MFIN. However, note has been taken and AFM shall start copying NAO in this return*".

Shortcomings in the Inventory Database

"*Measures are being taken to rectify the issues highlighted in the observations. This database is maintained by qualified AFM personnel. Arrangements will be made with MFIN to conduct refresher training for AFM account holders*".

Correctional Services

Expenditure

Background

The Department of Correctional Services is responsible for keeping inmates in custody in a safe environment while maintaining order, control and discipline. One of its principle goals is also to help such individuals prepare for their return to the community.

Corradino Correctional Facility (CCF) is the only civil correctional facility in Malta. According to Management, the number of persons in custody during the year 2015 ranged between 533 and 587. Another two sites, namely the Valletta Lock-Up and the Forensic Unit within Mount Carmel Hospital (MCH), are also considered by law as places of custody.

The audit covered Operational and Maintenance Expenditure incurred by Correctional Services during 2015 from Recurrent Vote 45, as well as expenses paid under Programmes and Initiatives from the same Vote. The Financial Estimates show that the aggregate approved budget in this regard for the year under review was €3,056,000 and subsequently revised to €3,099,744. Actual expenditure as per the Departmental Accounting System (DAS) report amounted to €3,085,271.

Audit Scope and Methodology

The scope of the audit was to verify that during financial year 2015 expenditure incurred was duly authorised and properly accounted for, and that the adopted procedures were in adherence to the Public Procurement Regulations, as well as other relevant circulars.

Further objectives were to assess internal control measures, confirm the proper use of vehicles, establish whether the relevant sections of the Public Service Management Code (PSMC) were complied with and that inventory records were duly maintained.

A sample of 25 payment vouchers, in aggregate amounting to €97,182, was selected for testing on the basis of materiality and related risk. However, due to reasons indicated under 'Limitation on Scope of Audit', it was not possible to complete the entire audit as planned.

Limitation on Scope of Audit

Postponement of Audit Testing on a number of concerns

CCF underwent substantial changes in the management set-up when the audit was in progress, with the result that a number of audit queries could not be answered. The audit was initially suspended for a number of weeks, pending the eventual engagement of a high-ranking officer who was expected to address the relative audit issues. However, due to reasons beyond the Ministry's control, this post remained vacant by the time the audit was concluded.

In the circumstances, the National Audit Office (NAO) had no option but to conclude the audit assignment with the available information and documentation. NAO agreed to address the remaining concerns at a later stage when the proper administrative set-up would eventually be in place.

Purchase of Curtain Material and Rails

Two direct order approvals from the Ministry for Finance (MFIN) were obtained for the purchase of curtain material and rails, amounting to €107,648.

DAS reports showed that payments made to the supplier during the year under review amounted to €122,980. An undated spreadsheet traced in the file indicated that these were purchased on behalf of St. Vincent de Paul Residence and were expected to be reimbursed in full accordingly, together with other expenses which had still not been incurred and which in aggregate amounted to €62,701.

Although internal correspondence indicated that arrangements had been made for inmates to sew curtains for St. Vincent de Paul Residence, this was not formalised.

Provision of Psychiatric Services

MCH employees provided psychiatric services to CCF. It was confirmed that invoices relating to 2014 and the year under review, amounting collectively to €75,392, were still pending by the end of 2015.

NAO could neither confirm the inception date of this service nor whether formal arrangements to this effect were in place. From correspondence received, NAO is also of the understanding that there is a dispute regarding claims for payment.

Key Issues

Lack of Progress in the Internal Control System

Testing performed during the audit revealed certain weaknesses, as detailed further down in this Report under the pertinent observations, which are a case of serious concern.

This Office also noted various changes in key Management positions over a relatively short period, hampering the implementation and continuity of sound administrative procedures. Nevertheless, NAO acknowledges the difficulties encountered by Management in filling vacancies at CCF from within the public service.

Provision of Medical Services

Background

Documented evidence made available during a previous audit revealed that a private company provided medical services to CCF since the beginning of the year 2003. NAO noted various shortcomings, including the fact that the procurement procedure of such medical services could not be substantiated due to lack of audit trail. The provision of the service was extended until 31 May 2013 whilst bringing into effect substantial increases to the applicable fees. No further agreements were entered into after this date even though this service continued until October 2015.

Non-adherence to Standing Procurement Regulations

Notwithstanding that during a previous audit carried out in 2013, NAO was informed that the drafting of a call for tender for the provision of medical services was in progress, this procurement was not regularised as it was obtained direct from the open market. As indicated above, the company continued providing its service till end October 2015, after which it voluntarily terminated due to lack of progress registered with respect to a request for substantial improvement in the remuneration package. 'Vendors Turnover' report in DAS shows that payments in this regard amounted to €54,410 during the year under review.

Charge for Services rendered not corroborated

NAO previously pointed out that amounts charged on invoices for medical services for the year 2012 could not be corroborated to the respective agreement and supporting documentation, indicating lack of control over such expenditure. The same situation prevailed during the year under review. Moreover, the sampled invoice, amounting to €5,471, was not even certified correct prior to payment.

Control Issues

Appointment of Medical Doctor

Inadequate Planning leading to Procurement by Direct Order

Failure to take timely action to find an alternate service provider led Management to resort to an emergency procurement of medical services through direct order upon the termination by the previously mentioned company in October 2015. A medical doctor commenced rendering services to CCF following MFIN approval to enter into a one-year contract as from 3 November 2015, for the maximum sum of €37,100.

Unsigned Contract for Service

Although the first invoice related to services rendered by the medical doctor in question, from the period commencing 3 November 2015, the relative contract for service was only finalised in April 2016.

Payments to Sports Coordinator

Justification for Direct Order Approval not substantiated

Following approval for direct order, a sports coordinator signed a contract to provide services for a period of one year at CCF. In line with section 2 of the contract, the service was applicable with effect from 17 October 2014.

The direct order approval from Finance (Direct Orders Office) was subject to Management's statement that "*… attempts to seek other potential providers that would have been able/willing to perform the services did not yield results*". However, no evidence was provided to NAO in this regard.

Finance Authority to renew Contract not made available

The contract with the sports coordinator was subsequently renewed for another period of three years, up to 16 October 2018, under the same terms and conditions as per original contract. However, the necessary Finance approval for such renewal was not made available for audit purposes.

Shortcomings in Procurement and Relative Documentation of Closed Circuit Television Maintenance

CCF pays an annual fee of €13,194 to a service provider to cover the maintenance of the Closed Circuit Television (CCTV) System and Telephone Audio Recording System. In this regard, amongst other issues, NAO previously noted that a retrospective Finance direct order approval for the maintenance service of the CCTV was granted for the three-year period, covering 2011 to 2013.

It now transpired that the same service provider continued to provide such maintenance service for at least two more years, *i.e.*, since January 2014, in complete disregard to the prevailing procurement regulations. As a result, such procurement is considered as a direct order without the necessary approval. Additionally, a maintenance agreement was not available to cover the period starting October 2014 onwards.

Absence of a File Registry System

In 2013, NAO noted that CCF did not have a Registry System to keep record of official files and their movements. This made the tracking of files difficult. Back then, the incumbent Management had stated that plans were in hand in order to establish the first proper file registry on site; however, they were put on hold due to a lack of personnel. This shortcoming was again noted during this audit.

Additionally, as documentation made available for audit review was not filed systematically, the Auditors could not obtain reasonable assurance that the information obtained was complete.

Stock Management

a. Contrary to past practice, when CCF stock records were held concurrently both on the computerised system and bin cards, only the latter were being used during the period under review. It also transpired that bin cards, which should be kept with the respective items in the store, were being retained by the store keeper in his office.

b. Treasury Circular No. 6/2004 stipulates that the officer in charge of stock, together with a member from the Finance Section of the same entity, are to ensure that stocktaking is carried out at least once a year, preferably at the end of the financial year. NAO was provided with records of a stocktake held on 27 December 2015, however food items were not included. Unserviceable and surplus stock was also not identified. Furthermore, the annual stocktake report signed by the Head of Department was not submitted to the Auditor General, as required in terms of section 4.3 of the said circular.

Compliance Issues

Vehicles for General-use

During 2015, CCF had 17 vehicles at its disposal for general-use, which in aggregate consumed fuel costing €22,167. Audit testing revealed that control over the expenditure on fuel consumption was lacking due to the following weaknesses:

a. PSMC section 8.2.4 requires Management to see that a logbook, containing details of every journey performed, is kept for each general-use vehicle. However, no logbook was available for 11 out of the foregoing 17 vehicles. Additionally, from the six logbooks provided for audit purposes, three did not cover the entire year whilst journey records for the other three logbooks stopped in January 2016[1].

b. NAO noted persistent shortcomings in the record of journeys performed across all logbooks presented. These varied from gaps in odometer readings to missing journey details, re-fuelling records and signatures of officers making the journey.

c. No evidence was provided to confirm that logbooks were inspected periodically by a responsible officer to monitor fuel consumption, as well as to ensure that irregular use of cars is duly reported, as required by standing regulations.

Absence of Inventory Database

Notwithstanding NAO's previous recommendations, inventory records were still not compiled, thus CCF was still not in compliance with the requirements of MF Circular No. 14/99. This hinders the monitoring over Government-owned assets.

Recommendations

Key Issues

Lack of Progress in the Internal Control System

Management is encouraged to implement NAO's recommendations suggested under the respective observations for a sound audit trail, transparent procedures and a marked improvement in internal controls.

Provision of Medical Services

Non-adherence to Standing Procurement Regulations

In order to ensure effective management, timely action is to be taken to optimise value for money, whilst ensuring a fair and transparent selection process, in accordance with standing procurement regulations. Additionally, formal agreements are to be invariably in place to secure the provision of the service and minimise misunderstandings, hence avoiding potential future conflicts.

[1] Logbooks requested for inspection on 12 February 2016.

Charge for Services rendered not corroborated

The terms and conditions regulating services procured are to be formally in place. Efforts are to be made to introduce systems which will enable adequate verification of charges imposed. No payments are to be effected unless invoices are properly verified to ensure their correctness and certified accordingly.

Control Issues

Appointment of Medical Doctor

Inadequate Planning leading to Procurement by Direct Order

Contracts are to be monitored, to avoid situations of crisis management and the need to resort to direct orders, which may not be the optimal cost efficient method of procurement.

Unsigned Contract for Service

All procurement involving the provision of services by third parties is to be covered by valid agreements with the service providers. Thus, in similar future instances, action is to be taken to ensure that the necessary agreements are formalised in due time to avoid negative repercussions that could jeopardise the service.

Payments to Sports Coordinator

Justification for Direct Order Approval not substantiated

Management is to ensure that all documentation supporting procurement of both goods as well as services is adequately filed to substantiate decisions taken, thus ensuring a complete audit trail.

Finance Authority to renew Contract not made available

Relevant approvals are to be invariably obtained as required by standing regulations before entering into a contract for service.

Shortcomings in Procurement and Relative Documentation of Closed Circuit Television Maintenance

CCF is to ensure that procurement by direct order is used only as a last resort. Strict adherence to the terms and conditions under which direct order approvals are granted is recommended, in line with MFEI Circular No. 3/12 – 'Public Procurement by Direct Order'. Management is also to be reminded that Article 25 of the Fiscal Responsibility Act provides for disciplinary action against the responsible officers, when procurement is not appropriately authorised.

As already recommended, the necessary maintenance agreements are also to be in place in order to avoid undue disputes.

Absence of a File Registry System

NAO reiterates that prompt action is necessary to implement an adequate and reliable file registry system. This will improve efficiency, in both the administration and management functions, as it facilitates tracking the location of files and accessibility to records, as necessary.

Setting up this system will also be of crucial importance for monitoring the duration, terms and conditions of agreements drawn up with suppliers and service providers, thus addressing a number of shortcomings which are being brought to the attention of Management through this Report. In this respect, files can be marked to be brought up for the necessary action on specific dates.

Stock Management

In order to strengthen the stock control function, besides maintaining bin cards, Management is to actively consider the reintroduction of a computerised system for stock recording purposes. Subsequent to its implementation, it is to be ensured that both records, *i.e.* the bin cards and computer system, are invariably updated simultaneously in a timely manner.

Adherence to Treasury Circular No. 6/2004 is paramount for the maintenance of proper stock records. Additionally, a report showing the balances of each stock quantity and value, as well as the unserviceable and surplus stock, is expected to be forwarded to the relevant authorities, namely Permanent Secretary, MFIN, Director of Internal Audit and the Auditor General, as stipulated therein.

Compliance Issues

Vehicles for General-use

Proper logbooks are to be kept for general-use vehicles, indicating each journey performed, the purpose of trips made and exact mileage covered, in order to enable adequate verification.

The attention of Management has also been drawn to the relative guidelines outlined in standing regulations, covering the use of such vehicles. Records maintained for every vehicle, will ensure that adequate details of each journey performed are recorded. The same guidelines also require that a certificate is entered on every logbook at the end of each month, confirming that the trips recorded therein were made on official duty.

Absence of Inventory Database

An inventory database is to be compiled without further delay, in accordance with MF Circular No. 14/99, in order to reflect precise and reliable data of assets at the disposal of CCF. Awareness of all the requirements outlined in this circular, including the statutory submissions to the Auditor General, is also to be ensured.

Management Comments

CCF, which is now under new Management, concurred with the majority of the highlighted observations, as well as with the proposed recommendations. The following comments and reservations were submitted:

Purchase of Curtain Material and Rails

Invoice that amounts to €62,701 has been settled. All the material that was paid by CCF has been reimbursed and no expenditure is incurred by Public Funds. Covering approval for the remaining amount will be sought from the Direct Orders section MFIN.

Provision of Psychiatric Services

Discussions with MCH are ongoing. CCF reiterates that this service should be free of charge since by law inmates are entitled to the same services available to all citizens free of charge.

Lack of Progress in the Internal Control System

Vacant posts are being filled in line with public service recruitment procedures to ensure adequate line of command resulting in best control practices particularly in the line of procurement procedures.

Provision of Medical Services

Non-adherence to Standing Procurement Regulations

This contract has been terminated. CCF finds great difficulty to find suppliers for medical services. Note has been taken of NAO recommendations.

Charge for Services rendered not corroborated

The contract under review has been terminated and new contract was signed. CCF is presently in the process of analysing the best way forward and type of medical services required to cater for all the medical needs of CCF. Procurement of such service will take place following public calls for the provision of such service and/or possibly recruitment of professionals required in the compliance with Public Service requirements and procedures.

All invoices in respect of 2015 are certified and countersigned. In particular the invoice for the month of October 2015 amounting to €5,471, was reviewed downwards by the authorising officer from the original invoiced amount of €7,762.

An exercise is being carried out as regards to the 2012 payments that could not be corroborated, to ensure that no incorrect payments had been issued.

Appointment of Medical Doctor

Inadequate Planning leading to Procurement by Direct Order

As previously pointed out CCF finds great difficulty in identifying such services and finding providers. Note has been taken of the recommendations and as already explained CCF is in the process of issuing calls/tenders for the provision of the relative medical services.

Unsigned Contract for Service

Although the contract was formally signed in April 2016, agreement in principal was reached in October 2015. Due to the urgency of the situation he was engaged as soon as approval was granted. The terms and conditions of the service rendered were clear to both parties and were being adhered to accordingly.

Payments to Sports Coordinator

Justification for Direct Order Approval not substantiated

The Management has taken note of NAO's recommendation.

Finance Authority to renew Contract not made available

The direct order approval from Finance (Direct Orders Office) for this service may be found in the file and was forwarded for auditing purposes.[2]

Shortcomings in Procurement and Relative Documentation of Closed Circuit Television Maintenance

The CCTV system can be considered obsolete and in many cases it is almost impossible to find spare parts required for maintenance. The present service maintenance provider has been giving this service for a very long time. The idea of having different service providers given access to such security matter is not considered feasible, hence the resort to the same service provider. Nevertheless, CCF is in the process of installing a new CCTV system and in fact preliminary work concerning the cabling throughout the whole premises is in process.

Following this, CCF will proceed to purchase a new system which will be covered by relative maintenance contract in respect of Government procurement procedures and in consideration of the security issues involved. CCF Management takes note of the recommendations made by NAO in this respect.

Covering approval will be sought to cover the period January 2014 to date and also request a direct order approval for the next 12 months or until the new contract is awarded supported by a maintenance agreement.

Absence of a File Registry System

CCF already appointed two officers in charge Main Registry. DocReg has already been installed on their computer. An electronic filing system has been planned and is being implemented. All CCF files are being inserted in the system.

Stock Management

CCF has already installed StoreIT on the Main Stores computers as a pilot project to tackle teething problems. The system will be extended to all secondary stores gradually. In this respect StoreIT is being considered as a short term solution and CCF plans to procure a modern suitable Stock Management System through the Office of the Chief Information Officer. It is planned that in the near future a tender for the supply and maintenance of the said system will also be issued and consequently all stock records will also be kept electronically. Following this, stocktaking procedures will be carried out frequently in accordance to the established regulations and procedures. CCF is planning to recruit administrative staff to conduct these procedures.

Vehicles for General-use

The recommendations of NAO are being implemented. Log books are in place for each and every vehicle. Instructions have been issued to all users that proper records are to be kept of each journey. Verbal instructions have long been issued to all users and will be followed by written instructions.

Absence of Inventory Database

CCF has already appointed an officer to carry out the functions of inventory officer. Preparation work is already being carried out in order that a full inventory is compiled and electronically stored according to the pertinent regulations.

[2] Notwithstanding this claim, only the direct order approval dated October 2014 and covering a one-year period, was made available for audit purposes.

Ministry for Finance

VAT Department

Expenditure and Personal Emoluments

Background

The Value Added Tax (VAT) Department, falling within the remit of the Ministry for Finance (MFIN), is entrusted with the role of collection and management of VAT in line with Cap. 406, VAT Act and other pertinent Legal Notices.

The Department was allocated a recurrent expenditure 2015 budget of €6,574,000, consisting of Personal Emoluments of €3,491,000, Programmes and Initiatives of €2,138,000 and Operational and Maintenance Expenses of €945,000. The actual incurred expenditure during the year was €5,994,594, being €3,156,894 for Personal Emoluments, €1,812,678 for Programmes and Initiatives and €1,025,022 for Operational and Maintenance Expenses.

Audit Scope and Methodology

Expenditure

The main objective of the audit was to ascertain that adequate internal controls, over the procurement and payment of selected line items, were in place during the financial year under review. This exercise also aimed to ascertain the efficient administration of public funds in line with existing regulations, policies and procedures. Targeted accounts included Utilities, Printing, Office Services, Transport, Contractual Services, Professional Fees and Training. A sample of 32 transactions falling under Operational and Maintenance Expenditure, with an aggregate value of €146,083, was selected, based on nature and materiality of expenditure.

Vehicles

Testing was carried out on the maintenance of logbooks of the three general-use vehicles. Three months for each vehicle were randomly selected for examination to verify compliance with relative sections of the Public Service Management Code (PSMC). Additionally, fuel consumption of a selected fully-expensed car pertaining to a senior officer, was verified to ensure that monthly fuel consumption limit, as set by MFC Circular No. 5/98 – 'Purchase and Use of Official Cars', was adhered to.

Inventory

The latest inventory database and related rooms lists were requested from the VAT Department in order to assess conformity with MF Circular No. 14/99 – 'Government Accrual Accounting: Revised Inventory Control

Regulations'. Subsequently, the National Audit Office (NAO) planned to perform a physical inspection of a number of listed inventory items. However, this inspection was not possible, as explained further on in this Report.

Travel

Five visits abroad on official business were selected in order to ascertain that travel arrangements, flights, accommodation and contingency money, were compliant with PSMC requirements. Rates established by MFIN in relation to subsistence allowance entitlement were also referred to. Particular consideration was given to the materiality of amounts when selecting the audit sample. The sample represented 15% of the Department's travel costs.

Personal Emoluments

The audit also sought to ensure that personal emoluments for 2015 were appropriately recorded and processed according to PSMC and other pertinent circulars in force at the time of the audit. The adequacy of internal controls, intended to ensure accuracy and validity of salary payments, was also determined.

Emoluments in favour of 15 employees were selected for testing. Factors considered for sample selection included, employee grades, employees on a reduced work schedule and/or telework arrangements as well as officers transferred to the Department. NAO is to remark that, after considering the materiality of the respective allowances and overtime expenses paid during the year under review, the selection comprised 10 officers, who were also assigned duties as VAT Inspectors.

The sufficiency of internal controls was tested, to ensure accuracy and validity of salary payments, including officers' entitlement to allowances and overtime paid. Time records from the Attendance Verification System (AVS) were verified against the Vacation Leave (VL) and Sick Leave (SL) documentation, provided by the Department, as extracted from a module within the payroll system. Recorded VL was also confirmed against the 'Vacation Leave Application Form and Record' (GP44). Apart from ensuring the reliability and correctness of these records, testing ascertained that overtime payments and VL utilisation were properly authorised, whilst SL was substantiated with medical certificates.

Good Practice

This Office satisfactorily noted that where applicable, all fiscal receipts in relation to the sample selected were available at the Department. Moreover, with the exception of one issue, accounting for travel abroad was in conformity with relevant regulations.

Key Issue – Personal Emoluments

Weak Internal Controls in the Human Resources Function

Various issues that were identified while conducting audit testing on salaries, depict a scenario of lack of internal controls, predominantly within the Human Resources (HR) and Payroll function. Instances were noted where overtime payments and allowances granted to employees were either unauthorised, inadequately supported by evidence, or incorrect.

Below is a list of internal control weaknesses identified during the audit, which will be elaborated further under the pertinent observation:

a. Lack of verification of time records against VL and SL documentation.
b. VL not supported by proper authorisation.

c. SL not substantiated by medical certificate.
d. Lack of attendance records verification.
e. Temporary Absence Record Sheet not prepared.
f. Overtime payments not properly authorised.
g. Paid overtime exceeding authorised overtime hours.
h. Inaccurate overtime and allowances payments.
i. Employees' personal files not properly kept and safeguarded against unauthorised access.
j. Teleworking regulations not followed.

Control Issues – Personal Emoluments

Discrepancies between Vacation Leave Documentation and Time Records

The Department maintains employees' VL records both on the payroll system, and 'Vacation Leave Application Form and Record'. In addition, time records (*i.e.* AVS), indicate VL hours availed of by each employee.

While verifying VL documentation against leave hours listed in AVS, 12 out of 15 employees portrayed inconsistencies between the three systems. In a number of instances, although both GP44 form and the payroll system records indicated the respective employees were on VL, no record of such leave was traced in AVS. On the other hand, a number of VL hours were identified in AVS, but omitted in VL documentation. Hence, this prevailing situation reveals that VL balances on the GP44 form are not reliable.

Lack of Authorisation of Vacation Leave

Testing revealed that two different procedures for recording requests for VL were in place at the Department during the year under review. In the initial months of 2015, the Department used a system of VL templates, which were completed manually by each officer requesting leave. The authorising officer would proceed to approve such VL by manually completing the second part of the form. After recording such VL, HR Section used to return such form[1] to the officer requesting leave. On the other hand, during the last few months of 2015, a similar template was used, but this time included as an attachment in an electronic mail sent to the authorising officer, who in turn forwarded such mail to HR Section in the form of approval.

a. Written approval for Vacation Leave not traced

It transpired that 120 and 21 hours of VL pertaining to two officers respectively, were not supported by authorised application forms.

b. Authorisations of Vacation Leave not dated

Date of approval of an aggregate of 518 hours of VL pertaining to seven employees was lacking.

Sick Leave not supported by Medical Certificates

Employees are to provide medical certificates as from the first day of SL, as per PSMC Section 4.3.1.4. However, an analysis of all sickness absences taken during the year by the 15 sampled officers, revealed 19 instances, related to seven employees, which were not covered by the necessary medical certificates. In relation to two out of these seven officers, VAT officials confirmed that following remarks received from this Office, action will be taken by the Department by deducting the respective amount of days from their actual leave balance in the current year.

[1] Upon changeover of procedure, HR Section did not request officers to return the VL templates applicable in the previous departmental practice.

Discrepancies between Sick Leave Documentation and Time Records

While verifying sickness absences recorded in the payroll system against SL hours listed in AVS, it transpired that 14 instances, relating to six employees, portray inconsistencies between the two systems.

In the majority of noted cases, except for four, AVS indicated that employees had sickness absences, which were omitted from SL records within the payroll system. On the other hand, in another two cases related to one officer, it transpired that such employee reported for duties to VAT offices on both dates, even though he was listed as sick on same days in the payroll system. Moreover, it was noticed that another officer was on SL on a particular date as recorded on the payroll system, however the respective time records specified that such employee was on VL instead. Finally, a SL day availed of by another officer was listed in the payroll system, but not in AVS.

Weaknesses in Recording of Attendance

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

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

NAO noted that one officer failed to clock out on the majority of days throughout the year under review. VAT officials confirmed that this can be attributed to lack of communication between two different Sections within the Department. Management explained that this issue was discussed during an internal meeting and such employee was to be subsequently admonished in terms of the PSMC.

Similarly, testing revealed that another nine officers, seven of whom performing VAT inspections, had regular occurrences in which they failed to clock out at the end of their working day. In the case of two of these officers[2], justification for not clocking out was provided to this Office, but not corroborated by any supporting documentation. With regards to the other seven officers, HR Section was not in a position to provide details.

A senior officer verbally explained that the cases being questioned may be related to duties carried out by Inspectors outside VAT premises during office hours. Consequently, NAO deemed it necessary to perform sample testing in the Inspectorate's Risk Analysis Application (RAA), in order to check whether inspections or related work were actually carried out by the respective Inspectors on the relevant dates. However, in 14 instances relating to three VAT Inspectors out of a total of 17 instances tested, this Office did not trace any evidence relating to work carried out, since nothing was documented in RAA.

In view of lack of communication between Inspectorate and HR Sections with respect to duties carried out by Inspectors outside VAT premises during normal office hours, NAO was informed that "... *a meeting was held with Director ... so as to start forwarding the list of inspectors on official duties to the HR Office ...*".

b. Telework hours not recorded on Time Records

Following testing of time records of four officers in the sample benefiting from telework facilities, it transpired that a number of working hours[3] performed from home by two of these employees, were not being recorded in their respective time records.

---

[2] One of these two officers, himself provided the relative explanations *via* email dated 16 June 2016.

[3] Hours of work performed from home by one officer (eight hours *per* week) and two hours *per* day from Monday to Thursday by another officer.

c. Sick and Vacation Leave hours recorded in Time Records not in line with Telework Arrangement

Audit testing of time records of an officer revealed various instances where SL and VL were being listed as being 8.75 and 6 hours in winter and summer periods respectively. However, the respective telework agreement specified that such officer was required to work a total of 8.25 hours from Monday to Thursday (two hours of which worked from home) and seven hours on Friday (from home), throughout the whole year. Consequently, a number of days of SL and VL were incorrectly recorded in AVS, resulting into a number of inconsistencies against data included in the payroll system. Upon enquiry by this Office, VAT officials confirmed that these anomalies have now been addressed and adjusted by HR Section.

Temporary Absences Records not maintained

As mandated in PSMC Chapter 3.1.2.3, temporary absences on official duties are to be recorded in a Temporary Absences Record Sheet (GP42). Nevertheless, VAT officials informed us that the Department does not prepare the form. Currently, the Department's time records indicate the hours of absence listed as 'FW'[4], without specifying the nature of such absence.

When requested to explain sampled employees' temporary absences, VAT Department was not always in a position to provide justification for such absences. Moreover, since this Office was informed that temporary absences also include inspections and related work carried out by Inspectors, sample testing in RAA was effected in order to verify whether absences were related to duties carried out by the respective Inspectors. However, in three instances, all relating to one officer, this Office did not trace any evidence in the Inspectorate's Application.

Following audit enquiry, Management explained that HR Section was instructed to prepare a Daily Record Sheet informing the pertinent Director of all staff movements, namely VL, SL, Court sittings, training courses, meetings, duties abroad and telework arrangements.

Inadequate Control and Various Weaknesses on Overtime performed

During the year under review, nine employees out of the sample of 15, performed overtime duties. Testing on the spreadsheets compiled to facilitate overtime payments calculation revealed a number of weaknesses and discrepancies related to the upkeep of overtime-related documentation. In fact, overtime records, which are constantly amended to log actual hours worked, do not portray sufficient evidence of an officer's overtime hours. To this effect, HR Section confirmed that the current system is "... *time consuming and subject to human errors*."

It is pertinent to remark that:

a. Overtime not authorised by Permanent Secretary

Management wrongly presumed that since the Department is allocated a budgeted amount for overtime in the annual Financial Estimates, such provision of funds would suffice as prior authorisation for overtime.

[4] 'FW' stands for Fieldwork.

b. Managerial Approvals for Overtime not traced

- Overtime worked by Inspectors not formally approved

Following this Office's request for the approvals of overtime carried out internally by Inspectors, it transpired that all overtime hours conducted during the year under review were only approved verbally. Moreover, VAT officials confirmed that such practice was rectified as from January 2016. On the other hand, outside inspections performed by Inspectors are recorded on the 'Outside Inspections 2015' file. During the course of the audit, it emerged that inspections were undated and not pre-approved, but only certified by an Assistant Director on a weekly basis.

- Approved Overtime hours exceeded

The actual overtime hours payments to one officer consistently exceeded his authorised overtime allocation. Upon enquiry, the Department informed this Office that the respective approvals for additional overtime hours were to be provided for audit purposes. Nevertheless, up to the writing of this Report, no reply was forthcoming. Moreover, Management confirmed that HR Officer was instructed not to process unauthorised overtime payments.

- Request for approvals for overtime not dated

Testing carried out also revealed several instances in which the overtime request approvals of two officers lacked endorsement date. Aggregate hours exceeded 300 hours.

c. Inaccurate Overtime payments

- Overpayments of Overtime

The spreadsheet recording overtime attendance hours in respect of one officer indicated that for the period between 2 to 31 December 2014, she had 14 hours of approved overtime. However, testing of time records of such employee revealed that the actual amount of overtime hours worked within VAT premises totalled 1.17 hours, thus resulting in an overpayment. Following this Office's remarks, the Department confirmed that the above-mentioned overpayment was to be deducted from the respective officer's remuneration during 2016.

Audit testing also revealed that 18 hours of overtime paid to two other officers, lacked managerial certification. The Department confirmed that as regards to the two overtime hours paid to one of these officers, no record of outside work was found and thus, it was erroneously paid.

- Rest Breaks not deducted from Overtime paid

Article 5 of Subsidiary Legislation 452.87 – 'Organisation of Working Time Regulations', states that every worker should be entitled to a break for at least an uninterrupted period of 15 minutes, in those cases where the working day is longer than six hours. However, testing revealed instances where no breaks were deducted in the calculation of overtime hours of one officer throughout the last three pay periods of 2015. In total, 31 instances were noted reflecting compensation for work performed during the break period.

- Inaccurate Overtime Rate

  Testing revealed that five hours overtime worked by an officer on a Sunday were paid at the normal overtime rate (*i.e.* at 1.5 actual time rate for every hour of work) instead of at a minimum of a day's pay, as *per* Section 3.2.6.1 of PSMC. This resulted in an underpayment made to the same officer, which fact was confirmed by the individual in charge of salaries.

Anomalies in Signature of Authorising Officer

Whilst testing VL approvals of an employee, NAO noticed that the first batch of VL approvals received on 28 April 2016 was signed by the respective senior officer. Following a further request in respect of missing approvals, a second batch of VL forms was forwarded to this Office on 14 June 2016, the authorising signature on which was different from that on the first batch provided.

Upon clarification, the senior officer in charge confirmed that the signatures on both batches were his. However, this Office has serious reservations regarding the veracity of these signatures.

Personal Files not properly maintained

Following this Office's review of employees' personal files, in a number of instances it transpired that significant documentation was not filed. In one example, although the minute sheet within an employee's personal file made reference to the officer's telework agreement, this document could not be traced in same file.

Employees' Personal Files not safeguarded against Unauthorised Access

During testing, this Office observed that the employees' personal files were located in HR office, which was being shared with other officers from different sections. It was noticed that any officer could easily obtain unauthorised access to the personal files of all employees within the VAT Department. Upon enquiry, VAT officials verbally confirmed that personal files were not maintained under a 'lock and key' system, but that remedial action will be taken to address such shortcoming.

A typical example of possible unauthorised change of information in a personal file, emerged after reviewing the personal file of one of the sampled officers. In fact, audit testing of this file revealed that on 6 December 2011, an application for telework was rejected on the basis that "*The sensitivity of the work of* ..." this officer "... *precludes telework to be performed*", which declaration was signed by a Director and the then Commissioner of VAT. However, on the following day, the HR Section sent a letter to the respective employee, in which the latter was advised that the "... *request for telework at the VAT Department had ___ been approved*." However, this Office noted that the word 'not' between "... *had* ..." and "... *been approved*." was concealed, thereby overturning the original managerial decision.

No Evidence supporting Inspector Allowance paid

An officer was paid an allowance of €1,978 on the basis of HR/MFIN Circular No. 7/2014, in respect of duties as inspector for the period from 1 April to 31 December 2015. However, this officer was not assigned any duties of VAT Inspector during year 2015, as confirmed through analysis of RAA.

Inaccurate Calculation of Allowance

HR/MFIN Circular No. 7/2014 also states that during such time that an employee was assigned the duties of VAT Inspector, besides the allowance of €3,000 *per annum*, those selected officers whose substantive salary is on Salary Scale 12 or below, or on Scale 11 but not on the maximum point of the said scale, were to benefit from an additional non-pensionable allowance equivalent to the difference between their substantive salary and maximum of Scale 11.

The Inspector allowance paid to one officer in the first two pay periods of year 2015, *pro rata* amounting to €300 each, correctly included the additional allowance. However, the remaining 11 payments amounting to €144 each excluded such additional allowance, resulting into an aggregate under-payment of around €1,719. This was confirmed through correspondence with HR Section, in which they explained that from the third payment of 2015 onwards this additional allowance was somehow deleted, which error went by unnoticed up till the second payment of 2016. It was later stated that the respective employee was paid the difference in the fifth payment of 2016. However, despite various requests, up to the date of writing of this Report, no evidence was provided to this Office in this respect.

Telework Practices not according to Standing Policies

Section 5.4.2.3 of PSMC requires an 'Application for Telework' to be filled in annually. When the application is duly endorsed, the decision is communicated to the applicant and all parties concerned. Following this, a 'Telework Agreement', valid for a period of one year, must be signed by both the Permanent Secretary and employee, outlining the work conditions. Moreover, employees who wish to renew their telework agreement for a further period of 12 months, have to complete the 'Renewal of Telework Agreement' form, which is to be authorised by the Permanent Secretary, through the respective Ministry's HR Office. 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 form used even though such arrangement was previously terminated.
c. Clauses of Telework Agreement not adhered to.
d. No evidence that telework is appropriately monitored.

Control Issues – Expenditure

Non-compliance with Public Procurement Regulations

Provision of legal services from three different lawyers, were procured directly from the open market, without a public call for applications being issued or relevant approval from MFIN sought. Entries in 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, representing 49%, 12% and 6% of the allocated funds in the respective account. Upon enquiry, VAT officials confirmed that for legal action against defaulters, the Department would refer cases to a pool of lawyers who are experts in tax legal matters, and that these three lawyers, amongst others, were utilised by the respective Section "*... according to their ability*." The Department also stated that "*These are particular cases as these do not relate to 'normal' procurement of services – legal fees are often recouped from taxpayers and therefore are not paid from public funds* ...". However, the Department did not substantiate this statement.

Moreover, Contract Agreements for the services in question were not drawn up to bind both parties with respect to the hourly fees of services to be delivered by these lawyers, as well as set a maximum amount payable to the same providers. NAO could not determine the date when these legal advisors commenced providing their services with the VAT Department.

Additionally, even though the respective Section certified the bills as fair and reasonable and referred them for payment, this Office did not trace any documentation supporting the invoices selected, with an aggregate value of €7,171.

Shortcomings in relation to General-use Vehicles

Audit testing revealed lack of control over general-use vehicles. Whilst reviewing whether the logbooks pertaining to the existing three general-use cars were adequately kept, in accordance with PSMC requirements, the following shortcomings[5] were noted:

a. In the majority of instances reviewed, the mileage was only recorded at the start of each day.
b. Regular instances were noted where the journey purpose was either omitted or incomplete, hindering NAO's testing as regards to the exact purpose of the journey[6].
c. Lack of monthly Logbook Certification[7].
d. All three general-use vehicles did not bear GVN number plates, thus going against MFIN Circular No. 5/2015 – 'Government Transport and Civilian Plates'.

Refunds Due in respect of Visit abroad following Audit Query

Testing of a visit abroad by two officers revealed that a refund of €540 was due by each employee to the Department in respect of that part of the advance relating to accommodation and meals, which were actually provided by the organisers. Upon enquiry by this Office, *via* email dated 17 May 2016, evidence was provided confirming that refunds were eventually refunded by the same officers, on 19 and 23 May 2016 respectively.

Compliance Issue – Expenditure

Ongoing update on Inventory List

The Inventory Database forwarded to this Office for audit purposes was dated end June 2012, thus indicating that such register has not been updated since. In fact, VAT officials confirmed that this was the last Inventory Database compiled by the Department. Moreover, related Room Inventory Lists were not forwarded to this Office.

Upon enquiry, VAT officials confirmed that in February 2016, *i.e.* prior to the commencement of this audit, "... *permission to start a fresh inventory template has been granted by the Treasury Department*.", on the basis that the VAT Department was experiencing difficulties in compiling and maintaining the Inventory Database, so it was decided to start the exercise from scratch. In fact, during this audit, it was noticed that VAT officers had already commenced a thorough exercise in order to compile the Inventory Database.

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

Recommendations

Key Issue – Personal Emoluments

Weak Internal Controls in the Human Resources Function

The VAT Department should immediately strive to establish effective measures to implement robust internal controls and reduce unnecessary costs within the HR and Payroll function.

---

[5] Albeit the majority of officers making the journeys were signing the respective logbooks in accordance with PSMC regulations, a few trips recorded in the logbooks of two vehicles lacked such signature.
[6] Upon enquiry, VAT officials explained in detail all queried journeys and informed responsible officers to start including adequate journey details.
[7] Upon enquiry, VAT officials confirmed that the officer in charge of transport has been instructed to start implementing this procedure.

Control Issues – Personal Emoluments

Discrepancies between Vacation Leave Documentation and Time Records

Management is to ensure that the record keeping of VL is reliable, as well as complete, by carrying out regular reconciliations of all documentation and systems in use.

Lack of Authorisation of Vacation Leave

In order to maintain an adequate control environment, it is recommended that all VL hours shall be 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.

Sick Leave not supported by Medical Certificates

The Department is to ensure compliance with PSMC requirements and initiate disciplinary proceedings against officers who fail to abide by these procedures.

Discrepancies between Sick Leave Documentation and Time Records

Documentation related to sickness absences is to be checked regularly against time records. Furthermore, similar to what was recommended in respect of record keeping of VL, the Department may consider integrating the SL function within the payroll system with AVS, in order to ensure the accuracy and completeness of records.

Weaknesses in Recording of Attendance

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 to be 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 premises in case of any emergency, such as an office fire.

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

Temporary Absences Records not maintained

Management is to ensure that all absences are 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 all unauthorised absences.

Inadequate Control and Various Weaknesses on Overtime performed

The maintenance of proper, correct and reliable records is a fundamental element of a sound system of internal control over personal emoluments, including overtime. VAT Department may consider reviewing the record-keeping process, to ensure enhancement of the present manual system in respect of overtime authorisations 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 PSMC requirements. Management must adequately approve all overtime in advance in order to maximise the value added to the Department.

Prior to settlement of overtime payments, verification is to be made by the HR Section as to whether overtime hours claimed have been actually carried out, as well as existing approvals not exceeded.

Anomalies in Signature of Authorising Officer

Management is to ensure that officers entrusted with the upkeep of records are aware of their responsibilities and that any type of information forwarded to third parties should be trustworthy.

Personal Files not properly maintained

It is recommended that the HR Section maintains records of all payroll related documentation, to ensure a sound system of internal control, as well as a reliable audit trail. Officers' personal files are to be updated with all relevant documents, including telework arrangements.

Employees' Personal Files not safeguarded against Unauthorised Access

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

No Evidence supporting Inspector Allowance paid

The Department is to ensure that it makes the best possible utilisation of its available staff and that the payment of any allowances is justified, ensuring best value for money.

Inaccurate Calculation of Allowance

In order to establish an efficient system, a review of the payroll processing procedures is to be carried out. Furthermore, to achieve a reasonable level of accuracy, independent checking is recommended.

Telework Practices not according to Standing Policies

Irregularities noted are to be rectified without delay and the employees' personal files are to be updated with all relevant documentation. Moreover, telework arrangements are expected to be revisited on an ongoing basis. Hours worked from home, as well as relative output, are to be monitored closely and continuously 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 duly authorised and recorded in the respective officer's personal file.

Control Issues – Expenditure

Non-compliance with Public Procurement Regulations

Local procurement regulations, where applicable, 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, and where applicable, a call for tender or applications for such mentioned services is to be considered.

In order to ensure accountability, the Department is to obtain the necessary approval from MFIN prior to procuring directly from the open market, which measure is to be resorted to only in exceptional cases.

Moreover, the Department is to ensure that procurement of services is at all times supported with a valid Contract Agreement.

Shortcomings in relation to General-use Vehicles

Reference is to be made to the guidelines, stated in Section 8 of the PSMC prevailing at the time of the audit, which stipulate that a proper logbook should be kept for each departmental vehicle to record the exact mileage covered and other journey details, and shall be signed by the respective officer. Moreover, each logbook is to be certified by the officer in charge of transport at the end of each month, in order to ensure that the trips recorded in the logbook were made on official duty and fuel consumption is reasonable.

The Department is recommended to ensure that all its general-use vehicles are issued with 'GVN' number plates.

Refunds Due in respect of Visit abroad following Audit Query

Officers entrusted with the governance of official visits, are expected to conform with the pertinent regulations, in order to ascertain full accountability of the expenditure incurred. Thus, all travel advances are to be reconciled, and any refunds due are to be collected within one month from return as stipulated in Section 8.10.1.1 of PSMC.

In addition, the Department is to carry out a thorough exercise to identify any other possible applicable reimbursements due to the Department relating to pending visits abroad, and any unpaid refunds due are to be recouped without undue delay.

Compliance Issue – Expenditure

Ongoing update on Inventory List

The ongoing exercise of updating the Inventory List has to be given the utmost priority in view of Government's move towards accrual accounting in the near future. 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.

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

Management Comments

Management explained that the VAT Department "*… has been in the process of a merger with Customs and IRD since 2014. As a result the Department's structure is currently somehow ambiguous since top managerial positions including the Director General (VAT) and Director Support Services (VAT) have been suppressed and are in the process of being restructured within the context of the merger*.

Although in the year of assessment (2015) the VAT Department identified lack of staff, especially to replace in-house recruited VAT Inspectors who used to carry out administrative (including HR and Salaries) work, HR plans were limited to reflect the budgetary allocations for the year."

It was also stated that "*The lack of middle management has been a concern to the top management at the VAT Department. The VAT Department had in the past requested through HR /Business Plans the services of*

an HR manager to carry out such controls; however, such request was never entertained. Therefore, such verifications did not take place. Also, the Department has requested the services of Accounting support officers to replace 'unskilled' personnel who are amongst others currently administering the Salaries.

In the interim, the Department issued respective guidelines to the officers concerned so as to report any irregularities to top management."

In view of concerns raised by this Office, Management reiterated that it "... *took note of the observations and recommendations put forward by NAO and is looking forward to embark on a strategic management plan in the context of the merger to ensure that any discrepancies and shortcomings are rectified*."

The VAT Department also remarked the following:

a. "*... the Department took on board the recommendations and for the time being the HR Section has been restructured. Also, action has been taken to adjust any discrepancies*. ..."

b. "*An officer has been appointed to ensure that the maintenance and updating of Personal files is carried out whenever required. Also, with regards to the payroll audit trail, a manager who is currently deployed on procurement and tendering process has been appointed to monitor and ensure a sound system of internal control*."

c. "*Although personal files are currently kept under lock and key, filing cabinets are being procured so that files are kept at managerial level by the end of next month*."[8]

d. "*The way forward for the provision of legal services is being explored to suit the Department's needs in terms of knowledge of taxation, capability and efficiency amongst others, in line with the Procurement Regulations*."

e. "*… With regards to GVN plates authorisation to register the vehicles under civilian number plates had been granted by the Director General Support Services MFIN. The rationale was that the "vehicle may be used amongst other purposes for covert VAT Inspection visits*." However, NAO opines otherwise considering that Inspectors are in receipt of an allowance specifically catering for VAT Inspection visits with their own means of transport.

[8] *i.e.* by the end of November 2016.

Department of Contracts

Expenditure and Personal Emoluments

Background

The Director of Contracts is responsible for the administration of the procurement procedures as laid down in S.L. 174.04 – 'Public Procurement Regulations', with the Department of Contracts (DC) as the 'central purchasing body'. According to its Mission Statement, DC binds itself to deliver an efficient and effective service to both economic operators and contracting authorities alike, by ensuring that all economic operators are treated equally and transparently.

During 2015, DC was allocated a recurrent expenditure budget of €1,518,000, consisting of Personal Emoluments of €1,226,000, Operational and Maintenance Expenses of €212,000, and Programmes and Initiatives of €80,000. The actual recurrent expenditure incurred during the year was €1,504,054.

Audit Scope and Methodology

Expenditure

The main objective of the audit was to ascertain that adequate levels of internal controls, over the procurement and payment of selected line items, were in place during the financial year under review. This exercise also aimed to ascertain the efficient administration of public funds in line with existing regulations, policies and procedures. Targeted accounts consisted mainly of Utilities, Rent, Transport, Professional and Contractual Services, Training, as well as Improvements to Property. A sample of 33 transactions, with a value of €32,797, was selected on the basis of materiality and frequency of expenditure.

Testing was carried out on the fuel consumption of two fully-expensed vehicles assigned to senior officers, as well as on the maintenance of logbooks of the two general-use vehicles. Each of the latter was examined to verify compliance with relative sections of the Public Service Management Code (PSMC). In the case of the fully-expensed cars, relevant extracts from the Fleet Management System were obtained to ensure that the monthly fuel consumption limit, as set by MFC Circular No. 5/98 – 'Purchase and Use of Official Cars' was adhered to.

Audit testing was also carried out on three official visits. The respective travel arrangements, flights, hotel accommodation, other expenses and advances, including subsistence allowances and contingencies, were verified as *per* PSMC requirements.

Furthermore, the electronic Inventory Database and Room Lists forwarded for verification were checked to ensure their conformity with MF Circular No. 14/99 – 'Government Accrual Accounting: Revised Inventory Control Regulations'. A physical inspection of selected rooms was carried out by the National Audit Office (NAO).

Personal Emoluments

The audit also sought to ensure that personal emoluments for 2015 were appropriately recorded and processed according to the PSMC and other pertinent circulars. The adequacy of internal controls, intended to ensure accuracy and validity of salary payments, was also determined.

Emoluments in favour of 10 employees, in addition to nine members of the General Contracts Committee, were selected for testing. Factors considered for sample selection included, employees in various grades, others on a reduced work schedule or teleworking arrangements, as well as employees who commenced or terminated their employment during 2015.

Testing focused on ensuring the accuracy of salaries paid to the sampled employees, including *honoraria* paid to Committee members, officers' entitlement to allowances and overtime paid. An analysis of the reports extracted from the electronic Attendance Verification System (AVS) was conducted to assess whether time records, Sick Leave (SL), Vacation Leave (VL) and Time Off *In Lieu* (TOIL) records, were being adequately maintained, properly authorised and that the information held was correct and reliable. Overtime claim sheets, rosters, teleworking agreements and any supporting documents were also analysed.

Control Issues – Expenditure

Additional VAT charged in respect of Lease of Equipment

During 2012, DC entered into an agreement with a supplier, for the leasing of two multi-function printers, including full maintenance costs for a period of five years at the price of €0.10 (Value Added Tax (VAT) incl.), *per* 10 copies (or part thereof).

Audit testing focused on three Payment Vouchers (PVs), whereby it was noted that in all three instances, DC was being charged an additional VAT element of 18%, over and above the rate as *per* Contract Agreement. This resulted in an aggregate overpayment of €355, in relation to the three cases tested.

Shortcomings in relation to General-use Vehicles

Audit testing revealed a lack of control over general-use vehicles. Whilst reviewing whether the logbooks pertaining to the two general-use cars were adequately kept in accordance with PSMC requirements, the following shortcomings were noted:

a. One of the logbooks was not adequately compiled, as some of the logbook sheets were not in date order and milometer readings were not consecutive.

   Moreover, the trips recorded on the last sheet of this logbook lacked the date and the only two milometer readings recorded on this sheet did not tally with the other readings traced in the logbook.

   Furthermore, the journeys performed during a certain period were not traced, consequently having unrecorded milometer readings.

b. All the logbooks of both vehicles had the following common weaknesses:

- There was no evidence confirming that the logbooks were being inspected periodically by a responsible officer, to monitor fuel consumption and to ensure that any irregular use of cars is duly identified and reported.
- No details regarding fuelling, such as requisition number and amount of litres taken, were noted on all the logbooks.
- Details were not always noted in a consistent manner and in the appropriate column. For example: the milometer readings were not being recorded for every trip; the purpose of the journey did not contain enough detail; and every trip was not accompanied by a signature of the respective officer making the journey.

Time Records not evidenced

During 2009, a retired civil servant, was engaged through a Contract for Service, in order to perform administrative support services at DC, for a period of one year. The rate at that time was €12 (VAT incl.) *per* hour, and this person was to work up to a maximum of 20 hours *per* week. With effect from April 2012, the rate *per* hour was exclusive of the VAT element, *i.e.* €10.17 (VAT excl.).

NAO tested three payments, effected to the said person, totalling €2,441. Attached to the PVs were the respective invoices, together with time records, extracted from AVS, indicating the hours performed.

Whilst verifying the respective AVS reports, it was noted that on a number of instances, the reported timings (both 'in' and 'out'), were not being recorded automatically by the system, but written down manually by the said person. Moreover, these AVS reports were neither signed nor certified by a senior officer.

Other Shortcomings

During audit testing, some other shortcomings were encountered.

a. A PV in respect of Gozo expenses reimbursement, in favour of an officer, was not signed by the responsible officer.

b. The respective Local Purchase Order of a PV amounting to €2,183 in respect of fees for professional services, was issued following receipt of invoice.

Compliance Issues – Expenditure

Shortcomings related to Inventory

Different Rooms having the same Room Number

MF Circular No. 14/99 requires that, the physical location of every asset is to be given a number which is made up of a site code and a room number. Upon analysing the Inventory Database, it transpired that on various instances, the same room number was allocated to different rooms.

Incomplete Asset Identification Number

All the Asset Identification Numbers (AINs) given to the items listed in all the Room Lists were incorrect, as the last four digits representing the 'sequence number' were omitted.

Asset Identification Number not unique

MF Circular No. 14/99 clearly indicates that "*The Asset Identification Number is to contain a unique and sequential reference which can identify the fixed tangible asset from any other asset within that Department*".

Nonetheless, upon verifying DC's Inventory Database, it was noted that on some occasions the same AIN was allocated to other assets. Similarly, on other instances, the same Sub-Asset Classification Code[1] was used, irrespective of the nature of the item.

No Asset Identification Number affixed to Assets

While conducting the physical verification, it transpired that all the assets falling within the audit sample lacked an AIN affixed to them.

The officer in charge of inventory verbally confirmed that practically none of the assets within DC is physically marked with the respective permanent identification number as outlined in the pertinent MF Circular. This resulted in a limitation of scope, since the planned testing by NAO could not be performed as intended.

Discrepancies encountered during Physical Verification

In view of the absence of AINs on items, it could not be ascertained that the assets as *per* Room Lists were the ones traced on site during inspection. Moreover, the fact that the AIN as indicated on the Room Lists was not complete, made testing more difficult. Therefore, NAO based its verifications by matching the description and quantity as indicated on the Room Lists.

Testing of rooms selected for verification revealed numerous discrepancies between the information according to the Inventory Database, against information as *per* Room Lists and what was actually traced on site. Some details as recorded in the Inventory Database differed from those included in the Room Lists. In some instances, description of items lacked the brand and/or serial number. On other occasions, items traced on site were neither included in the Room Lists nor in the Inventory Database.

Room Lists not updated to reflect Movement of Items

The rooms falling within the audit sample were verified to ensure that any movement of assets was being duly recorded. It transpired that the Room Lists were not amended accordingly upon the transfer of items from one room to another.

Items of Immaterial Value included in Inventory Database

MF Circular No. 14/99 indicates that tangible assets of immaterial value are not to be included in the inventory records. Following an analysis of the Inventory Database, it transpired that various items of insignificant financial value were included.

Shortcomings related to Travel

Whilst testing two visits, it transpired that the four travelling officers extended their visit by some days, which were not for official purposes. Nonetheless, in both instances, no quotations, showing the different costs of the return flights between the ones chosen and an alternative flight departing sooner, were traced in file.

[1] The purpose of this classification code is to determine the nature of the fixed asset and provide further sub-division of such asset.

The Department of Contracts confirmed that even though the extra days spent abroad were not on official business, the respective VL record cards of the two officers in respect of one of these visits, did not reflect the utilisation of VL, due to misplaced VL application forms. Following NAO's query, the pertinent VL record cards were updated accordingly.

Key Issues – Personal Emoluments

Weaknesses in recording of Attendance

Attendance Verification System being supported by a Manual System

Over the years, DC introduced flexibility in employees' work schedules. Since the current AVS was never updated to accommodate such measures, DC introduced the use of a spreadsheet, referred to as 'TOIL Database', in order to keep track of extra hours worked and/or underworked by every employee.

This TOIL Database is manned by the person who is engaged on a contract basis, whose main task is to verify the clockings of each employee on a daily basis, input them manually into this Database, taking into consideration the working arrangement, break time, SL and VL where applicable, and calculate the hours over/underworked. Such Database started being used as from June 2015, whereas in the previous months, calculations were recorded manually.

Therefore, in order to control the attendance of approximately 60 employees, DC is incurring supplementary overheads, through the engagement of a person on a Contract for Service, to be able to manage the AVS and the TOIL Database.

Attendance Verification System Reports with Incorrect Data

During verification, it was noted that AVS contained incorrect or missing data on employees, leading to inaccurate reports, as further detailed below:

a. The actual working hours inputted in AVS reports did not always reflect the current working hours being performed by the respective employee. For example, the working hours of an employee who has been on a 20-hour reduced timetable since 2007, were portrayed in the system as those of a full-timer.

   In another example, the working hours of two officers, as inputted in the system, did not reflect the difference between the winter and summer schedule. On another instance, the working hours as shown in the system, in respect of an employee who was performing watchman duties on a shift basis, were also not in accordance with his actual working schedule.

b. On those occasions where VL and TOIL were utilised in hours and not as a whole day, AVS reports did not portray the actual hours of VL and/or TOIL availed of.

   The Department indicated that the functions of the current electronic system in place are restricted as the current AVS module available does not cater other than for a full day's work.

   It is evident that the parallel running of both AVS and TOIL Database is not providing the Department with an adequate attendance recording system, which suits its present needs. Moreover, the costs incurred for administrating both systems are not providing DC with value for money, since neither provides accurate information.

Officers' Clockings not always evidenced

Despite that an AVS is in place at DC, this was not being properly utilised by the employees. Upon verifying the AVS reports of the officers falling within the audit sample, various instances were traced whereby the respective officers failed to record their 'in/out' time.

Since DC makes use of the TOIL Database to complement AVS, NAO determined that in those cases where clockings were not logged on AVS, such Database was useful enough to depict the missing information. The period verified was from June to December 2015, covering the months when TOIL Database was in use.

During testing, it transpired that the missing clockings as *per* AVS report could not be obtained from the TOIL Database, because no further record of such timings are kept. In fact, for every instance encountered on AVS reports, no timings could be traced except for computed added/deducted time as *per* TOIL Database. Testing also showed that sampled officers failing to register their clockings were quite frequent during these six months.

The person in charge of TOIL Database verbally explained that on those occasions when officers did not record their timings, the actual clockings were obtained *via* telephone, but that records thereof were not being kept. Therefore, it could not be ascertained that TOIL Database computations were accurate and that the total number of working hours performed by officers was also correct.

Documents made available following NAO Queries

a. Upon verifying the VL as *per* record card and application forms, as well as AVS reports pertaining to an employee, various discrepancies were noted which were forwarded to DC for clarification.

   According to the VL record card and AVS reports, this officer was on leave on a particular day, however the respective VL application form was not traced. Moreover, according to AVS reports, the same officer was also on leave on five other separate days, but these dates were not recorded on the VL record card, whilst the respective application forms were missing.

   Following NAO's query, DC provided the respective application forms. However, this Office noted that such forms were incomplete and not assigned a sequence number[2]. Subsequently, such forms were completed and given the sequential numbers.

   Moreover, the VL record card of this officer was amended to reflect the VL applications in question and update the VL entitlement accordingly. NAO noted that an entry, which was originally crossed-off, was amended to show VL utilised.

b. NAO verified whether any unutilised VL as at end 2014 was correctly carried forward to 2015 and supported by the necessary approvals.

   Testing revealed that in two instances, the respective requests and approvals thereof, in respect of two officers, were not traced in their personal files. These documents were made available when requested by NAO.

   On another instance, the request letter in respect of another officer, was found attached to the VL record card. This letter, which was unsigned by the respective officer, lacked the necessary approval from a senior officer. Following query, NAO was provided with a signed and approved request letter.

[2] This is an internal system used by DC, whereby every application form is given a number, showing that it has been processed by the officer in charge.

Control Issues – Personal Emoluments

Vacation Leave Application Forms lacking Date of Approval

All the VL application forms verified during testing lacked the date of approval. Therefore, it could not be ascertained whether approval from the respective senior official was done in a timely manner.

Requests for Approval for Overtime Work not raised

Section 3.2.1.2 of the PSMC requires Government Departments to formally request the prior approval of any required overtime work from the respective Permanent Secretary.

During the year under review, no such requests were prepared by DC, on the basis that Management verbally indicated that it was not aware of such requirement. To this effect, DC confirmed that they started to comply with this procedure and a request in terms of PSMC was made for the period July to September 2016.

Other Shortcomings in relation to Personal Emoluments

While conducting audit testing, various other observations were noted, which are outlined below:

a. The overtime performed during the year under review by an officer who was assigned duties as a watchman, was verified against the respective rosters. Various discrepancies were noted in the overtime paid, which resulted in an underpayment of €96.

   Whilst verifying the VL entitlement of the said officer for 2015, as worked out by DC, it transpired that this officer exceeded his entitlement by 43 hours. Moreover, various discrepancies were noted between the VL record card, the roster, AVS reports, as well as VL applications forms.

   Furthermore, upon verifying the rosters made available, it was noted that for October 2015, being the last month of employment, the same officer did not sign the roster on those days when he was on duty.

b. Upon verifying the VL entitlement of an official who started employment with DC on 1 October 2015, NAO noted that the amount of 129.75 hours unutilised VL as at end 2015 was carried forward to 2016, thus exceeding the limit of 96 hours specified in PSMC regulations.

   Following enquiry, NAO was immediately provided with an amended VL record card, showing 96 hours being carried forward to 2016. Following that, NAO brought to the Department's attention the officer's request and approval to carry forward the unutilised balance of 8.75 hours VL from 2015 to 2016. Without hesitation, the VL record card was once again amended in the presence of an NAO official, in order to reflect such unutilised balance.

c. Two officers carried forward 62 hours and 18.5 hours VL respectively, from 2014 to the following year. As *per* communication traced in their personal files, it transpired that the respective requests to transfer these hours were dated January 2015.

   Moreover, as at end 2014, the remaining balance of unutilised VL of two other employees, was 106 hours and 101.75 hours respectively. Both officers requested approval to carry forward 96 hours to the following year. Nonetheless, upon verifying the VL record cards, it was noted that 106 hours and 101.75 hours were actually carried forward to 2015, thus exceeding the stipulated limit under PSMC regulations.

d. On seven instances, an employee was on SL as indicated on the SL record card and respective medical certificates. However, these were not reflected on the AVS reports. Upon bringing these discrepancies to the attention of DC, the respective AVS reports were updated to feature these aforementioned seven instances.

In another instance, another officer was on SL as *per* record card. However, the supporting medical certificate was not traced, although the record card reported the day as 'certified' SL.

On another day, an employee did not clock 'in' and 'out' as *per* AVS report. Notwithstanding that this officer was recorded as being on SL in the TOIL Database, such date was not traced on the SL record card.

e. An officer applied for 8.75 hours VL as *per* VL application form. However, these were not deducted on the VL record card. Moreover, these were recorded as TOIL on the AVS reports, whilst six hours were deducted on the TOIL Database.

Furthermore, while verifying the VL availed of as *per* record card and AVS reports against the TOIL Database[3] of the same officer, it was noted that on six instances, instead of being marked as VL, at times the officer was erroneously granted TOIL, while in other instances TOIL was deducted.

f. An analysis of overtime performed by an employee during the summer schedule, revealed that no break periods were taken into consideration and thus deducted from overtime paid, which resulted in a total of €172 paid in excess. This is in breach of S.L. 452.87 – 'Organisation of Working Time Regulations', whereby every worker is entitled to a rest break of not less than 15 minutes after working more than six hours at a stretch.

Moreover, while verifying the overtime claim sheets in respect of this officer, the overtime claimed on two days, could not be substantiated against AVS reports, because such officer failed to clock 'in' and/or 'out' on the days in question. Nonetheless, overtime payment was still effected.

On the other hand, the same officer performed eight hours of overtime over two days. However, as *per* overtime claim sheets made available, only two hours were claimed each day, and consequently paid.

Recommendations

Control Issues – Expenditure

Additional VAT charged in respect of Lease of Equipment

More effort is to be made to ensure that all invoices requesting payments are vetted for correctness against supporting documentation and contract terms agreed upon, before being processed for payment. Moreover, DC is to carry out a full exercise to identify the total amount overpaid to this supplier, followed by the necessary steps to recoup the excess paid.

Shortcomings in relation to General-use Vehicles

Management is recommended to refer to the PSMC, in particular Section 8.2.4, to regulate the use of vehicles. These guidelines stipulate that a proper logbook should be kept for each vehicle to record the exact mileage covered and other journey details.

[3] Period verified was from June to December 2015.

Each logbook is to be certified by the officer in charge of transport at the end of each month, in accordance with Section 8.2.5 of the PSMC, to ensure that the trips recorded in the logbook were made on official duty and that fuel consumption was reasonable.

Moreover, full details regarding fuel intake are to be clearly recorded on every logbook as *per* Appendix 8.I of the PSMC, as a means to verify each general-use vehicle's fuel consumption.

Time Records not evidenced

The Department of Contracts is to make sure that AVS is reliable and that all clockings, both 'in' and 'out', are recorded. Moreover, every effort is to be made to ensure that any supporting documents on which payment is effected are to be duly endorsed and verified prior to effecting payment.

Other Shortcomings

All PVs should always be clearly endorsed, in order to indicate the responsible officer authorising the payment accordingly.

The Department is to make sure that officers observe the standard purchasing procedures. This will ensure that proper authorisation for the purchase is obtained and that adequate funds are also committed to cover the expense.

Compliance Issues – Expenditure

Shortcomings related to Inventory

Management is to ensure that officers entrusted with the upkeep of inventory records fully adhere to the Circular's requisites. This would eventually ascertain adequate and harmonised accrual accounting data.

All assets are to be recorded accurately within the Inventory Database. These are to be adequately identifiable with a permanent identification number, as far as is practical. Officers in charge are to ensure that information, including brand and/or serial number, entered into the Inventory Database and recorded in Room Lists, is accurate and complete. Room Lists are also to be updated to reflect latest movements. Both the Inventory Database and Room Lists should contain the same information, and any discrepancies resolved.

All sites/rooms should be appropriately identified and assigned a unique number. This would then be reflected in the Inventory Database and respective Room Lists. Periodic physical verification of inventory items is also recommended, to ensure that inventory records truly reflect the description and location of items.

Shortcomings related to Travel

For the sake of transparency and good practice, if officers decide to extend their stay for reasons other than those on official business, quotations, indicating the difference, if any, in the cost of flights, are to be invariably sought. If the cost of the return flight is higher, the responsible officer is to personally incur the difference in price.

In the event that officers opt to prolong their visit on non-Government business, the extra days are to be deducted from the officers' VL entitlement, as long as they do not fall on a weekend or national/public holiday.

Key Issues – Personal Emoluments

Weaknesses in recording of Attendance

Management is encouraged to review its current attendance record system and improve it to better suit its needs. An improved electronic system would not eliminate all weaknesses, but should reduce errors which are more prone to arise from the use of the manual system. Moreover, in addition to providing reliable and accurate records, such system may also result in better perception of transparency and fairness for all employees.

Officers' Clockings not always evidenced

While both the electronic and manual attendance systems are in themselves an element of internal control, incomplete and inaccurate records thereof hinder the benefits that are expected to be attained. Thus, Management is to ensure that all employees clock 'in' and 'out' every time they report to or leave their workplace. Moreover, immediate disciplinary measures are to be taken against those officers who fail to adhere to such directives.

Documents made available following NAO Queries

Management is to ensure that officers entrusted with the upkeep of records are aware of their responsibilities and that only trustworthy information is to be forwarded to third parties. It is also important to maintain proper records for a sound system of internal control, as well as a reliable audit trail.

In order to minimise the risk that important records are misplaced, VL application forms, as well as requests and subsequent approvals for accumulated VL, are to be systematically filed and retained for future reference.

Control Issues – Personal Emoluments

Vacation Leave Application Forms lacking Date of Approval

It is recommended that for control purposes, the date of approval of VL is recorded by the respective senior officer upon authorisation. Moreover, VL is to be authorised prior to utilisation.

Requests for Approval for Overtime Work not raised

A detailed analysis of the necessary additional hours and required personnel is to be prepared prior to the performance of overtime work. DC is also to ensure that these overtime requests are duly authorised by the Permanent Secretary, as *per* PSMC.

Other Shortcomings in relation to Personal Emoluments

The maintenance of proper, correct and reliable records is a fundamental element of a sound system of internal control over personal emoluments.

Regular reconciliations between AVS reports and VL, as well as SL records, are to be performed by the officer in charge, to ensure that any relevant documents and records are updated accordingly. Requests for transfer of VL hours from one year to the next are to be raised in a timely manner and in line with PSMC requirements.

NAO acknowledges that due to potential staff shortages, workload pressures may accumulate. Nonetheless, it is advisable that officers are encouraged to take the assigned break time, as outlined in the pertinent working time regulation. Moreover, every effort is to be made to ensure that overtime claim sheets are duly verified and tallied against related records, prior to effecting payment, in order to avoid any discrepancies.

Furthermore, NAO is again recommending DC to reconsider the enhancement of the present AVS, so that typical weaknesses, as outlined above, are minimised. DC is to make the utmost use of its system(s) in place.

Management Comments

In its reply, Management took note of the observations, and immediate action was taken to fully implement most of the recommendations put forward by NAO. This Office satisfactorily noted that Management acknowledged "*... in the absence of a proper internal audit function within Government, this kind of audit is indeed an important tool for good governance*." The following additional comments were also forwarded:

Additional VAT charged in respect of Lease of Equipment

Management appreciated that through NAO's audit, attention was drawn to this error and to that effect, immediate action was taken. The respective Contractor was notified and the error was acknowledged. NAO was informed that DC is at present liaising with the Contractor in order to agree on the precise amount to be recovered and on the best method to carry this out.

Time Records not evidenced

Management maintained that in such cases, the person confirms the time of attendance to the Human Resources (HR) Section and the respective Director is also copied in this process. However, NAO was not provided with any evidence in this regard.

The Department also stated that each invoice, accompanied by a detailed work schedule, is verified and endorsed by the Director General (DG).

Shortcomings related to Inventory

To address the issues in this regard, Management claimed that an Accounting Support Officer will be assigned duties to assist the person presently in charge of inventory, and the Senior Manager (Administration) will be asked to oversee and guide in terms of implementation. DC envisages to be in compliance with MF Circular No. 14/99 by the end of 2016.

Shortcomings related to Travel

By way of corrective measures, immediate action was taken during NAO's audit, whereby an email was sent to the Accounts Section and copied to Senior Management, outlining the fact that three quotations are to be invariably sought regarding flight arrangements, in respect of the dates of the training/conference and also for any extended stay.

Weaknesses in recording of Attendance

Management indicated that back in 2013, DC had budgeted for an update of the AVS through the purchase of an additional module to the basic one of Time and Attendance. Nonetheless, the Department was not granted the 'go-ahead' by the then Public Administration Human Resources Office, "... *as at the time Government's Corporate Policy on the subject was being revised following the piecemeal introduction of AVSs in some Departments*". According to DG Contracts, to date, there is no corporate policy governing AVSs.

The Department maintained that manual adjustments are "... *of utmost importance as it enables the Department to offer family friendly measures to all members of staff*." In its reply, Management confirmed that the Department intends to update or replace the current AVS, provided that the necessary funds are made available. In fact, for the forthcoming 2017 budget, DC has requested funds to upgrade the system or purchase a new AVS.

Officers' Clockings not always evidenced

Although Management agreed that the electronic and manual attendance verification system can be improved, it stated that, at least for the present, it prefers not to implement NAO's recommendations whereby officers have to invariably clock 'in/out' and to take disciplinary action accordingly.

Management maintained that it prefers to continue to adopt the Corporate Policy in respect of temporary absences, until the present AVS is eventually upgraded. NAO would like to point out that even though various queries were raised during the course of the audit, Temporary Absence Sheets were not presented.

Requests for Approval for Overtime Work not raised

Management stated that "... *only one person works overtime hours and a justification in this respect is submitted to MFIN each year as part of the preparation for the annual budgetary planning*."

Other Shortcomings in relation to Personal Emoluments

The Department acknowledged all the observations, risks and recommendations in this regard. Management indicated that work is being carried out to verify the contents of this Report in detail with its records and eventually take the necessary action.

Management reiterated that renewed effort will be made to implement the recommendations with respect to the proper reconciliations and updating of HR records. To this effect, since July 2016, an officer was assigned duties at the HR Section. Furthermore, where amounts were under or overpaid, action will be taken accordingly.

The Department also ensured that as *per* DC Internal Circular No. 1/2015, members of staff are reminded to avail of the mandatory minimum 15-minute break time after six hours of work. Moreover, in terms of overtime claim sheets, Management claimed that it has been standard practice for the HR Section to verify overtime hours and for the Director (Administration) to authorise accordingly.

Ministry for Energy and Health

Sir Paul Boffa Hospital

Contractual and Professional Services

Background

Sir Paul Boffa Hospital (SPBH) provided specialised in and outpatient services for Dermatology, Oncology and Palliative Care. From 7 September 2015 onwards, only Dermatology services continued being provided from this hospital as the other services were transferred to the newly inaugurated Sir Anthony Mamo Oncology Centre (SAMOC). However, as of late December 2015, new admissions of patients requiring long-term care were made at SPBH as a temporary measure to ease the burden from Mater Dei Hospital (MDH).

For financial year 2015, the revised budget earmarked for Contractual and Professional Services stood at €3,550,000 and €100,000 respectively, with actual expenditure eventually totalling €3,529,462 and €98,860.

Audit Scope and Methodology

The main objectives of the audit were to evaluate the system of internal controls relating to the procurement of Contractual and Professional Services, ensuring that funds were spent for their intended purposes, within the approved limits, and in line with the provisions of standing Public Procurement Regulations (PPR).

Other objectives were to ensure that Management discharged proper responsibilities in the exercise of its financial authority, notably with respect to the application of Articles 28 and 29 of the Financial Administration and Audit Act. Thus, audit testing was aimed to obtain reasonable assurance that payments effected were accurate, duly covered by supporting documentation enabling verification, and in line with applicable agreements.

The sample selected, comprising 130 invoices amounting to €1,648,709, was based on materiality and related risks.

Limitation on Scope of Audit

Patients' Meal Orders

Original menus or any other documentation showing the actual meals ordered by the patients were not available for audit purposes. This, together with other lacking controls as outlined in the respective findings, hampered the National Audit Office (NAO) from carrying out the necessary verification on such expenditure.

Key Issues

Lack of Internal Control

Audit testing revealed lack of internal control, synonymous to Management by crisis in various instances as indicated below. These cases will also be outlined separately further down in the Report under the pertinent observations, which mainly covered:

- expenditure falling outside the scope of the contracts in force;
- necessary authority for procurement not available or obtained retrospectively; and
- habitual contract extensions hindering fair competition.

The fact that procurement authority for a number of services of substantial value was being obtained in terms of Article 60 of the PPR, *i.e.* through negotiated procedure without prior publication of a European Union contract notice, was also a case for serious concern. In fact, the frequency with which negotiated procedure was being resorted to, as well as the considerable amounts disbursed, raised questions as to whether the respective PPR provisions were being breached or abused. *Table 1* details the instances encountered.

Table 1: Procurement Authority in terms of Article 60

Service Procured	Period Covered	Approval Reference[1]	Estimated Cost
			€
Security services at MDH and other entities within the Health Division	3/9/2013 – 2/9/2014	Article 60(b) and (c)	2,004,000
Security services at MDH and SAMOC	2/9/2014 – 31/12/2015	Article 60(d)	3,610,139
Care worker services at MDH, SAMOC, SPBH, Primary Health Care, Mount Carmel Hospital and Rehabilitation Hospital Karin Grech	4/5/2014 – 31/12/2015	Article 60(b)	11,082,101
Cleaning services at MDH and SAMOC	1/11/2015 – 31/5/2016	Article 60(b)	5,079,000

[1] Article 60(b):
"*when, for technical or artistic reasons, or for reasons connected with the protection of exclusive rights, the services may be provided only by a particular economic operator*";

Article 60(c):
"*where the contract concerned is awarded subsequent to a design contest and must be awarded to the successful candidate or to one of the successful candidates in which case they shall be invited to participate in the negotiations*";

Article 60(d):
"*in so far as is strictly necessary, when the time-limits for open, restricted or negotiated procedures referred to in regulations 40 and 41 cannot be respected for reasons of extreme urgency occasioned by unforeseeable events. The circumstances invoked to justify urgency must not be attributable to the contracting authority*".

Patients' Catering Services

Background

In December 2006, a service provider was awarded the contract for the provision of catering services to inpatients at MDH, SPBH and St. Luke's Hospital, following a call for tenders by the Department of Contracts (DC). As per section 38 of the original agreement, the contractor was bound to render the services for a period of 10 years starting from November 2007, being the date on which the migration from St. Luke's Hospital to MDH was practically completed. In line with the applicable agreement, two years prior to the expiry of the initial term, *i.e.* in 2015, the parties had to determine whether to extend the contract for a further period of five years.

Total disbursements amounting to €169,308 were effected from SPBH recurrent vote during the year under review.

Contract Extension Ambiguity

Notwithstanding that the provisions of the agreement indicated that an extension would be considered in 2015, through letter of intent dated 7 March 2013, DC extended the contract for an additional five years. Such extension was made on the condition that the existing meal prices would not be revised and that the service provider would finance the procurement of additional equipment, worth approximately €500,000, to cater for the increase in meal quantities, whilst maintaining the necessary quality control and food safety requirements.

Documentation reviewed confirmed that, as the original term of the contract was for a period of 10 years, the contract was extended from 2017 until the year 2022.

Furthermore, the conditions under which the contract was extended were deemed superfluous due to the following reasons:

a. as per section 12 of the contract, the costs of the necessary equipment were always expected to be borne by the supplier; and

b. the financial bid submitted had already provided for the number of meals to be in excess of 1,840 daily. Moreover, NAO was informed that during December 2015, the average number of meals supplied under this contract averaged only 1,688. Thus, there was no increase in meal quantities when compared to what was agreed upon.

Scope of the Agreement not Comprehensive

Addendum No. 1 to the contract agreement was drawn up on 19 October 2015 and approved by DC, specifically to exclude SPBH from the scope of the agreement whilst including SAMOC upon the commencement of its operations. It also catered for additional meals that were to be provided by the contractor, as SAMOC had 37 beds for inpatients over and above SPBH capacity of 50. The following shortcomings were noted in this respect:

a. Whilst SAMOC effectively commenced operating on 7 September 2015, the agreement to cater for its inpatient meals was signed over a month after this date. Thus, the provision of meals to SAMOC remained uncovered by the agreement for more than a month following inception.

b. The delivery of meals to the Dermatology Ward patients at SPBH continued, despite that the latter was specifically excluded from the scope of the contract. Thus, the respective expenditure was in actual fact not authorised.

c. By the end of December 2015, the service provider also started providing additional meals to the inpatients at the newly refurbished wards for Long Term Care, situated at SPBH. In fact, by the end of the year, the daily number of inpatient meals recorded as consumed at SPBH reached 42. NAO was not informed that any official agreement for the provision of meals to SPBH had been reached by the time this audit was concluded.

Late Undertaking of Insurance Policy

As per section 29 of the agreement, the catering contractor was bound to provide evidence of the existence of insurance policies to safeguard the client from potential mishaps. However, the insurance policy, which was due for renewal on 13 November 2015, was only renewed on 9 December 2015, following audit queries.

NAO also noted that the previous insurance policy, which expired on 13 November 2014, was only renewed on 3 February 2015.

Lacking Controls hampering the Verification of Invoices

NAO noted instances where adjustments were necessary to rectify the incorrect number of meals charged. A review of the ordering process revealed that the service provider was responsible for the data collection system to process the meal orders. To this effect, individual Menu Sheets containing the selected meals are collected from each inpatient by ward staff and handed over to the contractor's representative.

Subsequently, the 'Menu Selection Summary', which constitutes the delivery note, is given to each ward upon the distribution of meal trolleys. These documents are then forwarded to the Finance Section for invoice verification purposes. The following audit concerns were raised in this regard:

a. Copy of documentation showing the actual orders by the patients was not kept, thus one could not reconcile the meals ordered with those invoiced. In view of this absence, invoices were only checked against the delivery note, namely 'Menu Selection Summary' prior to payment. This also resulted in inadequate audit trail.

b. A review of the 'Menu Selection Summary', covering a sample period of six days of all five wards within SAMOC, revealed various discrepancies[2] between the 'Menu Count', which is the number of meals recorded as delivered, and thus charged for, and the items listed as chosen by the patients, indicated within the same document. A shortfall of 112 meals, comprising 50 lunches and 62 dinners, amounted to an adverse variance of €574 over a period of just six days.

c. Staff at the Palliative Care Unit, which was one of the wards where inconsistencies within the 'Menu Selection Summary' were encountered, verbally confirmed that, due to operational constraints, this document is endorsed without checking the contents of the trolley containing the meals.

d. Verification by the Accounts Section comprises the inputting of the 'Menu Count' indicated on the daily delivery order (lunch and dinner) for each ward on a spreadsheet, for the eventual reconciliation with the number of meals charged on each invoice. No consideration is given to the fact that such 'Menu Count' had not been previously confirmed to reflect the actual meals delivered. Thus, such verification is actually ineffective. Furthermore, NAO could not confirm whether any reconciliations were performed by SAMOC during 2015, to ascertain that the total meal orders did not exceed the number of inpatients in a given period since a query in this regard remained unanswered.

[2] Exact quantification of the discrepancies was not possible as the service provider charges for full meals whilst the items listed as delivered at times showed single item selection. Additionally, the agreement does not include a breakdown of the prices of the different components of each meal besides clear soup, dessert and sandwiches. Thus, in order to give an indication of the discrepancy, this was calculated as the difference between the number of meals charged by the supplier and the main meal component, multiplied by the cost of each meal.

Agreement Provisions not applied

The tender document required catering bidders to submit a quote for snacks and also stipulated that these options should always be shown, both on the lunch and dinner menus, giving patients the possibility of ordering a snack instead of the full meal. Although, prices for hot and cold snack boxes were provided by the contractor, the actual snack options were not included in the respective menu cards.

Provision of Staff Meals[3]

Background

Following a departmental call for tender, letter of acceptance dated 1 July 2012 informed the caterer that it was awarded the contract for the supply of staff lunches at SPBH for a period of one year, commencing 30 days after the date of the foregoing document. The contract could be extended on a monthly basis for a further period of 12 months, up to a total value of €120,000 excluding Value Added Tax (VAT), whichever was the earliest.

However, as at October 2016, both SAMOC and SPBH staff meals were still being supplied by the same caterer, at the tendered price of €5.66 per meal. NAO could not confirm total disbursements as from inception of the applicable contract, since such query remained unanswered. However, during the year under review the related expenditure amounted to €151,738.

Formal Extensions not available

Although staff lunches continued to be procured from the same supplier beyond the initial one-year term, no evidence of an official extension to the contract period, *i.e.* from August 2013 onwards, was furnished to NAO for audit purposes.

Procurement not in line with Standing Regulations

Retrospective Approval

On 4 March 2015, the Ministry for Health approved a variation of €38,400 above the original maximum value of the tender of €120,000 (VAT excl.). This related to an extension to the contract, covering the period starting from June 2014. Thus, procurement for the nine months in question was still carried out through an unauthorised direct order until approval was obtained retrospectively. Moreover, as indicated further down in this Report under the pertinent sub-title, no evidence was made available to confirm that this variation was published in the Government Gazette.

Unauthorised Procurement by Direct Order

The retrospective approval referred to above related only to SPBH staff meals and covered until May 2015 or until all staff was migrated to SAMOC; whichever came first. This implies that staff meals procured after May 2015, both for SAMOC and SPBH staff, were also obtained by direct order without the necessary Ministry for Finance (MFIN) approval.

The total expenditure for staff meals authorised by the Ministry for Health covering from July 2012 onwards amounted to €180,000[4]. However, such payments during 2015 alone amounted to €151,738, thus the aggregate amount spent exceeded by far the amounts authorised for procurement. The total negative

[3] Another concern related to the 'Provision of Staff Meals' also features under Control Issues.

[4] This amount is made up of €120,000 (VAT excl.), emanating from the departmental tender, plus the variation approval of €38,400 (VAT incl.).

variance remained unquantified, as information on the aggregate amount paid since inception of the contract to-date was not made available.

Provision of Internal Security Services[5]

Extensions to Contract hindering Fair Competition

Following a call for tender issued by DC, an agreement was reached with the service provider for the provision of internal security services at MDH. This was effective as from 3 September 2009, for a period of 36 months, extendable by two further periods of six months each.

When the applicable extensions expired, on 12 December 2013, approval was granted by the General Contracts Committee (GCC) for the provision of security services by the same contractor "... *at MDH and other entities within the Health Division, on a monthly basis, renewable every month up to a maximum period of one year or until the new tender is awarded, at the monthly estimated cost of €167,000 VAT Inc*". The total maximum estimated cost amounted to €2,004,000 for a whole year. Although justification did not meet the applicable criteria for negotiated procedures, such approval was inappropriately granted in terms of Article 60(b) and (c) of PPR, as already indicated in the observation entitled 'Lack of Internal Control' under Key Issues in this Report.

Furthermore, through letter of acceptance dated 15 April 2015 sent by the Central Procurement and Supplies Unit (CPSU), the same service provider was informed that the security services contract, covering MDH and other entities within the Health Department, was once more being extended on a monthly basis, again through negotiated procedures. This notification was effective retrospectively as from 3 September 2014 until 31 October 2015. *Table 2* refers.

Table 2: Provision of Internal Security Services Contract and Extensions

Type	Period	Duration	Estimated Cost
			€
Contract	3/9/2009 – 2/9/2013	48 months	7,400,000
Extension	3/9/2013 – 2/9/2014	12 months	2,004,000
Extension	3/9/2014 – 31/10/2015	14 months	3,509,344
Total			**12,913,344**

In the meantime, the provision of security services continued notwithstanding that it was not covered by any further approval. According to Management, in May 2016, CPSU was still awaiting clearance from GCC, following the conclusion of negotiations, to have the contract extended yet again.

Substantial Additional Security Hours not approved by the General Contracts Committee

The maximum expenditure approved by GCC on SAMOC internal security services for year 2015 was €217,073, consisting of 1,750 hours monthly at the rate of €8.76 per hour (VAT excl.), but inclusive of social costs[6]. Such approval[7] was granted in terms of regulation 60(d) of the PPR, as depicted in *Table 1* under the finding entitled 'Lack of Internal Control' under Key Issues.

[5] Other concerns related to the 'Provision of Internal Security Services' also feature under Control Issues.

[6] Besides the basic rate, this includes vacation leave, bonus and/or weekly allowance, public holidays, national insurance contribution and an average sick leave of six days.

[7] The approval, which amounted collectively to €3,610,139, also comprised MDH.

However, testing revealed that total expenditure incurred during the year in this regard amounted to €1,100,204, resulting in an unauthorised expense of €883,131. NAO was informed that the decision to increase security hours was taken by the Foundation for Medical Services, since expensive equipment was being installed at SAMOC while the building was still under construction.

On 25 October 2015, after obtaining the consent of the Permanent Secretary, approval from DC was requested retrospectively to revise the man hours as follows:

- from January to June 2015, 10,300 hours per month at a cost of €106,469, aggregating to €638,814 for the six-month period in question; and

- from July till December 2015, 9,000 hours per month at a cost of €93,031 monthly, aggregating to another €558,186.

However, GCC refused to sanction the request for the contracting of the additional hours for the year 2015, due to non-adherence to PPR. Notwithstanding this, DC reminded Management that payment for services rendered was still due to the company on the basis of a civil obligation.

Control Issues

Cleaning Services at Sir Paul Boffa Hospital

Lack of Control over Attendance Records

Following the sudden termination of the contracted cleaning company's services at SPBH and all other hospitals and health entities within the Ministry, approval from the Direct Orders Office within MFIN was obtained to engage various companies in order to provide such services in a number of different areas until a tender was awarded. In accordance with CPSU's instructions, these services were rendered on a temporary basis at SPBH between October 2014 and January 2015. The total expenditure incurred in 2015 by SPBH covered services rendered in December 2014 and January 2015, which amounted to €19,002.

The audit sample included the two payments effected to one of the temporary service providers for the aggregate amount mentioned above. It was noted that although the invoice for January 2015, amounting to €4,646, was supported with the relative 13 timesheets indicating the hours worked, these were not signed by the respective cleaners and housekeeper. Moreover, the timesheets were not endorsed by anyone from SPBH. This indicates lack of control over the record-keeping of hours worked and ultimately the respective payment.

Cleaning Services at Mater Dei Hospital and Sir Anthony Mamo Oncology Centre

Procurement of Cleaning Services not formalised

Approval was obtained from GCC to enter into a negotiated procedure in terms of PPR Article 60(b), for the procurement of cleaning services at MDH and SAMOC with *Servizi* Malta. As outlined in the observation entitled 'Lack of Internal Control' under Key Issues, this approval for a seven-month period, commencing 1 November 2015 until 31 May 2016, amounted collectively to €5,079,000.

According to communications received from CPSU Manager, in May 2016, negotiations in this respect had been concluded. However, by the end of this seven-month period, the agreement between the contracting authority and the service provider had not yet been formalised.

Software System Maintenance Agreement not formally renewed

An agreement between SPBH and the service provider, signed on 7 October 2011, included the provision of maintenance and support of a software system for a period of three years. This agreement could be renewed for an additional three years under the same terms and conditions, subject to SPBH giving written notice to the service provider, not less than 30 days prior to expiry.

However, although the services of the company were still being resorted to during the year under review, the relative formal renewal was not in place.

Care Worker Services

Background

Following negotiated procedures for the procurement of care worker services at various entities within the Health Division, namely MDH, SAMOC, SPBH, Primary Health Care, Mount Carmel Hospital and Rehabilitation Hospital Karin Grech, a letter of acceptance was issued to the service provider in April 2015. The entire approval from GCC, which covered the period from 4 May 2014 to 31 December 2015, amounted in total to €11,082,101.

Payments effected from SPBH Cost Centre to the service provider in question during the year under review amounted to €216,658.

Letter of Acceptance not in line with Finance Approval

As already noted under Key Issues, in April 2015 MFIN approval for the procurement of care worker services was granted in terms of regulation 60(b) of PPR. This relates to approval for a negotiated procedure without prior publication of a European Union contract notice, specifically when services may be provided only by a particular economic operator "*… for technical or artistic reasons, or for reasons connected with the protection of exclusive rights …*".

The respective letter of acceptance CPSU 0268/2015 relates to an extension of care worker services contract through negotiated procedures, erroneously making reference to contract agreements CT 2399/2008 and CT 2080/11. It is pertinent to note that SPBH and SAMOC did not feature in the foregoing agreements.

Services not covered by Agreement and necessary Approvals

MFIN approval for the procurement of care worker services was obtained on 26 April 2015. In view that such approval covered the period 4 May 2014 till the end of the year 2015, this implies that for almost a whole year, such services were obtained by direct order without the necessary Finance approval, until this was obtained retrospectively.

Although care worker services were still being provided, up to audit conclusion, *i.e.* July 2016, retrospective approval for the remaining period was still pending.

Furthermore, the respective letter of acceptance dated 30 April 2015, bearing reference CPSU 0268/2015, only covered care worker services from 4 May 2014 until the end of October 2015. No further agreements were entered into following this date.

Performance Guarantee

The letter of acceptance referred to in the preceding observation stipulates that "*All other terms and conditions remain the same as per contracts CT2399/2008 and CT2080/11. A valid bank guarantee is to be submitted in line to the terms and conditions and presented to this office*". The following shortcomings were noted in this respect:

a. Given that the value of the letter of acceptance, as per direct order approval, amounted to €11,082,101, the value of the bank guarantee, which was set at 10% of the contract value should have amounted to €1,108,210. However, the only performance guarantee made available for audit purposes amounted to just €270,700. This was equivalent to the bank guarantee which was required under a previous contract, namely CT 2399/2008, relating to services at MDH and Primary Health Care.

b. The performance guarantee was dated prior to the letter of acceptance and expired in May 2015. SAMOC's statement that this guarantee was extended until May 2016 was not supported by evidence.

c. The bank guarantee document presented makes reference to CT 2399/2008 even though Management had been specifically instructed by DC that this guarantee reference cannot be used. Following an NAO query, no explanation was forthcoming from MDH to this effect.

Timesheets

Hours worked by care workers under the agreement in question are recorded manually on two different timesheets, one provided by the service provider and another by SAMOC and/or SPBH. Aggregate expenditure on care workers in 2015 from SPBH Cost Centre amounted to €216,658. Detailed testing on timesheets supporting a sampled invoice, namely number 782 which related to care worker services for July amounting to €9,109, revealed the following shortcomings:

a. NAO was verbally informed that timesheets were collected on a weekly basis by the hospital administration. However, none of the timesheets were endorsed by a responsible public officer to confirm that attendance records were being checked periodically.

b. The possibility that timesheets were not being updated daily by the respective care workers cannot be excluded, as in one instance, an identical mistake was made and then overwritten on two consecutive days.

c. Attendance records were not always legible.

d. No attendance sheets were available for care workers assigned as replacement.

e. The service provider's timesheet for one of the care workers did not have the respective employee's particulars, *i.e.* the name and personal identification card number.

Attendance Verification

The tender for the provision of care worker services at MDH and Primary Health Care (CT 2399/2008) covered a four-year period from September 2009. The applicable contract specifically required the service provider to keep attendance records of all employees, by date and location, by way of "... *biometric electronic means*" at the company's expense. Such equipment had to be fully and immediately available to the client.

However, in February 2016, MDH confirmed that, although the service provider promised to install four such points, this requirement was not met. NAO was later informed that the contracted firm would eventually be installing the equipment at its expense and a meeting in this regard was scheduled on 1 June 2016.

Adjustments to Invoices

The absence of electronic attendance records led to the creation of six credit notes in 2015, to compensate for the various adjustments necessary to cover 13 instances of overcharging, following the checking of invoices against manual timesheets by the Accounts Section.

The excessive paperwork makes the checking of invoices time consuming, cumbersome and still prone to error.

Change in Staff Lunch Composition not reflected in a Change in Price

The staff lunches as per tender consisted of the provision of plated food at the rate of €5.66 per meal. However, the actual staff meals provided during the year under review was only a choice of baguettes, wraps, salads and bread charged at the same meal price. NAO could not confirm for how long this situation prevailed.

A call for tender for the provision of staff lunches, which tender also included the running of a staff and visitors' canteen, was unsuccessful as it did not attract any bidders.

During audit testing, *i.e.* April 2016, SAMOC staff was still being provided with a packed lunch. However, according to Management, when it was clear that this temporary measure was bound to take much longer than anticipated, discussions were entered into with the existing supplier to decrease the price. A recent offer by the contractor quoted a cost of €3.50 for a packed lunch and dessert. Management was planning a counter proposal to this effect.

Entitlement to Staff Meals

MDH Free Staff Meals Policy (section 3) states that employees who have direct contact with patients and who work a shift of 10 hours or more are entitled to free meals. When a roster includes days with different number of working hours, there is no such entitlement on those particular days when less than 10 hours are worked. The break time is considered to be part of the working hours and there is no distinction between grades.

Officers entitled to staff meals cannot choose to take a cash allowance instead. On the other hand, daily cash allowances of €1.40 and €0.93 for day and night duties respectively are given in the case of staff working shifts less than 10 hours.

The following shortcomings were noted with respect to staff meals entitlement:

a. SAMOC Salaries Section was aware that two officers working at SPBH stores were having staff meals instead of their entitlement to a cash allowance. Additionally, NAO was informed that another administrative officer at SPBH was also benefiting from staff meals even though she did not meet the necessary criteria.

b. SAMOC officers who previously benefited from free staff meals at SPBH when they were not so entitled, continued to enjoy the benefit following migration. NAO was informed that this matter was being discussed by Management.

c. The Accounts Clerk checks the invoices against the supplier's delivery notes prior to payment. However, the number of meals charged is not reconciled to the daily employees' attendances.

Provision of Internal Security Services

Insufficient Compliance Checking

As per letter of acceptance dated 15 April 2015, the contracting authority may request copies of employee payslips, in order to verify compliance with Contract Circular Nos. 27/2014 and 4/2015 *vis-à-vis* minimum hourly rate payable. According to MDH, the respective personnel payslips were requested twice. However, only employees' Payee Statement of Earnings (FS3s) for year 2013 and payslips in respect of October 2014, were provided for audit purposes. This implies that no compliance checking was carried out following the increase in the applicable hourly rate.

Provision of Information Technology Services

Background

Payments in aggregate amounting to €12,183 were effected to a service provider for the provision of Information Technology (IT) services. The foregoing was engaged on two consecutive six-monthly contracts for service commencing 20 February 2015. This procurement was covered by direct order approvals from MFIN.

Service not entirely covered by Agreement

Two sampled invoices, in total amounting to €1,800, were in respect of IT services rendered during the period 2 January 2015 to 25 February 2015. The agreement provided covered from 20 February 2015, thus the preceding seven-week period was not covered.

Agreements not signed by both parties

The contract covering the period 20 February to 19 August 2015, was only signed by the service provider; it was not endorsed by the Chief Executive Officer, CPSU. On the other hand, the contract covering the period 20 August 2015 to 19 February 2016 was signed by the latter but not by the former.

Invoices not endorsed prior to Payment

Four invoices, in aggregate amounting to €3,567, out of the 13 invoices raised by the service provider in question, were not endorsed by the then Chief Operations Officer.

Compliance Issues

List of Signatories not provided

The list of authorised signatories, in accordance with Treasury Circulars Nos. 5/2008 and 9/2015, was not made available for audit purposes. Moreover, testing also revealed that all payment vouchers in the audit sample, with the exception of multi-payments, were unsigned.

Publication of Awarded Direct Orders and Variation to Tender not confirmed

PPR Article 20(2) stipulates that lists of departmental contracts awarded, as well as cases involving variations of more than 5%, are to be published in the Government Gazette every six months. As per MFEI Circular No. 11/2011, this list is to include also those purchases effected through direct orders procedure.

No evidence was provided that eight direct orders, amounting to an aggregate value of €342,894, were published accordingly. Publication of the variation of 27%, to the departmental tender for the provision of staff lunch at SPBH, amounting to €38,400 was also not evidenced.

Payments to VAT Registered Service Provider bypassing the Purchases Ledger

During the year under review, payments made to a Medical Physicist engaged on a contract for service amounted to €28,426. Although the service provider is VAT registered, the invoices for services rendered were all settled through multi-payments, thus bypassing the purchases ledger. This increases the risk of having negative financial implications on the collection of income tax and VAT.

Non-compliance with VAT Legislation

Whilst carrying out the necessary verifications on the 130 payments included within the audit sample, the following were noted:

a. In 21 cases, proper tax invoices for the amount of €193,701, in line with the Twelfth Schedule of the VAT Act, Cap 406, were not provided since only the VAT registration number of the supplier was indicated.

b. In accordance with MFEI Circular No. 7/2011, service providers and/or suppliers registered under Article 11 of the VAT Act are exempt from charging VAT, but a fiscal receipt marked 'exempt' still has to be issued and furnished to the VAT registered departments. However, without prejudice as to whether a particular individual, providing IT services to the auditee, qualifies for such exemption, fiscal receipts in support of the 13 payments effected by the latter in 2015 to the foregoing individual, amounting to €12,183, were not made available.

Shortcomings in Inventory Management

Relevant documentation, covering inventory handed over from the Foundation for Medical Services to SAMOC, was available. However, proper inventory records were still being compiled by the latter. Room inventory lists were also not available.

Recommendations

Key Issues

Lack of Internal Control

The weaknesses in internal control ultimately impinge on the overall control environment within the respective functions of the hospital. In this regard, Management is encouraged to implement NAO's recommendations suggested under the respective observations for a sound audit trail and transparent procedures.

Patients' Catering Services

Contract Extension Ambiguity

Failure to abide by the original contract conditions creates ambiguities and reduces the level of transparency. Thus, such decisions are to be avoided.

Scope of the Agreement not Comprehensive

Requirements are to be duly planned in order to ensure that the respective procurement authority is obtained. Comprehensive agreements are to be drawn up accordingly.

Late Undertaking of Insurance Policy

A copy of the insurance policy is to be invariably requested and filed for ease of reference as well as for audit purposes. It is also to be ensured that such policies cover the entire contract period.

Lacking Controls hampering the Verification of Invoices

Keeping documentation to substantiate the actual meal orders is of utmost importance. SAMOC is to investigate the discrepancies highlighted during the audit and take necessary action with the supplier. Delivery notes are to be endorsed only after the details are verified with the actual meals consigned. When the delivery notes and invoices are reconciled to the actual orders, such verification is rendered more meaningful.

Agreement Provisions not applied

The provisions of the tender document are to be fully observed. Adequate internal controls are to be implemented to ensure an economic and efficient service.

Provision of Staff Meals

Procurement is to be adequately monitored such that the necessary arrangements to issue new tenders are planned well in advance and to ascertain adherence to standing procurement regulations for transparency and fair competition. Additionally, Management is to ensure that the necessary formal agreements with contractors are drawn up accordingly.

Provision of Internal Security Services

Extensions to Contract hindering Fair Competition

The limit, be it by period or amount, up to when contracts may be extended, is to be strictly in line with the original call for tender, following which, as per best practice, a fresh call is to be issued. This will enhance transparency and support a fair competition amongst prospective bidders.

Substantial Additional Security Hours not approved by the General Contracts Committee

All procurement is to be made in accordance with the prevailing regulations. Thus, appropriate approvals are to be invariably obtained prior to entering into any commitments.

The attention of Management is to be drawn to Article 25 of the Fiscal Responsibility Act which provides for disciplinary action against the responsible officers when procurement is not appropriately authorised.

Control Issues

Cleaning Services at Sir Paul Boffa Hospital

Management is to conduct adequate control and monitoring over third party contracts. Invoices are to be processed for payment only if the relevant supporting documentation is duly signed as required and confirmed by a responsible officer from SPBH or SAMOC, as applicable.

Cleaning Services at Mater Dei Hospital and Sir Anthony Mamo Oncology Centre

The relevant formal agreement is to be duly signed prior to the commencement of services.

Software System Maintenance Agreement not formally renewed

In order to enhance controls, it is important to monitor the provisions stipulated in a contract and draw up the relevant agreement for legal backing. Any renewal notices are to be endorsed by both parties.

Care Worker Services

Letter of Acceptance not in line with Finance Approval

Fairness and transparency are to be ascertained throughout the procurement process. Letters of acceptance are to be properly verified to ensure that they are in line with the approval from the relevant authorities.

Services not covered by Agreement and necessary Approvals

As reiterated, for proper internal control, SAMOC is to ensure that the necessary approval is in place before proceeding with the respective procurement. Subcontracted services are also to be backed up by a formal agreement.

Performance Guarantee

The appropriate management of contracts requires monitoring, such that the contractor's attention is drawn and corrective action is taken in the event of non-compliance. Strict adherence to the requirements laid down by DC is recommended; thus, a copy of a valid bank guarantee is to be duly provided and filed accordingly.

Timesheets, Attendance Verification and Adjustments to Invoices

Management is duty bound to ensure that the interest of Government is safeguarded, especially given that substantial amounts are being disbursed from the taxpayers' money on such services. Thus, any clauses included in the contracts are to be fully observed to avoid undue expenditure.

Change in Staff Lunch Composition not reflected in a Change in Price

Without prejudice to the method of procurement, in the event of future similar circumstances, one would expect SAMOC to negotiate a lower price in order to ensure that value for money is obtained. Documentation in this respect is to be filed for future reference and audit purposes.

Entitlement to Staff Meals

The distribution of meals to staff falling short of the established requirements is considered as unauthorised. Thus, Management is to ascertain that established policies are invariably adhered to in order to prevent discrimination between employees and to avoid antagonism in the working environment.

Provision of Internal Security Services

Insufficient Compliance Checking

Obtaining specific documentation enhances monitoring and control. Thus, it is advisable that the foregoing are requested randomly on a regular basis.

Provision of Information Technology Services

Contracts are to be formalised, signed and filed for ease of reference, as well as for audit purposes. Furthermore, before effecting payments, the responsible officer is expected to ensure that the respective invoices were duly checked and endorsed accordingly.

Compliance Issues

List of Signatories not provided

Authorised signatories should be formally documented, as well as approved and filed accordingly for future reference. Additionally, the responsible officer is to make sure that payment vouchers are duly endorsed.

Publication of Awarded Direct Orders and Variation to Tender not confirmed

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

Payments to VAT Registered Service Provider bypassing the Purchases Ledger

Control over creditors, as well as over the respective VAT payable, is easily lost if purchases transactions bypass the proper ledger. Multi-payments are to be used only for payments that do not include a VAT element. The VAT numbers of all registered suppliers for goods and/or services are to be invariably shown on the payment voucher. This will serve as audit trail to assist the VAT Department in ensuring the collection of the respective indirect tax.

Non-compliance with VAT Legislation

Officers in charge are to ensure that they are furnished with a proper fiscal document meeting the criteria set out in the VAT Act for every payment. All receipts are to be kept in the relevant file to support the relevant payments.

Shortcomings in Inventory Management

For effective controls over the tracking and valuation of fixed assets, SAMOC is to maintain an updated inventory database and ensure that the information is accurate and complete. An officer entrusted with the responsibility of inventory management is also expected to perform periodical physical reconciliations. To this effect, Management is to be guided by the Inventory Control Regulations established in MF Circular No. 14/99.

Management Comments

Management concurred with the majority of the highlighted observations, as well as with the proposed recommendations, and submitted the feedback reproduced below:

Lack of Internal Control

This is a common situation across the Ministry for Health where due to the constant delay in publication of the tenders, which is not under the control of CPSU, the contracting authority has no option other than resorting to negotiated procedures or extensions to gap-fill. We are in discussion with the Contracts Department to hasten procedures.

Patients' Catering Services

Contract Extension Ambiguity

During the year 2013, MDH requested the contractor to provide additional equipment to cater for new wards in the Hospital. The contractor argued that contractually he was only bound to provide equipment for those wards indicated in the original contract. Further to discussions, it was agreed that the contractor is to provide the additional equipment at its own expense required to cater for patients' meals in the new Wards, subject to the contract being extended further for a period of 10 years to enable the contractor to cover the additional investment required.

Scope of the Agreement not Comprehensive

a. *Although Addendum 1 was signed on the 19 October 2015, the Ministry through FMS[8] (as original signatory to the contract) had made a formal request for approval with DC in March 2015*.

b. *The Dermatology Department falls under the responsibility of SAMOC even though still stationed at SPBH*.

c. *The Long Term Care Patients are Mater Dei Hospital patients transferred to the Unit set up at SPBH*.

Late Undertaking of Insurance Policy

Subsequent to the auditors' report a centralised system was implemented. More rigorous controls were set in place in order to ensure timely action.

Lacking Controls hampering the Verification of Invoices

Action is being taken with MDH IT Department to include a programme for the registering of patients' meals orders within Clinical Patients Administration System, so that the Hospital will be in a position to monitor adequately the meals ordered by patients. At the time of writing, our IT department has submitted their requirement with the respective developer and is currently holding discussions with this service-provider. This item is included in list of proposed changes to be performed for year June 2016 - June 2017 by the system developer. No time frames are available yet, since the system developer has to provide a time schedule of such changes. In the interim, the supplier was requested to attach the individual patient orders with the monthly invoice to perform random checking.

SAMOC will be implementing controls, which are already in place at MDH, such that a reconciliation between the number of inpatient meals and the number of beds occupied by patients is carried out regularly.

Agreement Provisions not applied

Although the snack boxes' option is not included in the Menus distributed to the patients, these are included in the Order Sheets used by the wards. It is worth mentioning however, that patients almost invariably prefer a full meal rather than a snack.

[8] FMS – Foundation for Medical Services.

Provision of Staff Meals

Formal Extensions not available

This was a departmental tender issued by CPSU when SPBH was still operational. A DC tender was issued for catering services at SAMOC, which included the said Staff Meals. However, no submission was received and when CPSU asked for new specifications to re-issue, we were informed of a problem regarding the approval from the Environmental Health Department. This issue is still pending and SAMOC is still relying on a contract which has been expired long time ago, originally intended for SPBH.

Procurement not in line with Standing Regulations

In this case, the tender process was stalled due to infrastructural issues which affected Health and Safety and Commercial Regulations.

Provision of Internal Security Services

Extensions to Contract hindering Fair Competition

This is a common situation across MFH[9] where due to the constant delay in publication of the tenders, which are not under the control of CPSU, the contracting authority has no option other than resorting to negotiated procedures or extensions to gap-fill. We are in discussion with the Contracts Department to hasten procedures.

Substantial Additional Security Hours not approved by the General Contracts Committee

CPSU was informed retrospectively on this hefty increase in hours. Management confirms that a case was made to the GCC, however this was refused on the basis that it was retrospective. FMS justified the fact that security had to increase at project stage as new equipment worth millions of euros was being installed in tandem with other project works.

Cleaning Services at Sir Paul Boffa Hospital

The auditors' recommendations are well-noted. We will ensure that the cleaners follow our set procedures through regular testing.

Cleaning Services at Mater Dei Hospital and Sir Anthony Mamo Oncology Centre

Department is still awaiting the definite approval from the GCC. This is a common situation throughout all the service agreements.

Software System Maintenance Agreement not formally renewed

All systems software in the various entities within the Ministry of Health are to be negotiated centrally through the Information Management Unit. In the interim, measures are being taken to extend the contract.

[9] MFH – Ministry for Health.

Care Worker Services

Letter of Acceptance not in line with Finance Approval

Reference was made to CT2399/08 and CT2080/11 since the new negotiated contract was based on the technical specifications of such former agreements.

Letter of Acceptance 268/2015 refers to CT 2399/08 and CT 2080/11 only insofar as the technical specifications of the care workers' services which remained the same under such extension. Although the original contract did not include SPBH, the approval granted by DC in respect of Letter of Acceptance 268/2015 was to cover the care workers' hours for SPBH and SAMOC. Extension of the current contract is being requested until a new call for tenders is issued. The tender dossier has been forwarded to DC for approval, however, no such approval has been forthcoming yet.

Services not covered by Agreement and necessary Approvals

Approval for extension of contract up to 31 December 2016 was sought from DC. This was subject to clearance from DIER[10] as the rate charged had to be pegged with public service scales. Following DIER clearance, extension is being requested since the tender dossier is being vetted through DC and should be published in a few weeks time.

Performance Guarantee

Subsequent to the auditors' report a centralised system was implemented. More rigorous controls were set in place in order to ensure timely action.

Timesheets, Attendance Verification and Adjustments to Invoices

It is confirmed that the contractor had informed the Hospital that it intended to install the attendance verification equipment, but MDH management decided to issue a call for tender for the installation of such equipment, in order to have more control over the attendance of contractors' personnel.

Change in Staff Lunch Composition not reflected in a Change in Price

Issue is still pending as case to DC being drafted and Contracts MDH negotiating a favourable agreement. The latter will draft a case for MFIN authorisation.

Entitlement to Staff Meals

Action is being taken to issue separate meals' cards to all entitled staff, which will be related to the payroll system, in particular to staff rosters, in order to have proper monitoring and control of staff meals. Our service-provider issued a proposal and advices that this system will be implemented two to three months following our acceptance of the proposal. We are awaiting an amendment to the proposal which would indicate cost.

[10] DIER – Department for Industrial and Employment Relations.

Provision of Internal Security Services

Insufficient Compliance Checking

The process of random checking of payslips issued to the contractors' personnel will be resumed.

Provision of Information Technology Services

Agreed and this was communicated to Management in order to ascertain compliance. The Auditors' recommendations are noted. We will initiate procedures to ensure that all the invoices appertaining to professional services are duly endorsed by the responsible officer.

List of Signatories not provided

The Auditors' recommendations are noted. We will update our records accordingly.

Subsequent to the auditors' observations during their visit to our premises, systems were put into place to ensure that the Financial Controller duly endorses all payment vouchers.

Publication of Awarded Direct Orders and Variation to Tender not confirmed

Data is now being collected centrally and direct orders/variations are being published in the Government Gazette every six months as per Public Procurement Regulations.

Payments to VAT Registered Service Provider bypassing the Purchases Ledger

Subsequent to the auditors' observations during their fieldwork, payment of these invoices is being settled through the purchases ledger.

Non-compliance with VAT Legislation

The Auditors' recommendations are noted. We will initiate procedures to ensure that all the suppliers whose invoices are not compliant with the VAT Act are to send a separate fiscal receipt.

Shortcomings in Inventory Management

Inventory Management is one of our topmost priorities. We anticipate that our shortage of staff in the accounts section will be addressed in the very near future. Subsequently, a member of the accounts team will be identified to manage our Fixed Assets accordingly.

Ministry for the Family and Social Solidarity

Department of Social Security

Invalidity Pensions

Background

The Department of Social Security (DSS) within the Ministry for the Family and Social Solidarity (MFSS) is responsible for the implementation and execution of the provisions of the Social Security Act, 1987 (Cap. 318) (SSA), with particular reference to Article 26 of the said Act.

The Department's main operations, amongst others, are to assess, pay and provide information on social security benefits, and encourage individuals and organisations to be aware of, and to comply with, their obligations under social security legislation.

Social benefits in Malta are classified into the contributory and non-contributory schemes, with the former depending on the amount of National Insurance contributions made during one's lifetime, to provide for oneself when a later contingency such as sickness, unemployment or retirement occurs.

This audit focused solely on Invalidity Pensions[1] (IP) falling under contributory benefits. A person who is certified by the Medical Panel (appointed by law) as being incapable for suitable full-time or regular part-time employment, or self-occupation, due to a serious disease or bodily or mental impairment, is entitled to IP, subject to the relative contribution conditions[2]. Eligible persons must be incapable for work for at least six months prior to their claim, and in continuous employment or registering for work under Part 1 with the Employment and Training Corporation for at least one year.

Weekly IP rates are established as *per* Legal Notices issued by the Minister, following the implementation of the annual budget measures. Applicable rates are categorised according to the average annual contribution and the marital status of the respective beneficiary. The National Audit Office (NAO) feels it pertinent to note that in the case of female applicants, IP is paid at 'single rate', irrespective of their marital status.

[1] Invalidity Pensions also incorporate the following: National Minimum Invalidity Pension, Increased Invalidity Pension, Decreased National Minimum Invalidity Pension and National Minimum Pension.

[2] A contributory IP is awarded to any person having paid at least 250 contributions, and paid or credited at least an average of 20 contributions *per* year from the age of 19 or 18, as the case may be (or 1964/65 whichever occurs first), till the date of the claim.

Appeals

Cap. 318 permits the claimant to appeal any decision taken by the Medical Panel with respect to IP. Appeals were introduced in 2010 and an additional Umpire[3] was appointed specifically for appeals on IP medical decisions.

Appeals can be heard before the Umpire and the Multi-Disciplinary Board, but not concurrently. It is at the discretion of the applicant to choose whether his/her appeal is to be filed with one or the other. Any outcome from decisions taken by either, can be superseded by filing another appeal at the applicant's choice.

Departmental Reform

Prior to the reform that the Department undertook in 2007, a number of beneficiaries were awarded IP on a permanent basis, without prompting further re-assessments of the cases in question. Following the necessary amendments in SSA and the Department's policies and procedures, IP started to be awarded for periods not exceeding three years, followed by a re-assessment by the Medical Panel within MFSS to confirm eligibility[4]. Additionally, claimants had to be registering for work for at least one year, whilst Impairment Tables and criteria were introduced for the Medical Board to re-assess eligibility of the cases.

Financial Information

The Financial Estimates for Vote 41 – Social Security Benefits show that a total of €662,100,000 were originally estimated to be issued as contributory benefits for the year under review, €23 million of which were allocated for IP. Hereafter is a breakdown of the former amount:

Table 1: Contributory Benefits

Type of benefit	Estimated amount for 2015
	€
Invalidity Pensions	23,000,000
Retirement Pensions	441,000,000
Bonus	65,500,000
Widows' Pensions	119,000,000
Short-term Benefits	13,600,000
Total	**662,100,000**

The total amount of IP paid to beneficiaries during 2015, as provided by the Department, totalled €24,353,372, representing an increase of approximately six *per cent* over the original budget[5]. Up to the time of writing of this Report, DSS had not yet forwarded evidence of the amount provided against an extract from the Departmental Accounting System (DAS).

[3] The Board of Appeal is made up of an Umpire (being a legal person selected by the Office of the Umpire) and a medical person representing the Medical Panel, with the latter not being involved in the case being heard.

[4] In cases where IP was awarded on a permanent basis (prior to 2007), MFSS was instructed to re-assess only those cases where claimants did not exceed 45 years of age at the time the reform was introduced. Those who exceeded this threshold were not bound to be re-assessed by the Department. This was a policy imposed on the Department and to which MFSS adhered to.

[5] NAO noted a difference between the above-quoted figure and the amount reported in the Social Assistance and Benefits System (SABS), the latter amounting to €24,415,316. According to DSS, "*Discrepancies between SABS and DAS are a result of the fact that whereas SABS records the assessment process of benefits up to the date of issue of benefits due, DAS records the encashment of such benefits.*"

Audit Scope and Methodology

The main scope of the audit was to determine the level of existing internal controls over the payment of IP under contributory benefits. The audit also aimed to ascertain that such contributions to beneficiaries were made in an accurate, correct and timely manner, in accordance with the provisions laid out in SSA.

A total of 4,544 beneficiaries were in receipt of IP during 2015. A sample of 40 cases was selected for testing and related documentation was analysed to assess whether the procedures surrounding the application and payment were being correctly followed. Additionally, information from SABS was extracted in relation to all the payments made to the selected beneficiaries during 2015. NAO also tested the accuracy and correctness of such payments, including any arrears paid to these beneficiaries.

Furthermore, NAO noted that during the year under review, a total of 167 appeals were before the Office of the Umpire, thus excluding Multi-Disciplinary Board, for a decision to be taken accordingly, half of which were brought forward from previous years. Of these, 78 appeals were settled by the former, with an additional 10 withdrawn by the appellant.

Control Issues

Payment of Invalidity Pension in Excess

A claimant first applied for IP in 1996. The National Minimum Invalidity Pension (NMIP) was granted ever since, with the last re-assessment by the Medical Panel being held in 2014, during which the beneficiary was again granted NMIP for three consecutive years. NAO noted that in 2001, the claimant was in receipt of NMIP. In the meantime, the claimant's wife was also receiving NMIP with effect from the same year, as confirmed with SABS.

Testing revealed that €2,504 was paid in excess to the claimant, as a result of incorrect NMIP rate paid to the beneficiary from May 2012 till November 2014. This amount paid in excess cannot be recouped by the Department in full, based on Article 102(1)(ii) of SSA, which states that in the case of an overpayment which is not the result of the non-disclosure or misrepresentation of a material fact "... *the Director shall have no right to effect any such deductions … in respect of overpayments which have been made prior to the period of two years going back from the date when the Director became aware of such overpayment irrespective of the period to which the overpayment refers* ...". To this effect, DSS can only recover the amount of €694 from the beneficiary, implying that the Department will have to forgo the sum of €1,810 in public funds that were paid erroneously to the claimant.

Lack of Periodical Re-assessment of Cases

a. Incorrect Rate awarded to Claimant

NMIP was awarded to a claimant as from mid-June 1992, and since then, the case continued to be reviewed for eligibility throughout the years by the Medical Panel within MFSS.

Audit testing revealed that between 2012 and 2014, the claimant was awarded NMIP at the same weekly rate. It transpired that the Department did not take into account the cost-of-living increase as stipulated in Article 90A of SSA. This resulted in an underpayment of €425 pertaining to the years covering 2013 till 2015, after adjusting the weekly rate.

Upon further enquiry, it transpired that the case in question was not being re-assessed annually (either automatically through SABS or manually) to adjust for the service pension awarded to the same claimant. The service pension in question had to be re-assessed and eventually decreased by a fixed

amount as stipulated in SSA, until it was fully absorbed, resulting in full NMIP being paid to the claimant. This departmental error resulted in an underpayment of NMIP, dating back from 1998. Immediate communication with DSS officials led to a recalculation of the amount due to the beneficiary, which for the period 1998 up till 2016 amounted to €21,455. DSS provided NAO with supporting documentation in connection with the relative pension re-assessments. Meanwhile, DSS also stated that as from January 2016, the relative service pension was absorbed and NMIP was awarded as *per* current year rates.

b. Claimant not Re-assessed for Eligibility

An individual applied for IP in 2003. The Medical Panel within MFSS assessed the case in question and, at that time, awarded benefits for a period of at least three years. Between November 2006 and December 2011, no form of documentation was traced in file in relation to IP awarded to the claimant. Minutes in file evidenced that it was brought up for review in November 2005, whilst no further action was recorded until December 2011.

Upon enquiry with DSS, NAO was informed that during the period 2006 – 2011, the re-assessment due date was not captured in SABS, thus IP continued to be awarded without having a re-assessment of the case in question. This resulted in a total amount of €17,870, which was paid to the beneficiary during the above-mentioned period, when no review of the case was carried out. Meanwhile, the claimant submitted a fresh application in December 2011 and re-assessments of the case were conducted accordingly to-date.

Recoupment of Arrears following Payments to Beneficiary

In a separate case, it was observed that an individual first applied to receive IP in February 2013. The Medical Panel rejected the claim in March 2013, whilst in August of the same year, the applicant appeared before the Multi-Disciplinary Board for reconsideration of the case. Yet again, the claimant was not found eligible for IP, but after filing an appeal before the Umpire, this was eventually considered in favour of the beneficiary in 2014.

Payment of IP in arrears due to the claimant, for the period 2013 to 2015, totalling €11,109, was made in January 2015. Prior to this, an overpayment of €1,140 for Social Assistance paid to the beneficiary in relation to the period October – December 2014, which was created in December 2014, was set off against IP arrears due.

Another overpayment of €7,324, relating to Sickness Benefits which were paid to the beneficiary for the period 2013 – 2014, was created in SABS in February 2015. However, this was not fully recouped by the Department, as the date when such overpayment was created (*i.e.* February) was in effect after the date when the arrears due to the beneficiary were awarded (*i.e.* January). In fact, it transpired that the rate of recoupment was set at 10%.

Recommendations

Control Issues

Payment of Invalidity Pension in Excess

NAO recommends that a periodical review of personal files, especially those pertaining to claimants benefitting from a married rate, is carried out to ensure that any errors are detected as early as possible. Corrective action is to be taken in a timely manner, thus safeguarding the proper use of public funds.

Lack of Periodical Re-assessment of Cases

The Department is to conduct a periodic re-assessment of cases, which is to include those beneficiaries receiving a service pension and IP simultaneously. Moreover, the Department is to recheck in SABS those cases having IP awarded on a permanent basis, to reconfirm their status. In case of errors, immediate corrective measures are to be considered.

Recoupment of Arrears following Payments to Beneficiary

Proper checking is to be carried out prior to issuing IP arrears payments from one Section within DSS, whilst having another Section gradually recouping amounts overpaid. This can be achieved if all sections within DSS liaise with each other.

Management Comments

In its reply, Management concurred with most of the observations and recommendations put forward, whilst expressing appreciation for the work carried out by NAO. The Department also decided to introduce periodical sample checks on individual files to perform review and re-assessment of cases, whilst taking into consideration the limitation on human resources within DSS. Furthermore, in-house training is envisaged for assessors and checkers in order to reduce the risk of error.

The following comments were also forwarded:

Payment of Invalidity Pension in Excess

The beneficiary referred to was paid IP at the single rate with effect from February 2001 when his spouse was awarded IP in her own right. This rate was effective until the date when IP of the spouse was suspended and the husband's rate was accordingly adjusted to a married rate. When IP of the spouse was re-instated in May 2012, the IP rate of the husband remained unchanged, thus creating an overpayment to the beneficiary of €2,504 covering the period May 2012 to November 2014. The net amount that may be recouped within the last 104 weeks from when DSS was aware of same overpayment is €694. NAO was informed that arrears due from single to married rate of €129 were withheld to make good for part of this overpayment.

In this particular case, the standard procedure whereby both files (of the husband and wife) had to be presented and examined together, was not observed. Being unaware, the assessor was not in a position to correctly adjust the payable rates.

Lack of Periodical Re-assessment of Cases

a. Incorrect Rate awarded to Claimant

The Department stated that the case in question was not automatically reviewed by the re-assessment process, which is carried out yearly to award budget increases. Such cases are usually flagged in an error report and assessed manually. For some unknown reason, but likely due to data transfer from the previous system to SABS, this case was never highlighted.

b. Claimant not Re-assessed for Eligibility

Management stated that this was a genuine human error made by the assessor, who in 2005 reviewed the IP rate, but failed to insert the IP expiry date. As a result, IP continued to be paid and was only detected through an exercise carried out in connection with cases that were awarded IP for life.

Recoupment of Arrears following Payments to Beneficiary

Again, DSS cited this issue as another case of human error, rather than lack of communication, where overpayments on Sickness Benefits and Social Assistance were involved. Management confirmed that "... *The standard procedure is that as soon as an IP is authorised, an SB overpayment is created by the same checker authorising IP so that the resulting overpayment would be fully recovered from any due IP arrears*. ... *In the case in question there were several SB claims, but although such an overpayment was not automatically assessed by SABS, the system prompts checker that overpayment should be manually assessed*."

Elderly and Community Care Department

Personal Emoluments

Background

The Elderly and Community Care Department (ECCD), falling within the Ministry for the Family and Social Solidarity (MFSS), had a budget allocation of €4,622,000 for 2015 in respect of Personal Emoluments within Cost Centre 01, Finance and Administration. The majority of this budget was initially allocated to salaries and wages, as well as social security contributions, with €4,000,000 and €377,000 respectively.

Information obtained from ECCD, through the Payroll System, showed that payments effected throughout 2015 amounted to €3,814,563[1] and pertained to 322 employees[2]. The majority of this amount, totalling €3,345,578, related to salaries and wages, whilst a further €212,593 was paid on allowances.

Audit Scope and Methodology

The scope of the audit was to ensure that personal emoluments for 2015 were appropriately recorded and processed according to the Public Service Management Code (PSMC) and other pertinent circulars. The adequacy of internal controls, intended to ensure accuracy and validity of salary payments, was also reviewed.

Table 1: Cost Centre 01 – Personal Emoluments 2015

	Number of employees	Gross salaries[3]	Allowances
		€	€
Head Office	90	1,363,246	140,837
Social Assistants (SAs) in the Community	124	1,150,124	14,386
Day Centres	92	992,518	4,810
Servizz Anzjan	16	308,675	52,560
Totals	**322**	**3,814,563**	**212,593**

[1] Reports extracted from the Departmental Accounting System showed a net payment figure of €7,436,098. Up to the writing of this Report, ECCD did not provide a satisfactory explanation with respect to the discrepancy between this amount and the total paid as shown in the Payroll System (€3,814,563).

[2] The total number of employees falling under Cost Centre 01 and the respective 2015 gross salaries and allowances, are shown in *Table 1*.

[3] The figure for gross salaries is inclusive of allowances.

A total of 31 officers, who in aggregate received total gross salaries of €636,280 in 2015, were selected for audit purposes, representing 17% of total emoluments. These individuals were also the recipients of €179,922 in allowances, which account for 85% of the total allowances paid during 2015. This sample encompassed officers in different grades and of different job descriptions, such as General Practitioners (GPs), Nurses, SAs and Clerks, amongst others.

As part of audit testing, the basic pay and allowances were checked for accuracy and validity, and vouched against the Public Service Collective Agreement signed in 2012, and other relevant supporting documentation. Particularly, allowances earned by Nurses and GPs were vouched against the Collective Agreement between the Government and the Medical Association of Malta, and the Sectoral Agreement related to Nurses and Midwives.

Furthermore, recalculations were performed in order to determine the amount that the selected GPs were entitled to, over and above their basic salary. In view of the material differences ranging from €8,800 to €11,000 encountered when recalculating these amounts for 2015, testing was extended to also include the first four salaries paid during 2016, *i.e.* up to the date of audit testing.

Enquiries in relation to these allowances were also carried out with officials outside of ECCD. Specifically, follow-ups in relation to the Extra Duty Allowance (EDA) earned by GPs for extra duties carried out at St. Vincent de Paul Residence (SVPR) were conducted with an official within the said institution, who was in charge of the calculation of these allowances before their eventual payment from ECCD.

The National Audit Office (NAO) also analysed overtime performed by five officers from the selected sample, which in total costed €7,827.

An assessment of the timekeeping procedures, including the recording of working hours and absences, was carried out by verifying timesheets for the month of July 2015, which were obtained for all the officers selected in the audit sample. The relevant Vacation Leave (VL) and Sick Leave records were obtained as a means of corroborating the information on the respective timesheets.

Key Issues

Inaccuracies in Allowances paid to General Practitioners

A vacancy for the post of GP within MFSS, with a salary equivalent to the third step of Salary Scale six, amounting to €23,461, was issued in mid-July 2014. The appointee was required to work in accordance with an established working schedule and had to choose between contract A and contract B[4]. Both GPs selected for testing purposes were appointed as a result of this call and chose to work under the contract A conditions. To this effect, they entered into an agreement with ECCD as from March 2015.

The working week of GPs under contract A is that of 12 sessions, of which 10 are on-site, whilst the remaining two are off-site. Each session has a timetable value of four hours, thus each working week consists of 48 hours[5]. A minimum rate of €90 applies to sessions held before 16:00, however different rates may apply depending on the day and time when the session is held. Additionally, both GPs were also contractually bound to work an extra session of four hours *per* week, increasing their weekly hours to 52[6].

These GPs also worked a number of extra hours at SVPR, for which they were paid an EDA, usually relating to night shifts in between their normal session hours. Calculation for amounts due in relation to these hours was being handled by an SVPR official.

[4] The main difference between these two types of contracts is that GPs under contract A are precluded from undertaking any private practice, and therefore, their salary is higher than that paid to GPs choosing contract B.

[5] The basic working week consists of 40 hours, whilst off-site sessions account for the remaining eight hours.

[6] Given these conditions, this particular GP contract will be referred to as 'Job Plan A+1'.

NAO recalculated the gross salary ('Job Plan A+1' allowance, extra sessions and EDA) due to both GPs for the period March 2015 to April 2016. Testing revealed that they were overpaid the respective amounts of €14,089 and €13,344. Discrepancies emanated because of the following:

a. Wrong Choice of 'Job Plan A+1' in the Payroll Software

A breakdown of allowances requested for testing purposes revealed that GPs were receiving a 'Job Plan A+1' allowance at a rate of €3,552 with every four-weekly salary during 2015, and €3,697 during 2016.

These amounts could not be readily backed up by supporting documentation. In fact, it was only after various discussions with ECCD officials that it transpired that such allowances were not intended to be paid to GPs working on 'Job Plan A+1'. It was further confirmed that this error emanated from an incorrect selection on the Payroll System when these employees' data was originally being inputted back in 2015. The correct amounts *per* pay should in fact have been those of €2,464 and €2,367 in 2015 and 2016 respectively, which resulted in overpayments of €1,088 *per* pay in 2015 and of €1,330 *per* pay in 2016.

b. Erroneous Rates in relation to 'Job Plan A+1' Extra Sessions

The total extra session hours worked during 2015 at SVPR, were not paid at the relevant session rate but were remunerated at the applicable EDA rates, depending on when the session was held. EDA rates were calculated as a multiple of the basic hourly rate, and amounted to €11.60 in 2015 and €12.21 in 2016. Thus, the rate at which the GPs were paid was always considerably lower than the session rates, which at their minimum amounted to €22.50[7]. Consequently, such erroneous rates resulted in underpayments regarding 'Job Plan A+1' extra sessions.

Following discussions with ECCD officials, it transpired that payments for such extra sessions should in fact have been remunerated at the applicable session rates.

c. Errors in the Calculation of the Extra Duty Allowance

Workings in relation to the EDA were also obtained by NAO and assessed as part of the testing procedures.

i. It was noted that whenever a GP did not work on a Public Holiday (PH), the time that would have been worked during that day, *i.e.* seven or five hours[8], would be deducted from the weekly hours. It transpired that a top-up of five hours and 45 minutes was being added instead, which was effectively reducing the working week below the normal hours of work.

As a result, part of the extra hours worked during any such week were not being remunerated and were partially reducing the amounts due to GPs.

Following discussions with ECCD officials, it was ascertained that although GPs are not on duty on most PHs, they should still be paid for the sessions falling on these days at the normal session rates. Thus, the PH top-up is no longer necessary.

ii. Testing further revealed that information in relation to GP attendance was located in two different places. The basic working week timesheets were physically held at ECCD, whilst the timesheets relating to extra duties carried out at SVPR were only being held within the said institution.

[7] Sessions held before 16:00 are remunerated at the lowest rate of €90 for every four hours, *i.e.* €22.50.

[8] General Practitioners worked seven hours from Monday to Friday (08:00 – 15:00) and five hours on Saturday (08:00 – 13:00).

This, coupled with the fact that EDA workings were being conducted at SVPR and solely transferred to ECCD for payment purposes, denotes a lack of control from the Department on the amounts due to GPs in relation to the extra duties they performed during the period under review. In fact, NAO did not trace any form of controls or recalculations on these amounts before payment was made. SVPR workings were taken at face value and paid without further questioning.

iii. NAO calculations also revealed that one of the GPs selected for testing was not paid the amount of €1,096 relating to the EDA covering the period June to August 2015. This further reinforces the issue relating to the lack of apparent checks and controls from ECCD.

Employee simultaneously working with two Government Departments

In her application form to work on a reduced timetable of 35 hours *per* week, an SA who started her employment with ECCD in November 2010, cited her age and the state of her physical health as the reasons for her request. Moreover, as part of the reduced hours renewal process, she also provided ECCD with letters from her family doctor, declaring that health problems precluded her from carrying out duties for a full 40 hours.

a. Simultaneous Employment with two Government Departments

Testing revealed that, throughout 2015, the said SA was simultaneously working with two Government Departments.

NAO established that, in addition to her employment with ECCD, she was also working up to a maximum of 25 hours *per* week at the Education Department. ECCD stated that there is no record of the commencement of employment with the Ministry of Education and Employment in her personal file. However, NAO was later informed that she commenced her duties with the Education Department in January 2008.

Having additional employment when already working on a reduced timetable at ECCD, goes against the principle of this family-friendly measure. In line with PSMC requirements, although this SA was granted such work arrangements on medical grounds, in reality she was not only able to give a full day's work with ECCD, but was in total working up to a maximum of 60 hours *per* week.

Following discussions by NAO with pertinent officials, a letter was sent to this employee informing her that since she was making use of family-friendly measures, it was not possible for her to have an additional job. Consequently, the Department disclosed that the SA decided to revert to full-time employment with ECCD and to work 15.25 hours *per* week at the Education Department.

b. Non-deduction of Social Security Contributions

Additionally, audit testing revealed that whilst this SA's ECCD salary was correctly accounted for, the salary received from the Education Department was being included in ECCD's payroll records as an allowance. Consequently, since Social Security Contributions are calculated as a percentage of basic pay, in this case, no such contributions were deducted on the income earned from such Department for the period under review.

c. Government Bonuses exceeding Maximum Yearly Entitlement

NAO also traced Transfer Schedules of Payment, whereby funds were being transferred from the Education Department to ECCD. Included within these transfers were the basic salary, as well as Government bonuses.

Due to lack of adequate systems to capture such instances, this SA received *pro rata* Government bonuses from both Departments, with the result that she exceeded the annual maximum entitlement of €512.

In fact, NAO confirmed that during 2015, bonuses of €264 were received from the Education Department, and a further €448 from ECCD, totalling €712.

Erroneous Retardation of Increments

Two individuals selected for testing purposes were promoted to Senior Nursing Managers with a Salary Scale six starting at €21,649, with effect from February 2013. In both instances, these individuals were previously occupying the post of Departmental Nursing Manager, and their salary had reached the maximum of Salary Scale seven, at €23,422.

Since the salary before promotion was higher than the minimum salary applicable for the new scale, in line with Section 2.2.1.2 of PSMC, "*... they are to carry their previous salary to the new grade or position, and if resulting out of step, be placed on the next higher step with the consequent retardation or advancement of incremental date ...*".

Upon promotion, both Senior Nursing Managers were placed on step four of Salary Scale six, with a resulting salary of €23,438, which was higher than their closing salary before promotion.

Following recalculation by NAO, it resulted that the next increment, which is normally given after one year of promotion and in line with the provisions of Section 2.3.2 of PSMC, had to be delayed by 10 days. This means that the resulting increase in salary step in line with PSMC provisions, was to take place on 1 April of the year 2014 and subsequent years. However, this was not the case since increments were granted in October 2014 and 2015.

It transpired that the Gozo Salaries Department was responsible for such salary adjustments, and following enquiry by NAO, it was confirmed that this delay in the incremental date was done in error. To this effect, arrears for 2015, amounting to €388 and €392 were due to these individuals.

Control Issues

Lunch Breaks not being deducted from Public Holiday Allowances

Subsidiary Legislation 452.87 – 'Organisation of Working Time Regulations' states that every worker should be entitled to a break for at least an uninterrupted period of 15 minutes, in those cases where the working day is longer than six hours.

However, testing revealed that a Senior Nursing Manager and a Chief Nursing Manager were registering 11-hour shifts on their 2015 timesheets, without giving an indication of whether they availed themselves of a lunch break. This data was then used as the basis to calculate PH allowances. NAO noted that lunch breaks were not being deducted from the number of hours worked during PHs. Therefore, payments were being made with respect to the entire 11-hour shifts. Considering a 15-minute deduction *per* shift worked during PHs, the Department incurred an extra cost during 2015.

Shortcomings in relation to Timekeeping

Eight timesheets pertaining to SAs were not endorsed by an authorising officer, whilst four additional timesheets were duly signed but not stamped, giving no evidence of who signed the document. In another instance, the selected officer did not indicate the 'time out' on the timesheet, however it was still endorsed by an authorising officer.

Seventeen VL applications pertaining to 12 individuals did not have the necessary approvals from their Section's authorising officer, even though the majority of applications had their recommender's signature.

Compliance Issues

Inadequate Overtime Approvals

Lack of Permanent Secretary Approval

NAO noted that no approvals were granted by the Ministry's Permanent Secretary for overtime conducted by sampled individuals during 2015. This goes against the provisions of Section 3.2.1.2 of PSMC, which states that any overtime conducted in a particular Department has to be approved by the respective Permanent Secretary in advance, for periods not exceeding three months. Correspondence from ECCD confirmed that up till December 2015, no approval was obtained prior to the performance of overtime.

The Department's officials further maintained that such an approval was still not in place for the months of January to March 2016. Moreover, whilst overtime approvals have been requested for the quarter starting April 2016, such documentation was not made available to ECCD, and could therefore not be presented to NAO.

Backdated Approvals for Overtime by Head of Department

'Request for Overtime Work' forms were traced in relation to all overtime assessed during the audit. Whilst all forms were correctly supported by a timesheet and duly approved, such requests were always made after the overtime was conducted. By inference, the relative approvals were also obtained retroactively.

Recommendations

Key Issues

Inaccuracies in Allowances paid to General Practitioners

It was satisfactorily noted that ECCD has already fully collaborated with NAO to ensure that the full amount due from the mentioned GPs was duly recalculated.

The Department could consider introducing new procedures to ensure that controls over the payment of personal emoluments are in place. Management might use a system of periodical exception reporting, whereby figures such as unusually high or low payments, amongst others, are assessed and investigated. This would ensure that any issues are tackled immediately and that any errors do not spill over a large number of salary payments. By so doing, the Department would be ensuring that any overpayments or underpayments are kept at the minimum amounts possible. A record of these checks should be kept for future reference.

Furthermore, it is recommended that ECCD is in possession of the full details of the attendance at SVPR of said GPs. This would ensure that proper checks can be carried out before the amounts due to them, especially in relation to the EDA, are disbursed.

Employee simultaneously working with two Government Departments

In the eventuality that employees working within Government Departments have another employment, there should be a formal understanding between the two Departments about the employees' conditions of work and salary arrangements.

It is also recommended that the Department ensures that the Central Salaries Section is informed of this SA's situation, *i.e.* that she is working with two different Government Departments, hence practically engaged by the same employer, so that tax issues and Government bonuses are correctly accounted for.

Furthermore, ECCD should consider assessing whether the same situation in relation to the payment of Government bonuses recurred during the years 2010 to 2014, being the period during which this employee was employed with both Departments. The possibility of raising a claim for refund should also be considered.

Erroneous Retardation of Increments

It is recommended that the amounts underpaid are settled accordingly by ECCD. The Department should also consider the implementation of more controls, especially in areas related to promotions and progressions. This would go a long way in ensuring that errors related to changes in the basic salary computations are limited as much as possible.

Control Issues

Lunch Breaks not being deducted from Public Holiday Allowances

It is in the interest of employees that they avail themselves of a rest period whenever their working day exceeds six hours. The Department should consider issuing a circular to all its employees to ensure that they are aware of this entitlement.

This would not only ensure that the pertinent provisions are duly followed, but also that any calculations made on the basis of the time recorded on timesheets are accurate and consistent amongst officers.

Shortcomings in relation to Timekeeping

Authorising officers are to be made aware of the fact that whenever they are endorsing timesheets, they are assuming responsibility that every detail is correct. Before overtime is paid, thorough checks are to be carried out to ensure the correctness of payments to employees, as well as to minimise adjustments to subsequent salaries.

It is also recommended that ECCD ensures that VL records are duly signed before the VL is availed of, save in 'emergency leave' cases.

Compliance Issues

Inadequate Overtime Approvals

It is highly recommended that overtime approvals are properly obtained in line with PSMC requirements. Furthermore, attention must be given to ensure that, as far as possible, overtime is approved by the appropriate levels before it is carried out, ensuring that proper control is exerted over the claim/request for overtime, number of hours worked and the resulting costs.

Management Comments

In its reply, Management concurred with most of the observations and recommendations put forward by NAO. The Department is already implementing NAO's recommendations which have been taken on board with immediate effect and have been addressed as the audit was being conducted. NAO's attention was also drawn to a Debt Recovery Policy which has been compiled and implemented by the Department. The following comments were also forwarded:

Inaccuracies in Allowances paid to General Practitioners

Contrary to what was confirmed by ECCD at audit testing stage, the Department later stated that the Payroll System only allowed one option for 'Job Plan A+1', which option did not have any reference as to whether it was assigned to Consultants or GPs.

Management also commented that, "… *Considering that SVP*[9] *is a separate entity altogether from AACCD*[10] *implies that the Department cannot be held responsible and monitor duties which are to be performed by other entities*".

Furthermore, "*It has to be appreciated that although AACCD is a budget holder, and therefore paying agency for a considerable number of employees who render services across other departments and ministries, AACCD has no means to control duties performed across other entities*". It was also felt that, "… *third party entities exercise sufficient control over payroll calculations to an extent that workings are performed by respective salary sections and endorsed by a high ranking official …*".

NAO satisfactorily noted that the GPs in question were contacted by the Department and are currently on a repayment plan to settle amounts overpaid to them, by latest December 2018.

[9] Referred to in this Report as SVPR.
[10] Active Ageing and Community Care Directorate, referred to in this Report as ECCD.

Ministry for Justice, Culture and Local Government

Judicial

Expenditure

Background

The Law Courts' mission is "*to provide both the public and the judiciary effective and efficient services, structures and know-how to enable the public to understand, follow and be informed of the judicial processes in which they may be involved and to provide the judiciary with the necessary staff, tools and services in order that they may dispense justice properly and efficiently*"[1].

The audit focused on Judicial costs incurred in 2015 for 'Summoning and Expenses of Witnesses, Jurors and Experts in Criminal Court Trials', expensed from Programmes and Initiatives control account 5154. Expenditure on 'Transport' (line item 27) and 'Contractual Services' (line item 30) was also reviewed.

During the year under review, there was a shortfall of €424,752 between the recurrent budget of €1 million allocated to control account 5154 and the actual expenditure of €1,424,752. This discrepancy was financed through the issue of one warrant amounting to €398,000 and virements with a net amount of €32,085 from Personal Emoluments. Thus, the initial budget in respect of the account in question was augmented by a total of €430,085. It is to be noted that an amount of €1,269,317, *i.e.* 89% of the total disbursements from the foregoing control account, related to payments issued for professional services rendered by Court Experts. Furthermore, as also outlined in the Annual Report for 2015 prepared by the Ministry for Justice, Culture and Local Government (MJCL), such expenditure was also the main contributor to the substantial increase of €544,217, between what was spent in 2014 and 2015.

The allocation of €300,000 provided to the Courts of Justice (CoJ) to cover contractual services was also insufficient to meet the respective expenditure, which during the year under review amounted to €350,943 (*i.e.* an adverse variance of 17%). Meanwhile, the budget for transport stood at €500,000, whereas actual expenditure amounted to €469,380.

Audit Scope and Methodology

The main objectives of the audit were to ascertain that:

a. expenditure incurred in financial year 2015 from control account 5154 is accurate, complete and related to 'Summoning and Expenses of Witnesses, Jurors and Experts in Criminal Court Trials', as intended; and

[1] Source: https://mjcl.gov.mt/en/justice/pages/courts-of-justice.aspx.

b. procurement as well as contracting activities were carried out in accordance with standing laws, regulations, policies and procedures, thus ensuring efficient administration of public funds.

A sample of 72 Payment Vouchers (PVs), covering expenditure incurred for the 'Summoning and Expenses of Witnesses, Jurors and Experts in Criminal Court Trials' (43 PVs), 'Transport' (19 PVs), as well as 'Contractual Services' (10 PVs), were selected for audit purposes. The sample was based on materiality and related risk and collectively amounted to €490,460, *i.e.* 21.85% of the selected areas on which a total of €2,245,075 was spent.

Audit Disclaimer

Hospitality Expenses incurred during Trials

Actual board and lodging expenses, incurred for the hospitality of jurors during the four trials executed during the financial year under review, aggregated to €56,673, of which €38,992 related to accommodation on half-board basis, €17,280 incurred for lunches provided to jurors, with the remaining balance of €401 being expensed on refreshments[2]. Whilst the provision of accommodation for jurors was covered by a call for tenders, following which the contract was awarded to the sole bidder, no quotations were traced with respect to the procurement of lunches. Since provisions of the Public Service Management Code (PSMC) do not cover such expenditure, no audit procedures could be carried out to ensure that the rates charged were in line with the regulations.

Key Issues

No Formal Procedure for the Nomination of Court Experts

The appointment of Court Experts may be made directly by the Court or by the Minister responsible for Justice after consultation with the Chief Justice. However, no formal procedures regulating such nominations are in place. This concern was already highlighted in previous audits carried out by this Office for financial years 2003 and 2010 respectively, and was voiced again in a Report drawn up by the Commission for the Holistic Reform of Justice System in 2013.

Moreover, a roster system, as suggested in Article 650 of the Criminal Code is also not being prepared. Individuals are designated as Court Experts at the exclusive discretion of the respective Magistrate or Judge.

Rates for Court Experts not established

Explanations provided by Management during the course of the audit confirmed that, although substantial amounts of money are being paid to Court Experts for professional services rendered to the Court every year, no guidance is in place to establish the official rates to be charged. According to CoJ, the unofficial rates are taxed by the Court Registrar after negotiating the fee due with the respective Expert.

Lack of Segregation of Duties and Insufficient Internal Controls

From testing carried out, it transpired that the great majority of PVs in the audit sample, *i.e.* 33 out of a sample of 36 payments covered by a Local Purchase Order (LPO), were signed by the same officer that had formerly approved the relative LPO, and who also verified the respective timesheets in case of contractual services.

[2] This mainly included water, tea, coffee and sugar.

The absence of basic controls has led to undetected errors, resulting in inaccurate payments, as well as non-compliance with employment rules and regulations. Further details are highlighted under Control Issues in this Report.

Control Issues

Opportunities for improvement were identified in the following areas:

Court Experts

Reimbursement of Expenses to Court Experts not duly substantiated

Besides the professional fees, commonly known as *Dritt*, Court Experts are also reimbursed for miscellaneous expenses incurred whilst carrying out their task assigned by the Court, including but not limited to transport, *aċċess* and photos. Audit procedures carried out on this area revealed the following shortcomings:

a. From the verbal explanations provided by the two Deputy Registrars, who during the year under review were responsible to tax Court Experts, the National Audit Office (NAO) was given the understanding that the expenditure in question is reimbursed in line with the rates that have evolved throughout the years. However, the actual amounts reimbursed did not tally with the rates provided by the Deputy Registrars. Following a request to provide an explanation, another undated document with different rates was presented. Yet, at times discrepancies were still encountered between the unofficial rates and the actual rates charged.

b. Besides discrepancies with the unofficial rates provided, other inconsistencies were noted, mainly in the rates for report typing and with respect to *aċċess*. Although at face value the difference may appear to be immaterial, the number of sub-vouchers including such expenses was significant.

c. Out of a total of 662 sub-vouchers reviewed, collectively amounting to €212,433[3], 190 sub-vouchers included a breakdown of the additional expenses claimed, amounting to €21,797, that was reimbursed over and above the charge for the actual services rendered. However, due to the lack of supporting evidence of the claimed amounts, such as the respective receipts, this additional expenditure could not be validated.

d. In another 453 instances, no such breakdown was included. However, due to the absence of details, as well as the lack of transparency and inconsistencies in the chargeable rates, it could not be ascertained whether similar reimbursements were incorporated with the total chargeable amount referred to as *Dritt*, which summed up to €116,812[4].

e. Three of the remaining 19 claims included a lump sum for additional expenses on the sub-voucher, amounting to €309, with no specific breakdown being provided.

[3] This figure is stated net of Value Added Tax (VAT), as well as deductions outlined in section 7.4.2.5 of the PSMC, *i.e.* a deduction of 25% for the first €2,329.27 and 50% for fees in addition to the first €2,329.27.

[4] This figure is stated net of VAT, as well as deductions outlined in section 7.4.2.5 of the PSMC.

Public Officers serving as Court Experts

Section 7.4.2.5 of the PSMC stipulates that public officers giving expert advice or other service in Court, with respect to specific cases in which they do not deal with in the course of their duties, are allowed to retain 75% for the first €2,329.27 earned in a calendar year, whilst 50% is to be retained for fees earned thereafter.

During the year under review, 53 public officers provided their service to the Courts. Testing carried out on payments forwarded to four of these officers revealed that in three cases, the respective amounts were not duly retained by CoJ. In one case, the applicable retention was not deducted, resulting in the individual being paid the full amount, whilst in another instance the incorrect rate was applied. In a different instance, the 25% was also withheld on reimbursable expenditure.

Inconsistencies in Sub-Vouchers compiled by the Deputy Registrar

From a sample of sub-vouchers verified, it was noted that at times such documents lacked certain details which rendered them as incomplete.

Furthermore, a review carried out on the spreadsheet, titled 'Master Registry of Court Experts', which is being maintained by the officer responsible for the issuing of payments in settlement of such claims, revealed that 1,665 transactions, out of the 4,254 disclosed therein, also failed to indicate the respective sitting date.

These shortcomings do not give the comfort that counter-checks are being carried out to ensure that the same claim is not presented for payment more than once.

Transcribers

Limited Verification on Transcriptions

According to CoJ, random verifications are carried out by CoJ on the transcripts submitted by the respective transcribers. However, it was noted that at times transcribers failed to indicate both the nature of the respective transcripts, *i.e.* whether these relate to Direct or Indirect Hearings, as well as the applicable rate[5]. Thus, correctness of the respective amounts cannot be verified.

Over-reliance on One Transcriber

Notwithstanding that during 2015, at least 52 CoJ officers were available to carry out transcription work, it was noted that 23.5% of the total workload was assigned to one particular officer. The dependence on this individual poses a significant operational risk.

Translators and Interpreters

Fee for Translations decided by Deputy Registrars

No official documentation was traced with respect to the rates charged by the Court for typed translations of Court Hearings. The responsibility to determine such tariff was totally left to the discretion of the Deputy Registrars. From the audit sample tested, it transpired that during 2015, the chargeable fee was based on the number of words typed and varied according to the translated language.

[5] Transcriptions in respect of Sentences, Inquiries and Hearings of Indirect Witness, are paid at the rate of €1.20 for every 200 words, whilst the rate for Hearing of Direct Witness stands at €1.40.

Appointment of Translators and Interpreters who are not in the Official List

Disclosed on the Courts Services website is a list of individuals working as freelancers for CoJ, who accepted to serve as translators or interpreters during Court Hearings. However, instances were identified whereby appointment of such individuals was not carried out accordingly. Out of a total expenditure of €104,814, the total amount of €28,417 was disbursed to 120 individuals and/or companies who are not included in the aforementioned list.

Lunches

Insufficient Control in the Procurement of Lunches

In order to be catered for on a full-board basis, individuals nominated as jurors are also provided with free lunches during trials. From the verifications carried out in this area, the following was noted:

a. The current procedure in place is that quotes for set menu lunches held in Valletta restaurants are obtained over the phone by the Assistant Principal. However, formal agreements stipulating pre-established prices to be charged by the restaurants were not evidenced. During the year under review, the amount of €17,280 was expensed in this respect, of which €9,443 related to lunches procured from the same four restaurants.

b. It also transpired that no proper records of the number of persons attending such lunches was being kept by the Deputy Registrars. The only traceable evidence was a handwritten paper[6], disclosing solely the date and name of the restaurants where lunches were held. This does not give the comfort that adequate verifications were being carried out, especially when considering that, at times, the invoice is not provided instantaneously, but sent by post later on during the month.

c. Invoices submitted by certain restaurants also failed to disclose specific details, such as the number of meals provided. This issue was discussed with CoJ, who verbally stated that all set menus are provided at the fixed rate of €20 *per capita*.

d. During the audit, two instances were encountered whereby different dates were indicated on the cash-register chit, the subsequent invoice, and the covering letter prepared by the respective officer at CoJ and forwarded to the Accounts Section for payment. *Table 1* refers.

Table 1: Different Dates

Details	Date on cash register chit issued by the service provider	Date on invoice submitted by the service provider	Date indicated on internal correspondence supporting payment	Amounts
				€
Take-away service for lunch	30 September 2015	5 October 2015	2 October 2015	225
	14 December 2015	n/a	16 December 2015	199

[6] As from 2016, a typed document disclosing the name of the restaurant, as well as the number of set menus procured is being maintained.

Lunches paid for Individuals other than Jurors, Marshals and Deputy Registrars

An exercise carried out on expenditure recorded in the Departmental Accounting System (DAS), in relation to lunches paid for jurors, revealed that very often meals paid for were in excess of the number of jurors and Court officials for whom accommodation was booked.

Transport

Parking Fees not formalised

Due to the acute parking problem in Valletta, CoJ resorted to the leasing out of parking spaces at a private car park in Floriana, to accommodate the 42 cars used by the Judiciary. Notwithstanding that this practice has been in place for the last 15 years, no formal agreement was traced in this respect. This issue was already highlighted by the then Director Finance and Administration, in an internal communication dated 2 January 2003, addressed to the then Director General and Registrar of Courts. However, no decisive action was ever taken to rectify this situation.

Throughout the years, the annual parking charge per vehicle increased from €176 in 2001, to €575 in 2015. The only source documentation available to substantiate such rates is the renewal notice and the subsequent invoice.

Contraventions paid on behalf of Members of the Judiciary not recouped

As at 29 April 2016, *i.e.* during the audit period, CoJ had still not recouped the amount of €2,980 paid in contraventions for traffic infringements made by Members of the Judiciary. The amount in question includes the sum of €1,223 relating to traffic fines dating back to 2012. This is in breach of section 8.2.6.2 of the PSMC stipulating that "... *where the Department/Directorate have already settled the fine, the amount in question is to be refunded by the officer concerned*".

Insufficient Control on Government-owned Vehicles and Fuel Consumption

During 2015, CoJ had three vehicles at its disposal for general use. In addition, in line with a three-year contract issued in 2012, it also hired another 13 self-drive cars to be used by Court Marshals. A review of the logbooks held in respect of such vehicles revealed that these were not being maintained as required by pertinent regulations, thus leading to insufficient control.

By way of example, records were kept in the form of loose sheets, which at times lacked the necessary details, such as mileage covered per trip and the fuel intake. Furthermore, no evidence was traced to confirm that these records were being inspected periodically by a responsible officer. Variances noted between the closing odometer readings and the opening readings taken before the subsequent journey also imply that certain trips were not recorded.

It also transpired that in breach of MFIN Circular No. 5/2015 – 'Government Transport and Civilian Plates', general-use cars did not carry a GVN number plate.

Invoices for Chauffeur-driven Services not adequately substantiated

Members of the Judiciary

Members of the Judiciary are provided with a taxi-service[7] when the driver assigned with them is on vacation leave or reports sick, and the other reliever drivers are fully occupied. Requests for such services are placed directly by the Chief Security Officer with the service provider. Verifications carried out on a sampled PV amounting to €866, revealed the following weaknesses:

a. No adequate records are kept by the Chief Security Officer with respect to the number of trips requested and performed by the service provider. The only source documentation forwarded for audit purposes was a diary in which the latter jotted down the names of the drivers who were absent on the day, and whether their responsibilities have been assigned to a reliever.

b. An instance was noted whereby the duration of the chauffeur-driven service was not disclosed in the 'Clients Report', despite that such trips are charged by the hour. This does not give the comfort that the necessary arithmetical verifications were actually being carried out.

c. Payment was still effected in full despite that during the audit, the Chief Security Officer confirmed that he was unaware of the respective bookings on four occasions.

Jurors

d. Instances were encountered whereby transport for jurors was invoiced by the hour. However, no records to this effect were maintained by the Deputy Registrars accompanying the jurors. According to CoJ, upon receipt of invoice, Deputy Registrars check that timings of the trips are approximately the same. It was also stated that, on the first and last day of the jury, when jurors are picked up from and dropped off at their residence respectively, trip timings are checked and compared with hours quoted for each trip.

   However, no internal control procedures are in place to ascertain that the rates charged are correct and paid accordingly. CoJ relied completely on data provided by third parties. Thus, no verifications could be carried out on certain trips, due to lack of substantiating records.

Attendance Records

Absence of Attendance Verification System

In line with OPM Circular No. 14/2009 – 'Procurement of Attendance Verification Systems', Government was bound to introduce an electronic device to record attendance in all its places of work by not later than December 2010. However, by the time the audit fieldwork was concluded, *i.e.* in April 2016, the necessary equipment was not yet installed within CoJ. Consequently, attendance is recorded manually through the signing of attendance registers.

Attendance Records not verified on a Regular Basis

Verifications carried out on the manual attendance sheets maintained in respect of the contractors' employees revealed that these are not checked for correctness at least on a weekly basis. For example, the attendance registers for cleaners are only being endorsed on a monthly basis. Moreover, from a three-month sample, it was noted that, the attendance records kept for the month of July 2015 were not signed at all.

[7] Total expenditure incurred in this respect during 2015, amounted to €1,573.

It was further noted that although certain attendance registers were endorsed, the officer in charge did not indicate the respective date. Thus, it still could not be ascertained that these were certified on a regular basis.

Shortcomings in the Manual Attendance Sheets noted during an On-the-Spot Inspection

On Thursday 3 March 2016 at 10:30, NAO carried out a physical on-the-spot inspection whereby a copy of the attendance records maintained by security officers and cleaners was requested for the necessary audit verifications. The following concerns were noted:

a. In both cases, the respective attendance records were kept by the officers signing the attendance sheets, rather than maintained securely at the Manager's Office.

b. At the time of inspection, two out of the eight cleaners had already recorded the time out as 12:30.

c. In contrast, another two cleaners failed to sign in the attendance records upon arrival. These were then endorsed in the presence of NAO officials.

d. Similarly, none of the 11 security officers who were on duty on the day recorded the arrival time, but simply signed the attendance sheet as a way of formality. One of the officers verbally stated that the respective timings are then written upon departure.

e. The attendance records of another seven security officers were left blank, without indicating whether they were either off duty, or on vacation leave, or sick leave. The fact that such absence was not instantaneously indicated accordingly implies that the said officers could still sign the attendance records retrospectively on their return. As a matter of fact, on 21 March 2016, the same attendance sheets were requested by NAO for review. It transpired that three out of the seven officers in question had eventually signed their attendance records in retrospect for 3 March 2016, *i.e.* the day of the on-the-spot inspection, as if they were present on that day.

Medical Services

Shortcomings encountered in the Provision of Medical Services

Audit testing carried out on the 264 doctors' visits requested by CoJ during the year under review revealed several shortcomings as indicated hereafter:

a. The service provider failed to carry out almost 10%[8] of the total visits requested by CoJ during 2015. In reply to queries raised, the latter stated that verbal complaints to this effect are regularly lodged with the contractor.

b. On 11 instances, officers could not be located by the doctor. In such cases, visits were not performed and thus not paid for.

c. Thirty-five out of the remaining 227 invoiced visits were not answered by the respective officers. There were only two of such instances where the respective officers presented a hospital form, acknowledging that they were at hospital at the time of the visit. On another instance, an oath was taken by an officer, declaring that though at the time of visit she was at home, she failed to answer the door as she was asleep as a result of the prescribed medication.

[8] In total this added up to 26 visits, four of which were not carried out due to a power supply failure on 10 September 2015, with the result that the service provider did not receive the respective request submitted by CoJ.

d. In another five cases, the address provided by CoJ to the service provider, generally being that forwarded by the respective Directorates, was incomplete and/or incorrect. Such visits were still paid for by CoJ.

e. On another occasion, according to the doctor's report, the request and the actual visit took place on the same day that the respective officer returned to work.

f. Two instances were encountered whereby officers were not certified as being sick.

Security Services

Retrospective Agreements

a. Despite that the provision of security service at CoJ commenced as from 26 March 2010, the service provider only endorsed the respective contract on 22 April 2010, which agreement was then countersigned by the Director General (Department of Contracts) on 4 May 2010.

b. Irrespective of the other provisions of the contract, CoJ took this last date as the official date of the commencement of the agreement.

c. Addendum 2, covering an extension of three months falling between 26 March and 25 June 2014, was also signed retrospectively on 16 July 2014.

d. Although not provided for in the original contract, through an addendum endorsed in July 2014, upon expiration, the contract was formally extended for an additional period of three months. However, the service continued to be procured from the same contractor up to 15 May 2015. Whilst approval from the Ministry for Finance was traced in this respect, no agreements were entered into with the contractor for services provided during the extended period.

e. By the date the new agreement was signed on 30 April 2015, there were already clear guidelines on the new contractual rates payable for security services undertaken by Government. However, these were only formally approved four weeks later, through an addendum endorsed on 25 May 2015.

Officers paid at Overtime Rates for Work carried out during Core Hours

Article 4.2.6 of the Terms of Reference of the three-year contract agreement for security services endorsed by the Director General (Department of Contracts) on behalf of CoJ, outlines that the core business hours (Monday to Saturday, excluding public and national holidays) are construed to be from 06:00 to 19:00 all year round. Notwithstanding this, source documentation provided for the two months falling within the audit sample, namely June and October 2015, revealed that a total of 94 hours (15 hours in June and the remaining hours in October) were paid at overtime rates, despite that the respective service was provided during the established core hours.

According to CoJ, additional hours worked beyond the traditional 40-hour week are paid at overtime rates to ensure the smooth running of security services.

Others

Engineering Consultancy Services not backed up by Agreement

There was no documentation formalising the engagement of an engineer as a consultant on the electrical, as well as mechanical plant and equipment at CoJ. The only source documentation evidenced was the

recommendation of the then Director General to the Permanent Secretary for such engagement, and the subsequent approval granted on the basis that the necessary funding was available. From additional correspondence traced, it also transpired that the respective engineer was responsible to appoint technicians to carry out the necessary maintenance at CoJ.

This service which has been provided for the last 20 years is being paid at the quarterly rate of €699.

Second Extension to the Contract not covered by the Original Tender

The three-year contract agreement entered into on 30 May 2012, for the provision of accommodation for jurors during trial by jury, provided the possibility of being extended for a further six months[9]. However, through two separate addenda, the contract was extended for over nine months, where "*the last departure of jurors and accompanying staff will be 18 March 2016*".

Bank Guarantees overlooked

Instances were encountered whereby either bank guarantees were not traced at all in the respective departmental files, or these were not renewed upon expiration. This implies that CoJ is not protected if the contractor fails to deliver as agreed upon.

Contract Extensions endorsed retrospectively

During the audit, NAO came across two instances whereby the addenda covering a six-month extension to the original contract, were endorsed retrospectively.

Lack of Source Documentation

Following a call for tenders issued on 13 April 2012 by the Information Management Unit (IMU), the contract for the setting up, installation and commissioning of an open filtered wireless internet service at CoJ was awarded to a contractor for a total cost of €40,801 over a period of three years. A review of the tendering process revealed the following shortcomings:

a. A copy of the quotes submitted by the two bidders was not traced in the respective departmental file. According to CoJ, since such documentation was not found with the records maintained by the latter, it is understood that it was retained by the IMU, being the entity responsible for the publication, evaluation and awardance of the respective tender.

b. Despite that upon expiration of the contract, an addendum covering the extension of the contract by a further six months was drawn up, this was neither signed by the service provider nor by the contracting authority.

Police Conduct and Private Guard Licences not provided

Agreements in place for the provision of cleaning, clerical, as well as security services, invariably bound the respective contractor to furnish CoJ with the police conduct and where applicable, the police guard licence of those employees assigned to carry out their duties at the Courts. However, instances were encountered where the respective documents were either not provided for audit purposes, or failed to cover the full year under review.

According to CoJ, rather than requesting a police conduct, a search was being conducted through the court system to ensure that the respective individual does not have any criminal records. However, a record of such searches is not kept on file.

[9] A tender with a closing date of 7 April 2015 was issued, but the only offer submitted was rejected on the basis that it exceeded the budget.

Compliance Issues

Non-compliance with VAT Legislation

On the grounds that CoJ is not registered for VAT purposes, goods and services provided to the former by VAT registered suppliers or service providers are to be covered by a fiscal receipt in line with the Thirteenth Schedule of the VAT Act. Out of a sample of 72 payments, 19 which collectively amounted to €134,600, were not supported by the relevant fiscal document.

Furthermore, substantial delays were noted in the submission of all the quarterly defaulter lists covering financial year 2015.

Lack of Audit Trail for Income Tax and VAT purposes

No action was taken to rectify the following shortcomings, which were already highlighted in the audit conducted by NAO for financial year 2010.

a. Persons providing medical and health services fall outside the scope of the VAT Act and thus are not obliged to issue a fiscal receipt. However, these service providers are not precluded from issuing an ordinary receipt as required under other legislation. Audit testing carried out revealed that medical professors appointed as Court Experts were rarely furnishing CoJ with any receipts upon the settlement of payments for services rendered.

b. Despite the fact that the contractor providing transport services was authorised by the VAT Department to issue computer generated receipts, the exemption number issued by the foregoing Department was not quoted on the invoices submitted by the respective service provider. This is in breach of pertinent regulations issued by VAT Authorities.

Postings to Inappropriate Accounts

Six PVs in the audit sample, totalling to €20,078, were posted to the wrong line item, making the respective information rather misleading.

Delegations of Authority not evidenced

In line with standing regulations, public procurement through a call for quotations, tender, or direct order, is to be authorised by the Minister responsible for the respective department or by an authorised official in his stead.

During 2015, procurement was approved by the Permanent Secretary, however no evidence of the Minister's official delegation was provided for audit purposes.

Police Conduct not requested prior to appointment as Court Experts

Verifications carried out revealed that CoJ does not request any records evidencing that individuals appointed as Court Experts are of a good conduct. An instance was encountered whereby despite of his criminal past, an individual was still providing his services to CoJ in 2015. Following NAO's request for the individual's police conduct, the auditee confirmed that this was not available from their end.

Permanent Secretary's Approval to act as Court Experts not requested

Public officers engaged on full-time basis are failing to request permission from the respective Permanent Secretary, prior to giving expert advice or other service in Court with respect to specific cases which they do not deal with in the course of their duties. Such consent is required in terms of section 7.4.2.5 of the PSMC.

Incongruous Payments effected to Service Provider

The agreement entered into with a contractor for the hire of self-drive cars for the members of the Judiciary clearly states that the service provider is responsible for all ordinary and extraordinary maintenance and repairs of the cars. However, expenditure totalling €814, incurred in July 2015 for the towing and repair of a particular vehicle following damage sustained to the clutch, was fully absorbed by CoJ notwithstanding that the latter accepted the service provider's statement that this repair was related to misuse of the vehicle rather than to wear and tear. CoJ maintained that it was difficult to establish who was responsible for such damage.

Delays by the Tender Evaluation Committees

a. The Standard Operating Procedures/Guidelines for Tender Evaluation Committees recommend that evaluation of bids is to be concluded within six weeks from the closing date of the tender. However, instances were encountered whereby this timeframe was extended up to almost three months.

b. A *curriculum vitae* of each of the members of the Evaluation Committee was not always prepared and maintained for record purposes in line with the cited procedures.

Recommendations

Key Issues

No Formal Procedure for the Nomination of Court Experts

Whilst acknowledging that the ultimate prerogative for the selection of Court Experts remains with the respective Members of the Judiciary on a strictly fiduciary basis, CoJ is encouraged to adopt methods, in close collaboration with said Members, to further enhance fairness and transparency.

CoJ may consider publishing an expression of interest in the Government Gazette, on an annual basis, whereby professionals and suitably qualified individuals who are interested in giving such service are given the chance to express their interest.

Once persons appointed as Court Experts are identified, a register disclosing both the name of the individuals and their area of expertise can then be compiled, regularly updated and made accessible to MJCL.

Rates for Court Experts not established

An official and legislative guidance on tariffs for payments to Court Experts is expected to be established and adhered to, in order to enhance transparency.

Lack of Segregation of Duties and Insufficient Internal Controls

In view that internal controls are fundamental to the success of the day-to-day running of CoJ, the latter is encouraged to develop adequate internal control procedures. Lines of responsibility are to be clearly identified and communicated to all employees. A formal system for the authorisation and approval of procurement, certification of invoices and subsequent payments is to be in place. Different levels of the procurement process, including the recording thereof, is to be undertaken by different individuals, where this is possible.

Control Issues

Court Experts

Reimbursement of Expenses to Court Experts not duly substantiated

For the sake of fairness and transparency, reimbursements are to be effected in line with official rates. Furthermore, requests are not to be honoured unless duly substantiated by detailed breakdown of the claimed expense.

Public Officers serving as Court Experts

Adequate controls are to be implemented, enabling verifications to be carried out prior to the issuance of payments. Moreover, deduction rates are to be applied in line with PSMC provisions.

Inconsistencies in Sub-Vouchers compiled by the Deputy Registrar

Being the main source documentation on which Court Experts are paid, sub-vouchers are to be carefully compiled and are to include all the necessary details and endorsements. No payments are to be effected unless proper certification is carried out.

Transcribers

Limited Verification on Transcriptions

For the sake of transparency, it is recommended that verifications are carried out on a larger sample, and are not to be limited to the number of words but are also to be extended to the rate being charged. Moreover, CoJ is to ascertain that the data provided for reimbursement purposes is clear, complete and can be relied on.

Over-reliance on One Transcriber

To minimise inherent risk, Management is to consider the possibility of reducing the dependency on particular transcribers by distributing the work more evenly and/or consider engaging full-time officer/s to carry out such tasks if it is deemed more economically feasible.

Translators and Interpreters

Fee for Translations decided by Deputy Registrars

It is pertinent that fees related to Court proceedings are official and are not left at the discretion of Deputy Registrars.

Appointment of Translators and Interpreters who are not in the Official List

CoJ is encouraged to issue an expression of interest for interpreters and translators. Once the process is concluded, the current list is to be updated accordingly and any appointments are to be made from such register when the listed individuals are available.

Lunches

Insufficient Control in the Procurement of Lunches

For the sake of transparency, agreed rates are to be documented in a formal agreement, endorsed by both parties. In addition, a reliable recording system is to be maintained, whereby the number of meals provided during each lunch is indicated, so that upon receipt of invoice, the necessary verification could easily be carried out. Any errors noted are to be rectified with the supplier in due time.

Lunches paid for Individuals other than Jurors, Marshals and Deputy Registrars

This issue is to be discussed with pertinent authorities and unless consent for such practice is obtained, Management is to refrain from paying for additional lunches.

Transport

Parking Fees not formalised

Transparency in the management of public funds is an integral part of good governance and accountability. Thus, following proper negotiations of the applicable annual rates, CoJ is recommended to draw up an agreement, to be endorsed by both parties.

Contraventions paid on behalf of Members of the Judiciary not recouped

In line with pertinent regulations, where no exceptional circumstances justifying the traffic infringements exist, fines imposed are to be paid by the respective officer.

Insufficient Control on Government-owned Vehicles and Fuel Consumption

The attention of Management has been drawn to the relative provisions outlined in PSMC to regulate the use of such vehicles and ascertain accountability of the expenditure incurred out of public funds. CoJ is encouraged to use the specimen logbook for all vehicles, as found in PSMC Appendix 8.I, thus ensuring that adequate details of each journey performed is recorded. The same regulations also require that a certificate, as per PSMC Appendix 8.II, is entered on every logbook at the end of each month, confirming that the trips recorded in the logbook were made on official duty.

Invoices for Chauffeur-driven Services not adequately substantiated

Officers verifying and endorsing invoices are to be provided with all the information required for such review. They are to be aware that once they certify the correctness of the invoice, they are assuming responsibility for such payment.

To enhance control over this expense, Management may consider requesting the service provider to issue a transport voucher for each trip, indicating the destination and the duration of the journey. Members of the Judiciary making use of such service, as well as Deputy Registrars, are to sign these forms which could then be attached with the respective invoices by the service provider.

Attendance Records

Absence of Attendance Verification System

Besides being an effective means of capturing employee attendances, the use of electronic reading devices simplifies payroll calculations. In this regard, CoJ is encouraged to take action for such system to be installed without unnecessary delay.

Attendance Records not verified on a Regular Basis

In line with section 3.1.2.1 of the PSMC, "*attendance registers are to be inspected and certified correct at the start of each week by Directors or senior officers authorised by them, who are to see that the previous week's record of attendance is complete in every detail, and all employees are accounted for*". Once such checks are carried out, the attendance records are to be endorsed, clearly indicating the date, as well as the name and the grade of the officer performing the respective verifications.

Shortcomings in the Manual Attendance Sheets noted during an On-the-Spot Inspection

CoJ is expected to check that the attendance sheets are signed on a timely basis in the presence of its personnel and kept by appropriate staff. Furthermore, NAO reiterates the importance of an electronic device to record staff attendance, in order to mitigate the inherent risk of a manual system.

Medical Services

Shortcomings encountered in the Provision of Medical Services

Management is to ascertain that employees' personal details are accurate. Moreover, a formal complaint is to be raised by the officer in charge, and forwarded to Management for any action deemed necessary, indicating the number of requested visits that were not performed by the service provider.

Security Services

Retrospective Agreements

Agreements are to be in place and signed by both parties before the contract commences. These are to show the hourly rates payable under the full contract period, so that invoices can be easily corroborated by third parties.

Officers paid at Overtime Rates for Work carried out during Core Hours

Contractual obligations are to be honoured, thus the rates stipulated in the respective contract are to be applied.

Others

Engineering Consultancy Services not backed up by Agreement

Best practice dictates that appointments are carried out either following a call for applications or a call for tenders. The respective engagement is to be duly backed by an agreement endorsed by the two parties involved. Furthermore, both the conditions of service and the duration of the agreement are to be clearly spelled out.

Second Extension to the Contract not covered by the Original Tender

Agreements are not to be extended beyond the provision specifically included in the original tender.

Bank Guarantees overlooked

A bank guarantee mitigates certain inherent risks arising from the awarding of tenders in case the selected bidder does not deliver up to the standards expected. Thus, it is of utmost importance that such guarantees are provided in due time.

Contract Extensions endorsed retrospectively

Prior to the expiration of the contract, an agreement for the extension is to be signed.

Lack of Source Documentation

Contracts are to be adhered to and duly renewed prior to expiration. Furthermore, all related documentation is to be kept in file for future reference by CoJ.

Police Conduct and Private Guard Licences not provided

Such records are to be requested and obtained in line with the respective tender. It is also to be ascertained that valid licences cover the whole duration of the contract.

Compliance Issues

Non-compliance with VAT Legislation

CoJ is to ascertain that all suppliers or service providers, who have received payments in part or in full for goods and services provided, adhere to the VAT regulations by furnishing the former with a fiscal receipt. Moreover, the VAT defaulters lists are to be compiled on a timely basis and submitted to the VAT Department within the stipulated timeframes.

Lack of Audit Trail for Income Tax and VAT purposes

It should be in the interest of CoJ to request a receipt from all service providers in order to be aware of what the latter is being paid for. Furthermore, in line with pertinent regulations, subsequent to payment CoJ is invariably to ask for a fiscal receipt from all VAT registered service providers.

Postings to Inappropriate Accounts

More diligence is to be exercised when allocating expenses so that amounts are correctly reported under the pertinent line item/s, as required by Article 52(1) of the General Financial Regulations.

Delegations of Authority not evidenced

Official delegation of authority is to be given from the respective Minister.

Police Conduct not requested prior to appointment as Court Experts

Presentations provided by Court Experts are considered as key witnesses on how legal cases are ultimately decided by the Court. Therefore, the integrity, honesty and good conduct of such individuals is of utmost importance and is to be incessantly ensured. Thus, as already emphasised in the Report drawn up in 2013 by the Commission for the Holistic Reform of Justice System, CoJ is recommended to request a copy of the police conduct prior to the appointment of a Court Expert.

Permanent Secretary's Approval to act as Court Experts not requested

Approval from the right level of authority is to be sought by public officers, before they act as Court Experts. Furthermore, payments to the respective public officers are not to be honoured unless procedures and regulations are fully adhered to.

Incongruous Payments effected to Service Provider

Strict compliance with agreed terms is recommended. If it is eventually established that damages incurred were due to misuse of the vehicle, these are to be borne by the user of the vehicle.

Delays by the Tender Evaluation Committees

As also outlined in the Standard Operating Procedures/Guidelines for Tender Evaluation Committees, the evaluation process by the Adjudication Board is to be carried out within six weeks from the closing date of the call for tenders.

Management Comments

Management concurred with most of the findings highlighted in the Report and action was immediately taken to comply with a number of NAO's recommendations, whilst others were to be taken on board in due course. The following comments and reservations were also submitted:

No Formal Procedure for the Nomination of Court Experts

"*Court experts are appointed at the sole discretion of Members of the Judiciary. It is to be noted that the Justice Department within MJCL is in the process of setting up a Court Experts Register in line with Bonello Justice Reform Report. It is the intention that this Register be made available to the Judiciary at the start of the forthcoming forensic year (October 2016). At a later stage it is planned to issue an open request for Expression of Interest for interested individuals who wish to be included in the Court Experts Register. This will not include stipulated rates payable. However, one has to keep in mind that the Judiciary may still continue to appoint Court Experts at their discretion*".

Rates for Court Experts not established

"*CoJ intends to follow up the matter once official list is established by Justice Department within MJCL. CoJ had in the past started an exercise to update tariffs in the Criminal Code but it seems that the matter was never followed up*".

Over Reliance on One Transcriber

In view of the transcription work carried out, CoJ claimed "*it is very difficult to find employees to accept this type of work. Three calls issued for Court Assistants whose duty includes the transcription of court sittings were unsuccessful*".

Appointment of Translators and Interpreters who are not in the Established List

Talks with respect to the regularisation of the appointment of translators and interpreters and the applicable fees are ongoing with the Court Police Interpreter Translator Association. However, it was pointed out "*that it is not always possible for the appointments to be made from these lists, since there are instances where these are selected beforehand by the Police during the interrogation stage*".

Lack of Control in the Procurement of Lunches

"*Current procedure followed by the Assistant Principal is subject to specific instructions given by the Presiding Judge in order to avoid that jurors take their lunches in the same restaurant for safety reasons*". However, "*Deputy Registrar will now be instructed to obtain a quote from chosen restaurant indicating price per cover provided to include details of meals and drinks. With the introduction of this procedure, invoices will also be checked against the quotation*".

Parking Fees not formalised

"*CoJ has always held back from making a formal agreement on the assumption that it would find alternative parking arrangements in subsequent years. It would be detrimental if CoJ had an agreement binding for a period of years and an opportunity for a cheaper parking area will be found. However, the latter will discuss the next renewal to negotiate a better rate for a number of years with the option that the agreement may be suspended within an agreed number of months notice. It must be noted that the rates charged are always discounted at the request of CoJ*".

Absence of Attendance Verification System

"*CoJ has already studied the possibility to introduce a palm reader, however it was not allowed to introduce such system by OPM*[10] *citing Data Protection Act. It must be noted that each directorate monitors closely attendance on a daily basis and staff are requested to sign both when arriving and leaving the place of work*".

[10] OPM - Office of the Prime Minister.

Ministry for Tourism

Institute of Tourism Studies

Personal Emoluments

Background

The Institute of Tourism Studies (ITS) is an institution for higher education established to meet the changing needs of the hospitality and tourism industry. ITS was established in 1987 and consolidated by the Education Act No. XIII of 2006 of the Laws of Malta. The main responsibility of the Institute is to furnish the tourism sector with professional personnel who can guarantee an excellent standard of products and services within the hospitality industry.

With effect from 28 July 2014, the Minister for Tourism has appointed the present Chairman, Deputy Chairman and Members of the Board of Governors for a period of three years, as per the terms of Legal Notice 131 of 2012 of the Education Act.

During 2015, *i.e.*, the year under review, ITS went through major changes with respect to key headship positions.

Financial Information

The 2015 Financial Estimates show that the Institute was allocated a budgeted contribution of €2.4 million from Vote 47 under Control Account 6804. However, during the year, following the issue of a warrant of €253,000 to cover salary payments, allocation increased to €2,653,000 by end of December.

The audit mainly focused on personal emoluments where the total expenditure for 2015 stood at €2,417,073, covering the salaries paid to an average of 112 employees on the payroll and the remuneration of nine Board Members.

Out of the foregoing paid total, throughout the year, the aggregate amount of €698,803 was recouped from the Ministry for Tourism and other Government entities.

A further amount of €213,596 was disbursed from account 30606804, namely 'Contractual Services – Others', as remuneration to another 52 individuals engaged on contract for service.

This increase in payroll was the result of the Institution's business reengineering process that took place in 2015. In its management accounts, ITS indicated that during the year under review, new Management posts were created at an additional cost of *circa* €253,000. Supplementary staff in the lower level, costing around €51,000, was also enrolled. Furthermore, as the Institute commenced a wider spectrum of part-time courses that resulted in an increase in the intake of students, more part-time lecturers were engaged at a cost of approximately €16,000.

Audit Scope and Methodology

The main scope of the audit was to assess the internal control system in place, relating to the calculation and payment of personal emoluments, and to obtain reasonable assurance that benefits paid are accurate and in line with the applicable regulations and agreements. Other objectives were to ensure that allowances were approved from the right levels of authority and that payment thereof was supported by appropriate documentation.

A sample of four administrative officers and four academic staff with different designations was selected for testing based on the materiality of salaries and allowances paid to them throughout 2015. In addition, a review of the policies and procedures for the administration of vacation leave on the sampled population was carried out.

Audit verifications were extended further to ascertain that the remuneration paid to the Chairperson, as well as two members appointed on separate Boards was in accordance with the guidelines issued by the Cabinet Office.

Audit procedures were also carried on two service providers, namely one providing messenger driver duties and the other performing general cleaning services, so as to ascertain that the procurement of service was in line with standing regulations.

Key Issues

Inadequate Handover and Lack of Internal Controls

Prior to the engagement of the present Executive Director in March 2015, there was a management vacuum following the self-suspension of the previous incumbent. Most of the key headship positions were also vacant or non-existent. As a result, there was no proper handover of the respective tasks.

From verifications carried out on a sample of employees, it transpired that internal controls in various areas were also lacking. Though it was noted that the present Management was doing its utmost to ameliorate the situation (for example, by the end of the year, it changed the way the employees record their attendance), there was still room for improvement when it comes to internal controls.

Below are examples of instances of internal control failures identified during audit testing. Each issue will be discussed separately further down in the Report, under the pertinent observations.

a. Attendance records not endorsed as certified correct.
b. Lack of control over attendance records and related payments.
c. Various shortcomings in the payment of allowances, including lack of approvals from appropriate levels of authority.

Hours expected to be performed by Part-time Employees not specified in the Contract

Limitation on Scope of Audit

As per contracts of employment on a definite period of two part-timers in the audit sample, both employees were entitled to *pro rata* benefits and entitlements as stipulated by law, which are calculated on the weekly hours worked. However, the National Audit Office (NAO) could not calculate such entitlements since both contracts failed to specify the number of hours expected to be performed weekly. By way of example, the hours claimed as sick by one of the employees varied from one day to another. Thus, the related payment could not be verified.

In addition, the related contracts only state that employees are expected to perform duties as required by ITS from time to time and the hours may vary from one semester to another. No other official documentation in this respect could be traced in the personal file.

It was only from the time recorded on the attendance sheets that NAO concluded that these two employees performed 20 and 16 hours per week, respectively.

Control Issues

Recording and Verification of Attendance

Absence of Attendance Verification System

In line with OPM Circular No. 14/2009 – 'Procurement of Attendance Verification Systems', Government was bound to introduce the necessary devices in all its places of work by not later than December 2010. However, up to the date of audit testing in September 2016, no electronic Attendance Verification System (AVS) was yet in place at ITS. Consequently, officers were required to record their attendance manually by signing the attendance registers.

Attendance Sheets not endorsed as Certified Correct

All the attendance registers for different staff levels employed at ITS, which were examined during the audit, lacked endorsement by senior Management, in disregard of section 3.1.2.1 of Public Service Management Code (PSMC). Hence, NAO could not ascertain that the time of arrival and departure recorded on the attendance records was correct.

Lack of Control over Attendance Records and related Payments

Internal controls on the manual record of attendance were found to be lacking. The following shortcomings relate:

a. Attendance by Employees at Gozo Campus not evidenced

No attendance records for 2015 were provided for a sampled official at the Gozo Campus, to support the presence at work of this individual.

According to ITS, the Personnel Office had repetitively sent attendance sheets to Gozo to be filled in; however, these were never returned or completed by the incumbent nor by the other two individuals working on the same Campus.

b. Missing Attendance Sheets and other Shortcomings related to a Part-time Employee

A part-time administrative employee was paid at a standard hourly rate. However, notwithstanding that none of the attendance records, covering hours performed during 2015, were certified correct by an independent officer, claims for payment raised were still paid by ITS.

c. One Week's Attendance Records by a Full-time Lecturer not held

From a sampled period of five months, it was noted that during the week ending 27 February 2015, a full-time lecturer was recorded in the ITS lecturers' attendance sheets that he was to lecture at an annex building of ITS, namely 'Martin Luther King Campus'. However, no evidence of signature of the said official could be traced in the respective attendance sheets.

d. No Attendance Records for a particular Week by a Cleaning Service Provider

No attendance records could be traced for the first week of employment of an individual performing cleaning duties at ITS. Only a confirmation from the housekeeper stating that the foregoing individual reported for work during the respective period was provided.

e. Discrepancies between Attendance Sheets and Hours claimed for Payment

A review of the time recorded in attendance sheets for 2015 by a messenger driver on a contract for service and the invoices forwarded to ITS for payment revealed a number of discrepancies. Notwithstanding this, the invoices were still certified correct and processed for payment.

Lecturers' Additional Contact Hours and Overtime

Incorrect Payment of Additional Contact Hours

During 2015, an individual who was a full-time lecturer and department coordinator received the total amount of €7,712 as payment with respect to overtime. The payment received in payroll 13, amounting to €1,423 was selected as an audit sample, covering overtime performed between 26 October and 27 November 2015.

It transpired that the overtime returns were not signed by the Director as evidence of approval. Furthermore, although the Personnel Office certified these documents as correct, a number of inconsistencies were noted, amongst which were the following:

a. Two modules which were included in 15 different instances in this lecturer's overtime return sheet did not form part of the lecturer's timetable. No evidence of such requirement was provided to NAO for these two claimed modules.

b. In five instances, time out preceded the time in.

c. The pre-authorisation sheet, for unscheduled hours of overtime in the sampled period, was not endorsed by Management, namely the Head of Section, Deputy Director and Executive Director.

d. The attendance sheets for the sampled period were signed by the lecturer and covered from 08:00 to 16:00. However, during this period there were 10 instances wherein the lecturer claimed for a total of 45 hours performed after 16:00.

These shortcomings cast doubt on the accuracy of the expenditure on overtime in general, as this indicate lack of internal controls and the absence of the necessary verifications that are expected to be carried out before overtime is processed for payment.

Lack of Attendance Sheets supporting Claims for Overtime Payment

Overtime claimed was not being accompanied by a certified extract of the attendance book. Payments were only based on the request for overtime form where various deficiencies were noted and already highlighted under the previous observation. Unless these claims for overtime are supported with an endorsed copy of attendance sheet, the officer in charge of salaries will not be in a position to validate payments in this respect.

Allowances

Allowances paid to Public Officers performing Security Duties not validated

a. Payment of Shift Allowance when not entitled

As per section 2.4.10 of the PSMC, employees performing surveillance duties (watchmen) are not eligible for a shift allowance.

However, during the year under review, seven public officers performing security duties at ITS were in receipt of a shift allowance which is even above that established by standing regulations. This is costing ITS the aggregate amount of €11,806 *per annum* which expenditure was not duly authorised.

b. Payment of an Allowance if Overtime performed does not exceed stipulated Threshold

According to the respective overtime return, two other officers in scale 18, also performing security duties, were each to be paid an allowance of €132 monthly, if the overtime performed does not exceed the said amount. However, ITS has no records to substantiate the approval for this allowance.

Furthermore, this allowance was not included in the bi-annual return of allowances, which was prepared when attention of the Institute was drawn on such submission, as indicated in an observation under Compliance Issues.

Increase in Program Quality Validation Board Remuneration not substantiated

On 23 September 2014, a lecturer was selected on a Board, namely Program Quality Validation, with an annual remuneration of €1,000. However, following his engagement as an Executive Director, on 4 November 2014, the said officer informed Head of Personnel that "... *it has been decided* ..." that this remuneration was to be amended to €1,165 annually for all Board Members. No further documentation to this effect was provided.

Further shortcomings relating to the approval of such allowance were noted by NAO and feature under Compliance Issues.

Coordinators' Allowance not covered by Collective Agreement

During 2015, five ITS officials who were appointed as coordinators received an annual allowance of €1,165 each. However, such allowance is not included in the collective agreement between ITS and the Malta Union of Teachers, covering a four-year period between 2012 and 2016.

This entitlement was only supported by an email dated 4 November 2014, from the then Executive Director and thus it could not be established whether the respective payments were officially approved.

Overpayment of Mobile Allowance

An Executive Director resigned from the respective post with effect from 19 May 2015. However, up to August 2015, his mobile bills were still being paid by ITS.

Leave Records

Insufficient Control over Vacation and Sick Leave

Vacation and sick leave records were being maintained on loose sheets lacking the controls for the necessary updates. Moreover, only records for 77 out of an average of 112 employees were forwarded for audit purposes. Inadequate verification was also noted before payments are effected.

Compliance Issues

Individuals rendering service to the Institute

a. Throughout the year under review, ITS forked out the amount of €224,025 for remuneration to 58 individuals rendering their services to ITS, 52 of which were paid the amount of €213,596 from account 30606804, namely 'Contractual Services – Others'. The balance of €10,429 was paid by ITS from the Personal Emoluments accounts, notwithstanding that the remaining six individuals were engaged as service providers and not employees.

b. ITS did not provide evidence that the necessary Finance clearance was obtained prior to procuring the services of the two Value Added Tax (VAT) registered individuals in the audit sample falling under this category, namely a messenger driver and a cleaner.

   Furthermore, notwithstanding that contracts for service are to be entered into when procuring specialised service that cannot be made available by public officers, the following transpired:

   - On 22 September 2014, the messenger driver was "... *employed for the time being as a VAT Service Provider* ..." through a contract for service for a period of 14 weeks, however this agreement was renewed for a further two years through two different contracts for service.

   - The other individual in the sample was engaged on 22 October 2015 to provide cleaning services for a period of three months[1]. This agreement was subsequently renewed for a further six months, through two different contracts.

c. Given that, for 2015 only, the messenger driver in question received the amount of €13,057, this procurement should have been obtained after issuing a departmental call for tenders or after publishing a call for quotations in the Government Gazette since the applicable threshold of direct orders is exceeded. However, Public Procurement Regulations were not complied with.

Part-timers not paid their Entitlements stipulated by Law

In breach of the applicable regulations, two part-time employees falling within the audit sample were not being paid at all for public holidays that did not fall on their day of rest. They were also not paid the statutory bonus, as well as, the statutory weekly allowance.

[1] For the period 22 October 2015 till 31 December 2015 only, this individual was paid the amount of €2,444.

No Break Deductions

Two individuals in the audit sample had no break deductions effected for working days over the legally established threshold of six hours duration.

The fact that the rest period is compulsory, this could either imply that the service provider is being paid for during his rest period, or no break is taken, which in both cases is in breach of employment regulations.

The Use of Mobile Phone at Government expense not approved by the Permanent Secretary

PSMC section 2.6.2 states that "*... the use of a mobile phone at Government expense should invariably be addressed to the respective Permanent Secretaries* ...". However, ITS confirmed that it has no evidence that approval from the Permanent Secretary was obtained for two individuals in the audit sample, who were provided with mobile phone facilities during 2015. In such absence, reimbursement of mobile bills may not be considered as duly authorised.

Bi-annual Return not prepared

The two annual returns, providing updated information on allowances paid to entitled personnel, were not prepared and sent to the Ministry for Finance, as stipulated by pertinent regulations[2]. Neither is a certificate being issued to confirm that the conditions pertaining to the allowances received by each officer still apply. It was only following NAO queries, *i.e.* in 2016, that ITS prepared the returns for 2015.

The non-submission hinders the periodical monitoring and review of all allowances, envisaged to be performed through the preparation and subsequent submission of the aforementioned information.

List of Signatories not provided

ITS did not have an authorised list of signatories in line with Treasury Circulars Nos. 5/2008 and 9/2015.

Qualification Allowance not paid in line with the Collective Agreement

A full-time lecturer at ITS, holds a doctorate degree in Business Administration. However, the foregoing has never received the respective qualification allowance of €935 *per annum*, in accordance with the collective agreement for doctorate qualification.

Recommendations

Key Issues

Inadequate Handover and Lack of Internal Controls

Strong internal controls are essential in assisting ITS to mitigate financial risks and achieve its objectives to manage public funds entrusted to it effectively. Moreover, Management is encouraged to reengineer the present processes so as to avoid inadequate past practices.

[2] PSMC section 2.4.1.2, MFEA Circular No. 4/2003 and section 2.4 of the Manual on Allowances Payable to Public Officers (August 2014).

Hours expected to be performed by Part-time Employees not specified in the Contract

Limitation on Scope of Audit

Management is to ensure that contracts of employment clearly indicate the number of hours expected to be performed so that employees know the exact terms governing their employment.

Control Issues

Recording and Verification of Attendance

Absence of Attendance Verification System

NAO encourages Management to acquire an electronic AVS to be used by all employees at ITS without unnecessary delay. Besides being an effective means of duly recording employee attendances, the use of electronic reading devices simplifies payroll calculations.

Attendance Sheets not endorsed as Certified Correct

The provisions of PSMC section 3.1.2 are to be invariably adhered to in order to strengthen controls over employee attendance and ensure the correctness and completeness of the registers in question.

Lack of Control over Attendance Records and related Payments

Pending the introduction of an electronic AVS, adequate controls are to be in place in order to address the shortcomings noted in attendance records. Reconciliations are also to be performed with the hours claimed in the invoices forwarded for payment by the service providers.

Lecturers' Additional Contact Hours and Overtime

Incorrect Payment of Additional Contact Hours

A review of overtime paid is recommended in order to ensure that correct payments are made.

Lack of Attendance Sheets supporting Claims for Overtime Payment

In line with PSMC section 3.2.2.1(c), overtime claimed is to be accompanied by a certified extract of the attendance records. Such claims are to be thoroughly checked against the respective attendance sheets by the officer in charge of salaries, before payment is processed.

Allowances

Allowances paid to Public Officers performing Security Duties not validated

ITS is to regularise its position prior to continuing with the payments of these allowances. The necessary approvals are to be obtained and any discrepancies in the amounts already paid are to be rectified.

Increase in Program Quality Validation Board Remuneration not substantiated

ITS Management needs to ensure that it is in possession of all official documentation related to the payment of allowances, especially those indicating the authorisation, as well as the amount to be paid.

Coordinators' Allowance not covered by Collective Agreement

If the allowance in question is considered justified, a formal policy regulating its entitlement has to be in place. Thus, Management is to obtain the necessary authorisation from the People & Standards Division within the Office of the Prime Minister, as per PSMC section 2.4.1.3 and, if such allowance is approved, a provision in future collective agreements is to be included, clearly stipulating its eligibility.

Overpayment of Mobile Allowance

Internal controls are to be strengthened in order to avoid unnecessary disbursement of taxpayers' money. Furthermore, ITS is to recoup the related payments from the individual concerned.

Leave Records

Insufficient Control over Vacation and Sick Leave

In order to reduce administrative paper work, as well as ensure that records are automatically updated, ITS should consider introducing a system whereby leave is applied for and approved electronically. Furthermore, regular reconciliations between attendance reports and vacation leave records are to be performed by the officer in charge, to ensure that the respective records are updated accordingly.

Compliance Issues

Individuals rendering service to the Institute

Transactions are to be appropriately posted in the respective accounts, ensuring consistency, as also required in terms of the regulations.

Management is also to abide with OPM Circular No. 20/2006, whereby it is stated that "... *contracts for service are to be treated at Ministry level in accordance with current financial regulations, that is, the Budgetary Operations Division within the Ministry of Finance* ...".

Furthermore, as per standing regulations, such services are to be provided following a departmental call for tenders or after publishing a call for quotations in the Government Gazette if the respective amounts exceed the applicable thresholds.

Part-timers not paid their Entitlements stipulated by Law

Management is to ensure that it is in compliance with relevant legislation.

No Break Deductions

Employment regulations are to be invariably adhered to. Thus, ITS is to ensure that the break period is deducted from the respective payments, as applicable.

The Use of Mobile Phone at Government expense not approved by the Permanent Secretary

Approval from the right level of authority is to be sought in such instances. The respective payments are not to be honoured if this benefit is not duly authorised.

Bi-annual Return not prepared

Management is to ensure that all allowances are reviewed regularly in order to ascertain whether the conditions under which they were granted are still valid. The relevant information is to be collated and the return submitted on a regular and timely basis.

List of Signatories not provided

The lists of authorised signatories are to be compiled and updated in line with the relevant circulars and General Financial Regulations.

Qualification Allowance not paid in line with the Collective Agreement

Adherence with the collective agreement for academic staff, as well as compliance with the respective provisions of the PSMC, is recommended. The attention of Management is also being drawn to the recognition criteria by Malta Qualifications Recognition Information Centre.

Management Comments

Management concurred with all observations and will take the respective recommendations on board. Relevant feedback is being reproduced hereafter:

Inadequate Handover and Lack of Internal Controls

Management will look into the processes, reengineer them as required and implement better internal controls in the following areas as listed in the report:

- *Attendance records not endorsed as certified – to be implemented*
- *Lack of controls over attendance records and related payments – to be implemented*
- *Various shortcomings in the payment of allowances, including lack of approvals from appropriate levels of authority – to be implemented*

Hours expected to be performed by Part-time Employees not specified in the Contract

Limitation on Scope of Audit

We agree with the findings of the auditors. ITS will ensure to include the number of hours (or an addendum as applicable) to the contracts of all part-time employees.

Recording and Verification of Attendance

Absence of Attendance Verification System

Management has implemented a new attendance recording system in October 2015 which is also being acknowledged in the auditors' report. Management is currently undergoing negotiations with the union to finalise the collective agreement. The new management had installed an attendance verification system (AVS)

to be used with immediate effect. However, the union informed the new management that there was an agreement with previous management that the AVS will be implemented once the new collective agreement come into effect. This was also confirmed by PACBU[3]. Both parties agreed on this as a way forward.

Attendance Sheets not endorsed as Certified Correct

Attendance records of administration staff are collected at 8:30am and a report is drawn and sent to management. A member of the personnel office takes note of the attendance records of academic staff and send a daily report to management. Management will take the recommendation of the auditors on board and the Head of Corporate Services will endorse the attendance records as per section 3.1.2.1 of the PSMC.

Lack of Control over Attendance Records and related Payments

a. Attendance by Employees at Gozo Campus not evidenced

An AVS is already installed at the Gozo campus and will become operational upon signing of the collective agreement. The Head of Administration in Gozo has been approached by the Head of Corporate Services to ensure that all attendance records are sent to St Julians campus on a weekly basis. This procedure is currently being complied with.

b. Missing Attendance Sheets and other Shortcomings related to a Part-time Employee

Upon the introduction of the new attendance recording system by the new management, the part-time employee did not sign the new attendance records despite reminders by the Personnel Office. According to the personnel office, the employee was keeping records in her diary. This was never brought to the attention of the HR[4] manager or Head of Corporate Services. This situation has now been rectified.

c. One Week's Attendance Records by a Full-time Lecturer not held

Noted and procedures are now in place to avoid similar instances in the future.

d. No Attendance Records for a particular Week by a Cleaning Service Provider

No attendance records were retrieved. The housekeeper keeps a record of the roster and updates accordingly if cleaners report for work or not. The housekeeper confirmed that she did report for work between 22 and 30 October 2015. Procedures are now in place to avoid such instances.

e. Discrepancies between Attendance Sheets and Hours claimed for Payment

Following the report of the auditors, management will look into the discrepancies reported by the auditors and will take necessary action.

Lecturers' Additional Contact Hours and Overtime

Incorrect Payment of Additional Contact Hours

Management will look again into the attendance records, timetable and overtime returns of the individual and will rectify accordingly if discrepancies are confirmed. Management will also review the overtime recording, authorisation and payment process.

[3] PACBU - Public Administration Collective Bargaining Unit.
[4] HR – Human Resources.

Lack of Attendance Sheets supporting Claims for Overtime Payment

Management will ensure that the request for overtime is also accompanied by a certified extract of the attendance records in line with PSMC Section 3.2.2.1.

Allowances

Allowances paid to Public Officers performing Security Duties not validated

a. Payment of Shift Allowance when not entitled

Management could not find all the documentation related to these allowances. These allowances were already in place years before new management took over. Five of these officers are now employed with ITS through an expression of interest and these allowances are now regularised. Approvals will be requested for the other two employees.

b. Payment of an Allowance if Overtime performed does not exceed stipulated Threshold

The bi-annual return was amended to include the allowances ... . These allowances are no longer paid as one of the officers is now employed with ITS under new employment conditions and the other has now retired.

Increase in Program Quality Validation Board Remuneration not substantiated

Management took the auditors' recommendation on board and is ensuring to be in possession of all official documentation related to the payment of allowances including authorisation and the amount to be paid.

Coordinators' Allowance not covered by Collective Agreement

Management will follow the recommendation of the auditors and seek approval as per PSMC Section 2.4.1.3. It will also include any applicable allowance related to this role in the new collective agreement.

Overpayment of Mobile Allowance

Management will look again into the records and will recoup the related payments.

Leave Records

Insufficient Control over Vacation and Sick Leave

The vacation leave is being recorded in a spreadsheet for each employee and now also on the payroll software system. Management will ensure that all employees' records are updated. Managements intends to work the payroll in-house and is considering an electronic leave system in parallel with AVS.

Individuals rendering service to the Institute

In view that the new management found skeleton staff at the Institute and also a situation where sub-contracted cleaners were not being paid by the contractor, and after consultation with the Ministry, it was decided to engage self-employed cleaners. This situation has now been rectified as ITS now employs its own cleaners[5].

Part-timers not paid their Entitlements stipulated by Law

Management has already rectified the current situation and will also issue payment for entitlements and any other payments due for entitlements. Management will also ensure that all part-time lecturers are benefiting from said entitlements.

No Break Deductions

Management is ensuring that anyone who works more than 6 hours takes a minimum of a 15 minute break.

The Use of Mobile Phone at Government expense not approved by the Permanent Secretary

Approvals for mobile phone reimbursements will be sought accordingly.

Bi-annual Return not prepared

Bi-annual returns are now being sent as duly noted by the auditors. Management will review allowances as recommended and future bi-annual returns will be sent as required to the Ministry of Finance.

List of Signatories not provided

Authorised signatories will be updated accordingly.

Qualification Allowance not paid in line with the Collective Agreement

The situation ... ... has been rectified.

[5] No reply was given on whether Management intends to procure such contracts for service in compliance with Public Procurement Regulations and whether Finance clearance is being obtained. Another point of concern on whether transactions are being appropriately posted in the respective accounts was also not addressed.

Other Reports

Arrears of Revenue 2015

Background

In terms of Article 49(i) of the General Financial Regulations 1966, all officers charged with the supervision of the collection or other moneys due to Government are required to submit an annual Arrears of Revenue Return (ARR), in duplicate, to the Accountant General, for transmission to the Auditor General. Treasury Circular No. 6/2016 – 'End of Year (2015) Statements of Account' also required officers to forward 'Nil' Returns.

All Returns were to reach Treasury by not later than 30 March 2016. As *per* the foregoing Circular, officers also had to forward a copy of the Statement of Arrears to the Budget Affairs Division, Ministry for Finance (MFIN).

Ministries and Departments are obliged to submit the position of debtors on a quarterly basis, on specified templates, to be uploaded on the Accrual Accounting Financial Reporting System. In this regard, the same Circular also states that "... *Heads of Departments are requested to note the link between this return and the end of year Debtors template sent to Treasury as part of the Accrual Accounting data submission programme*. ..."

As also noted during last year's review, Departments were required to submit details of payments received during January 2016 relating to balances due as at 31 December 2015. This data allows for the calculation of amounts due as at year-end but still unpaid on 31 January 2016. Information submitted revealed that an amount of €33,071,794 was collected during January 2016, with a resulting unpaid balance of €401,283,462 pertaining to amounts due as at 31 December 2015.

Through the issue of Treasury Circular No. 12/2016 – 'PAC[1] Specific Request', Heads of Departments were further requested to provide additional information in relation to their Statement of Arrears of Revenue, 2015. This request was made specifically by the PAC Chair following a meeting held on 4 July 2016 discussing the Arrears of Revenue reported by the Auditor General in the Public Accounts 2014 Report. The relevant submissions by the various Ministries and Departments were required by 17 August 2016.

[1] Public Accounts Committee

From these submissions, it is estimated that out of total reported gross arrears of revenue of approximately €2.6 billion:

- €1,560,540,351 were statute-barred;
- €121,617,202 were pending Court action;
- €294,147,832 were deemed recoverable by departmental action; and
- €639,700,910 are considered recoverable.

Table on page 326 refers.

Returns

Thus, details of Arrears of Revenue included in the Table on page 322 have been compiled only from Returns forwarded to the National Audit Office (NAO) by Treasury. The following submitted 'Nil' Returns:

- Office of the President
- House of Representatives
- Office of the Ombudsman
- Office of the Prime Minister
  - Public Service Commission
  - Electoral Office
- Ministry for European Affairs and Implementation of the Electoral Manifesto
- Ministry for Home Affairs and National Security
  - Correctional Services
  - Probation and Parole
- Ministry for Finance
  - Treasury Department
- Ministry for Energy and Health - Energy

Notes and Comments on Arrears of Revenue[2]

Office of the Prime Minister

The gross/net closing balance as at 31 December 2015, reported by the Office of the Prime Minister in its ARR, amounted to €18,358. This outstanding balance is made up of:

- €1,948 is in respect of reimbursement of Maternity Leave; and
- the amount of €16,410 is to be refunded from four employees who failed to fulfil their obligations in connection with a sponsorship of a Masters Degree.

All pending amounts are being settled gradually.

[2] Figures may not add up due to rounding-up.

Ageing of debtors can be classified as follows:

	€
Amounts outstanding for less than one year (2015)	6,700
Amounts outstanding for over one but less than two years (2014)	9,710
Amounts outstanding for over two but less than five years (2011 – 2013)	-
Amounts outstanding for over five years (– 2010)	1,948
Net Closing Balance	**18,358**

Department of Information

The outstanding balance of arrears as at 31 December 2015, disclosed by the Department of Information, amounting to €49,249, is all due from Government Departments and Entities, out of which the amount of €38,359, *i.e.* 78%, is in respect of Government Gazette adverts.

The ageing of the Department's debtors is categorised as follows:

	€
Amounts outstanding for less than one year (2015)	42,827
Amounts outstanding for over one but less than two years (2014)	492
Amounts outstanding for over two but less than five years (2011 – 2013)	5,890
Amounts outstanding for over five but less than ten years (2006 – 2010)	40
Net Closing Balance	**49,249**

By the end of January 2016, a total of €31,578 had already been recouped.

Moreover, as *per* Appendix A in reply to Treasury Circular No. 12/2016, the Department claimed that the gross closing balance as at 31 December 2015 for the amount of €49,249 was entirely recoverable as at that date. However, it was also disclosed that an aggregate amount of €5,890, pertaining to years 2012 and 2013, have since been deemed as uncollectable. As stated by the Department, these balances related to overtime refunds in connection with photo coverage of Ministries which no longer exist.

Government Printing Press

The net closing balance as at 31 December 2015, as provided by the Government Printing Press consists of:

	€
a. Revenue	301,113
b. Revolving	165,710
Net Closing Balance	**466,823**

The majority of this amount is due from Government Departments and other Entities.

An ageing of the net collectable arrears can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	211,636
Amounts outstanding for over one but less than two years (2014)	69,357
Amounts outstanding for over two but less than five years (2011 – 2013)	58,563
Amounts outstanding for over five but less than ten years (2006 – 2010)	125,817
Amounts outstanding for over ten years (– 2005)	1,450
Net Closing Balance	**466,823**

Government Property Division

The Government Property Division (GPD) had a gross/net closing balance as at 31 December 2015 of €28,378,986 in its ARR.

During 2015, the Department progressed further on the data cleansing exercise on properties allocated to Government Departments, Parastatal Entities and Local Councils, initiated in the previous year, consisting of reconciling its own data with that obtained from the respective Department/Entity. Consequently, several accounts were deleted, whilst others were newly created.

Following instructions from MFIN to start charging rent from Government Departments in advance and not in arrears, there were a few Departments who could not settle a doubled amount due to limited fund allocation. As a result, the Department reported a newly accrued arrears figure of €2,659,779 in respect of these Entities. GPD claimed that unless there is an increase in fund allocation to each respective Department, it would be difficult to recoup such arrears.

Ageing Analysis

The net collectable arrears can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	8,253,830
Amounts outstanding for over one but less than five years (2011 – 2014)	12,231,917
Amounts outstanding for over five years (– 2010)	7,988,744
	28,474,491
Less unallocated credit	(95,505)
Net Closing Balance	**28,378,986**

The amount of €95,505 reported as unallocated credit relates to payments made on account, for which the relative invoices had not been issued. These instances may arise when instructions to stop rent or to refuse payment are in place, or else when the tenant pays the due rent before the invoice is issued.

Collection Efforts

In order to recoup its outstanding arrears, the Department consistently monitors arrears due and pursues the relative defaulters, whilst avoiding any chance of prescription. In case of a chance of prescription, GPD still attempts to recover the amount.

A mailing system is used in the collection of arrears, whereby a statement is sent to tenants who fail to pay their rent within the stipulated period, followed by adequate reminders and phone calls, where applicable. Apart from pursuing tenants through phone calls, Enforcement Officers are also sent to deliver final notices for payments by hand. If tenants remain in default, legal proceedings will be initiated accordingly. If all these measures prove futile, then GPD may exercise its legal right to institute a Court case to terminate lease and regain possession of property.

Public Accounts Committee Request

The amount of €3,167,795 reported as statute-barred within Appendix A in reply to Treasury Circular No. 12/2016, was extracted from the Department's system. Nevertheless, GPD claimed that the amount is not in its entirety unrecoverable, as the Department will continue in its efforts to recover these dues. GPD maintained that it does not have the resources required to consult the relative files and provide a breakdown of this amount, since a statistic of all amounts covered by judicial letters is not available. Moreover, the Department stated that "... *the aggregate of €4,963,174 is all being contested in Court by tenants* ..." with "... *one particular contested amount from the stated figure stands alone at circa €3.6m*".

Ministry for Foreign Affairs

As *per* updated Return submitted by the Ministry for Foreign Affairs, the amount of €28,774 was collected (*i.e.* 47%) from the opening balance of €61,299, whilst a total of €34,774 was reported as an upward revision. This amount mainly relates to dues expected to be collected from Government Departments by five Missions that were erroneously omitted from the 2014 Return.

The Ministry reported the figure of €188,033 as newly accrued, of which the amount of €134,925 was to be recouped by an aggregate of 15 Missions.

From the gross closing balance of €255,332 as at year-end, the Ministry is only making a provision for the amount of €2,648 since it is being considered as statute-barred. This amount relates to the refund of settling-in allowances due by an officer following his early termination from diplomatic duties in 2007.

The Ministry reported a net outstanding arrears balance of €252,684 for the year ended 31 December 2015, which amount can be analysed as follows:

		€
a.	Salaries	9,686
b.	Allowances	54,178
c.	Transport	1,152
d.	Travel	711
e.	Improvement to Property	17,138
f.	Dues to Embassies	169,819
	Net Closing Balance	**252,684**

From this outstanding amount, 65% is due from Government Departments, whilst 35% is owed by individuals and private companies.

The ageing of the Ministry's debtors is categorised hereunder:

	€
Amounts outstanding for less than one year (2015)	188,033
Amounts outstanding for over one but less than two years (2014)	30,597
Amounts outstanding for over two but less than five years (2011 – 2013)	7,200
Amounts outstanding for over five but less than ten years (2006 – 2010)	26,854
Net Closing Balance	**252,684**

In line with Treasury Circular No. 12/2016, the Department considers the amount of €188,978, *i.e.* 74% of the said gross closing balance, to be recoverable through department action, whilst €2,648 (1%) was reported as statute-barred and the remaining €63,706 (25%) recoverable without department action.

In its Return, the Ministry reported that 25% of the net collectable arrears as at 31 December 2015 were received in January 2016.

Ministry for Education and Employment

Preliminary testing by NAO revealed that not all the opening balances tallied with the gross closing balances as reported in the respective Return as at 31 December 2014. Subsequent to a meeting with the officer in charge, updated versions were requested and re-submitted to this Office. However, supporting documentation provided could still not be all corroborated with the amounts quoted in the Returns; thus, the reported figures could not be verified. Furthermore, since documentation in question was submitted rather late and was voluminous as well as inconclusive, no testing could be conducted by NAO. In addition, due to lack of information, an ageing of debtors could not be compiled and the Debtors' Analysis remained unverified.

NAO recommends that an intensive exercise is carried out by the Ministry in order to ensure that such shortcomings are addressed.

Details on the amounts reported in the Returns are still given hereafter, under the pertinent sub-titles.

Ministry for Education

As *per* updated Return submitted by the Ministry for Education, the opening balance of €293,035 was revised downwards by €5,456. Furthermore, whilst past arrears collected amounted to €47,461, arrears in respect of year 2015 totalled to €130,965. An amount of €548 was recorded as written off, however the respective approval was not provided for audit purposes. The remaining gross closing balance of €370,535 as at 31 December 2015 can be analysed as follows:

	€
a. Travel Refunds	17,616
b. Breach of Contract	4,120
c. Overpayments in Salaries	233
d. External Examinations	4,183
e. Stipends: University of Malta	199,095
f. Stipends: Malta College of Arts Science and Technology	102,288
g. Stipends: Junior College and Giovanni Curmi Higher Secondary	43,000
Gross Closing Balance	**370,535**

A provision of €7,342 was made, leaving a net collectable balance of €363,193, out of which the amount of €352,919 (95%) is recoverable by department action. A total of €17,616 is due from Government Departments, while the remaining balance of €345,577 is to be collected from individuals and/or private companies.

Education Department

The opening balance of €384,087 disclosed by the Education Department in its amended ARR was revised downwards by €91,615, mainly related to salary overpayments. Whilst €16,142 was collected during the year under review, the newly accrued arrears stood at €83,599, mostly comprising overpayments in salaries. The remaining gross closing balance of €359,929 as at 31 December 2015 can be analysed as indicated hereafter:

		€
a.	Overpayments in Salaries	145,688
b.	Breach of Contract	125,325
c.	Tuck Shop	36,212
d.	Travel Refunds	52,704
	Gross Closing Balance	**359,929**

The Department considers the amount of €332,811, *i.e.* 92% of the gross closing balance, to be recouped through department action, whilst €27,118 (8%) was reported as pending Court action.

Out of the aforementioned gross closing balance, €125,369 (35%) relates to dues that are being considered as difficult to recoup, including €72,202 which is under contestation. The remaining net collectable balance of €234,560 as at end December 2015 is all due from individuals and/or private companies.

Ministry for Sustainable Development, the Environment and Climate Change

The Ministry for Sustainable Development, the Environment and Climate Change reported a gross balance in its ARR of €1,611,591. Of this, an amount of €29,762, was reported as not collectable, leaving a net balance of €1,581,829, which was split under the following categories:

		€
a.	Plant Health	1,613
b.	Veterinary Services	178,167
c.	Paying Agency	55,881
d.	Salaries	42,131
e.	Aquaculture	463,973
f.	Fisheries	824,315
g.	Parks	15,749
	Net Closing Balance	**1,581,829**

Revisions

The total amount of €144,281 was reported as an upward revision in respect of Veterinary Services (€10,441) and Fisheries (€133,840). The latter related to two long outstanding amounts, which were erroneously omitted in previous reports.

Estimated Amounts considered as Not Collectable

The same amount of €29,762 as reported in the previous year, was again being considered as not collectable for the year 2015. As indicated last year, the amount of €19,029 relates to long outstanding cases dating back to the late 1980s and early 1990s and may hence be time-barred. Further legal action is being pursued with the Attorney General (AG). The other amount of €4,500 is still at arbitration stage. Furthermore, according to Treasury Circular No. 12/2016, the amount of €181,768 was pending Court action.

Ageing Analysis

An analysis of the amounts outstanding at the end of 2015 revealed the following:

	€
Amounts outstanding for less than one year (2015)	711,921
Amounts outstanding for over one but less than two years (2014)	216,814
Amounts outstanding for over two but less than five years (2011 – 2013)	400,729
Amounts outstanding for over five but less than ten years (2006 – 2010)	252,365
Net Closing Balance	**1,581,829**

Collection Efforts

Various measures are being taken by the Department to collect the amounts overdue. These include issuing of reminders, legal letters, judicial actions, agreements for the possibility of set-offs, as well as agreements to settle payments by instalments.

Ministry for Transport and Infrastructure

The ARR submitted by the Ministry for Transport and Infrastructure (MTI) for 2015, incorporates the following revenue categories and the net closing balance of €1,698,017 comprises dues:

		€
a.	From Local Councils issued by the Central Districts Office	88,699
b.	From Local Councils issued by the Cleansing Services Department	146,015
c.	From deposit of waste and rubble issued by Cleansing Services Department	12,766
d.	To Manufacturing Services Department	1,333,712
e.	From Breach of Contracts, Damages, Maintenance and others	67,894
f.	From Refund of Salaries	48,931
	Net Closing Balance	**1,698,017**

Ageing of net collectable arrears at the end of the year, can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	524,123
Amounts outstanding for over one but less than two years (2014)	410,509
Amounts outstanding for over two but less than five years (2011 – 2013)	645,372
Amounts outstanding for over five but less than ten years (2006 – 2010)	23,868
Amounts outstanding for over ten years (– 2005)	94,145
Net Closing Balance	**1,698,017**

Past Arrears Collected

Past arrears collected during 2015 amounted to €111,399. Of this amount, €34,918 and €62,765 (in total 88%) related to the collection of 'Dues from Local Councils issued by the Cleansing Services Department' and the collection of 'Dues to Manufacturing Services Department' in respect of a number of years since 2011.

Newly Accrued Arrears

Out of total newly accrued arrears of €524,128, €462,597 were related to 'Dues to Manufacturing Services Department' mostly for fuel supplied to a company. To this effect, MTI is now receiving monthly payments for fuel dues to the Maintenance and Services Department, with the balance as at end of the financial year 2015 amounting to €364,749.

Amounts Estimated as Not Collectable

No reasons were forwarded explaining why the statute-barred figure as reported in Treasury Circular No. 12/2016 were almost double in amount as the amounts estimated as not collectable.

Dues to Manufacturing Services Department

The amount of €17,969 remained the same as in the previous year. This includes three claims, totalling €12,467, which were written off during 2016, and another two claims which are in the process of being written off. A claim of €1,282 is with another Government Department, while three balances amounting to €2,626 are currently under contestation and undergoing legal action.

Dues from Breach of Contracts, Damages and others

The total of €19,003, made up of three claims with a company, were "... *being discussed further for write off*". These amounts date back to 2004, 2007 and 2013.

Collection Efforts

It is the Department's procedure to issue a monthly statement to all creditors. If no payment is effected within six months, legal action is then initiated. In the case of very old claims, after all possible actions prove fruitless, these are referred for write-off. Moreover, in some cases, the Department also considers set-off solutions with other Departments or Entities, subject to MFIN approval.

Ministry for Gozo

The opening balance beginning 2015 stood at €293,874 and comprised solely amounts payable to the Projects and Development Directorate, namely to the Public Cleansing, Works, as well as Agriculture Departments. This included an amount of €37,619 due to the Ministry by a private company with respect to electrical and mechanical engineering services provided years back to the Ministry for Gozo (MGOZ). The respective matter was reported upon in the Report by the Auditor General, Public Accounts 2010, and was then discussed by the PAC in February 2012. Subsequent legal advice sought from AG also confirmed that MGOZ misinterpreted the proper chargeable rates as featuring in the bid, and thus the amount in question was to be recouped. However, the contractor concerned opened a Court case against the Ministry, amongst other things, claiming that the agreement *vis-à-vis* the payable rates was clear by both parties. The Ministry lost the case in question in November 2014 and was ordered to settle all outstanding dues. As a result, this claim is to be considered as not collectable during the year under review.

Arrears newly accrued totalled €31,679, of which €10,679 are due by Local Councils to the Public Cleansing Department, while the balance of €21,000 is payable to the Eco-Gozo and Regional Development Directorate

(EGRD) by the Victoria Local Council. According to correspondence provided by MGOZ, the Council was given an advance payment in 2012, being 30% of the contribution for the project to upgrade the Victoria playing field, as part of a scheme managed by EGRD. It transpired that the project was cancelled since the established period had elapsed and the Council was asked to refund the advance payment to MGOZ by the end of March 2015. However, this claim was refuted by the Council on the basis that the said funds were used for the agreed purposes.

As at 31 December 2015, the Ministry's closing balance of outstanding arrears stood at €317,909, of which €47,443 due by Local Councils, as well as the claim of €37,619 mentioned above are estimated as not collectable, leaving a 'Net Collectable' balance of €232,847. No further provisions were made despite that once again no movements were recorded in the balances of €39,880 and €149,030 due to the Works Division and the Public Cleansing (Waste Disposal) respectively, which amounts have remained constant for a number of years.

MGOZ considers the amount of €293,481, *i.e.* 92% of the gross closing balance, to be recoverable through departmental action, while no such action is necessary to recover the balance of €24,428.

The Ministry's performance and ageing of debtors can be analysed as follows:

Table 1: Ministry's Performance

Department	Opening Balance	Amount Collected	Percentage Collected	Newly Accrued	Gross Outstanding Balance	Amount considered as not collectable
	€	€		€	€	€
Public Cleansing – Local Councils	38,741	7,338	19%	10,373	41,776	20,392
Public Cleansing – Waste Disposal	149,030	-	-	-	149,030	-
Works	77,499	-	-	-	77,499	37,619
Agriculture	28,604	306	1%	306	28,604	27,051
Eco-Gozo	-	-	-	21,000	21,000	-
Totals	**293,874**	**7,644**	**20%**	**31,679**	**317,909**	**85,062**

Ageing of the net collectable arrears:

	€
Amounts outstanding for less than one year (2015)	30,189
Amounts outstanding for over one but less than two years (2014)	4,505
Amounts outstanding for over two but less than five years (2011 – 2013)	9,244
Amounts outstanding for over five but less than ten years (2006 – 2010)	-
Amounts outstanding for over ten but less than fifteen years (2001 – 2005)	20,024
Amounts outstanding for over fifteen but less than twenty years (1996 – 2000)	168,886[3]
Net Closing Balance	**232,848**

[3] This includes an amount of €149,030 relating to arrears pertaining to the period 1997-2004, but which did not include the date, and thus could not be identified separately.

Gozo Law Courts

The opening balance as at 1 January 2015, reported in the ARR submitted by the Gozo Law Courts, stood at €392,317 and €239,651 for Fees and Fines respectively.

Court Fees

The ARR's opening balance of €392,317 is slightly understated when compared to the balance disclosed in the Fees Report extracted from the CORTEX computerised system. The variance of €422, brought forward from the previous year, arose from the shortcomings of this Information Technology (IT) system, as a result of which, a total of nine fees varied in the CORTEX reports from one year to the next, while two other fees were excluded. For this reason, an upward revision was carried out to update the ARR's opening balance.

During the year under review 'Past Arrears Collected' totalled €90,509, a rather substantial increase over the prior period (€18,291). Collections included fees dating back to 1998. Revenue accrued during the year amounted to €69,131, giving a closing balance of €371,361, of which €51,530 is 'Estimated as not Collectable'. This resulted into a net collectable balance of €319,831, as at 31 December 2015.

Court Fines

The closing balance of €239,651 as at 31 December 2014 was revised upwards by €1,705, mainly as a result of two fines which, during the year under review were reinstated and incorporated in the LECAM report, while another nine fines, totalling €1,170 were revoked. Out of the revised balance of €239,827, the amount of €50,477, *i.e.* 21% (2014: 20%), was collected in 2015. On the other hand, newly accrued amounts totalled €171,816, ending the year with a net collectable balance of €362,696.

The shortcomings reported in previous years were noted once again during the current period under review. Fines which were settled quite a while ago are again shown as outstanding in the current year's LECAM report. Similarly, the report still includes fines disclosed with a negative balance, amounting collectively to €696, which although not financially material are affecting the accuracy of outstanding amounts.

All fines are to-date deemed to be revenue attributable to the Courts of Justice (CoJ) Division in Malta, with the role of Gozo Courts limited to the monitoring of their respective collection process. Thus, outstanding amounts of the latter are not included with the Debtors List prepared by the Gozo Courts. This has given rise to a discrepancy of €362,696 between the Debtor's List and the ARR.

The ageing of the gross outstanding arrears can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	240,947
Amounts outstanding for over one but less than two years (2014)	87,653
Amounts outstanding for over two but less than five years (2011 – 2013)	214,481
Amounts outstanding for over five but less than ten years (2006 – 2010)	89,387
Amounts outstanding for over ten but less than fifteen years (2001 – 2005)	48,360
Amounts outstanding for over fifteen but less than twenty years (1996 – 2000)	29,935
Amounts outstanding for over twenty years (1960 – 1995)	23,292
Net Closing Balance	**734,055**

The Gozo Law Courts consider the amount of €439,038, *i.e.* 60% of the gross closing balance, to be recoverable through departmental action. No such action is deemed necessary to collect the amount of €246,845 (34%), while the amounts of €24,486 and €23,686 are deemed to be statute-barred and pending Court action respectively.

Gozo General Hospital

The opening balance for the year under review, which stood at €146,054, differed from the closing balance for the previous year with an immaterial amount. While the Gozo General Hospital reported 'Past Arrears Collected' and 'Newly Accrued Arrears' of €6,362 and €25,589 respectively, as well as a downward revision of €1,654 to the gross arrears as at 31 December 2014, no documentation was submitted to substantiate any of these amounts. As a result, their accuracy could not be ascertained. The outstanding arrears of €163,627 as at 31 December 2015, of which €98,078 are deemed collectable, could also not be confirmed. Analysis of the debtors' ageing was also hindered.

The Gozo General Hospital considers the amount of €88,768, *i.e.* 54% of the gross closing balance, to be recoverable through departmental action, €65,523 (40%) were reported as statute-barred, whilst the balance of €9,310 (6%) is deemed recoverable.

Ministry for Social Dialogue, Consumer Affairs and Civil Liberties

As *per* Return submitted by the Ministry for Social Dialogue, Consumer Affairs and Civil Liberties (MSDC), the opening balance of €13,917 was revised downwards by €723.

Arrears in respect of year 2015 amounted to €13,612, ending the year with a net collectable balance of €26,806, which can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	13,612
Amounts outstanding for over one but less than two years (2014)	13,194
Net Closing Balance	**26,806**

The foregoing amount comprises outstanding salary reimbursements amounting to €18,461 in respect of three employees transferred from MSDC to other Government Ministries. Although this amount was considered as recoverable by department action, MSDC confirmed that the process to write them off will commence in 2016.

An amount of €4,523 represents allowances and extra payments erroneously disbursed to three employees, which are being recouped by way of monthly salary deductions. The balance of €3,822, relates to salary overpayments.

Industrial and Employment Relations

Arrears due to the Department for Industrial and Employment Relations (DIER) consist of outstanding repayment of loans under the 'Self Employed Loan Incentive Scheme', which was introduced by Government in its 1989 budget, with the aim to assist individuals to start up a business enterprise. The scheme was terminated at the end of 1992.

The opening balance of €306,461 was due to DIER by 75 individuals who benefitted from the said Scheme which was terminated at the end of 1992. During the year under review, only 20 debtors forwarded payments, in aggregate amounting to €2,953, representing less than 1% of the foregoing opening balance. As reported

last year, the Department maintained a provision for doubtful debts of €195,686. This resulted in a net collectable figure of €107,822 at year-end, as analysed hereunder:

	€
Amounts outstanding for over ten but less than fifteen years (2002)	4,115
Amounts outstanding for over fifteen but less than twenty years (1996 – 1997)	26,438
Amounts outstanding for over twenty but less than twenty-five years (1993 – 1995)	77,269
Net Closing Balance	**107,822**

From the gross closing balance of €303,508, no amount was considered to be statute-barred and €265,183 representing 87% of the total was considered to be recoverable by department action.

During the year under review, reminders were once again sent to defaulters who had committed themselves to start effecting periodic payments, following the receipt of a legal letter in years 2011 and/or 2012.

Through its Legal Office and in consultation with the Office of the AG, in 2016 the Department had to evaluate and recommend what action can be taken after considering whether it is cost-effective to proceed with recouping the outstanding dues.

Ministry for the Economy, Investment and Small Business

The Ministry for the Economy, Investment and Small Business reported a gross outstanding balance of €457,823 relating to the following:

		€
a.	Malta Communications Authority (MCA) Arrears	222,431
b.	Ship Radio Licences	235,392
	Gross Closing Balance	**457,823**

Out of the gross amount reported under MCA arrears, €207,201 is considered as not collectable, and is made up of dues from companies which are either untraceable, in dissolution or "... *without a registration number* ...", as well as including other small amounts which are not economically feasible to chase. The remaining balance of €15,230, which in reply to Treasury Circular No. 12/2016, is still pending Court action, is analysed as follows:

	€
Amounts outstanding for over two but less than five years (2011 – 2013)	1,623
Amounts outstanding for over five but less than ten years (2006 – 2010)	11,702
Amounts outstanding for over ten years (– 2005)	1,905
Net Closing Balance	**15,230**

The balance of €235,392 in respect of Ship Radio Licences, relates solely to newly accrued arrears, generated within the same year. According to the Ministry, these amounts were collected by the Malta Maritime Authority, but not yet transferred to the former.

Malta Gaming Authority

The Malta Gaming Authority (MGA) reported a net outstanding arrears balance of €3,978,136 for the year ended 31 December 2015.

The opening balance of MGA stood at €1,977,923, whereby the gross closing balance reported in the 2014 ARR was €3,937,084, thus differing by €1,959,161. The Authority explained that the amounts reported as at 2015 were the ones payable to Government. MGA also stated that the aforementioned difference of almost €2 million "*... is made up of License fees due to the Authority which were not listed in this report as Agreed with MEIB ...*". However, no documentation was forwarded substantiating this statement.

Newly Accrued Arrears

The amount of €3,435,006 was reported as newly accrued, consisting of Tax Invoices issued during 2015, still due as at end of year. However, most of these arrears, result from timing differences between invoice and payment date. MGA explained that as stipulated by the Gaming Act, December 2015 duties are required to be paid by the 20th day of the following month.

Ageing Analysis

An ageing analysis of the gross outstanding arrears provided by MGA confirmed that the majority of arrears (83%) were outstanding for less than one year. Ageing of arrears is as follows:

	€
Amounts outstanding for less than one year (2015)	3,436,207
Amounts outstanding for over one but less than two years (2014)	265,128
Amounts outstanding for over two but less than five years (2011 – 2013)	131,125
Amounts outstanding for over five but less than ten years (2006 – 2010)	287,842
Gross Closing Balance	**4,120,302**

In reply to Treasury Circular No. 12/2016, this gross closing balance is further categorised as having the amount of €122,581 pending Court action, €1,722,565 considered as recoverable by department action, while €2,275,156 is also deemed recoverable.

Moreover, out of the €4.1 million gross balance, the amount of €142,166 is being considered as not collectable. This figure represents provisions for long outstanding tax dues originating from 22 operators. MGA stated that with respect to these operators, the Authority initiated enforcement and/or legal action to recoup such debts and to-date, €32,000 have in fact been collected.

Collection Efforts

The Authority follows its credit control policies and procedures in order to monitor the amounts due and take the necessary action to recoup them. Such policies and procedures include:

- e-mails and telephone reminders which are executed within the first 60 days from the invoice due date;
- amounts exceeding the first 60 days threshold are forwarded to the Defaulters' Committee for further action, which are later on forwarded to the Enforcement and Investigation Department if need be;
- the issuance of an Enforcement Letter requesting compliance within 15 days, otherwise an administrative fine is imposed by the Authority; and
- resorting to legal action as stipulated by the Gaming Act.

Malta Communications Authority

The net closing balance of €879,120 as reported by the Authority for the year ending 31 December 2015 is made up of the following:

		€
a.	Fees for rights of use	805,543
b.	Radio Communication Licence	73,577
	Net Closing Balance	**879,120**

This amount, which was also reported as newly accrued arrears, is made up of dues generated within the same year. Moreover, in reply to Treasury Circular No. 12/2016, such balance is fully recoverable, with no departmental action necessary.

Television Licensing Unit

Net arrears due to Government falling under the responsibility of the Television Licensing Unit (TVLU) as at 31 December 2015, were reported as €4,024,572.

NAO was informed that with effect from April 2016, the files pertaining to TVLU, which during 2015 was under the remit of the Ministry for the Economy, Investment and Small Business, were transferred to the new Ministry for Competitiveness and Digital, Maritime and Services Economy. Because of this transition, NAO was not provided with the requested documents and consequently the necessary testing could not be carried out.

Amounts estimated as not collectable

A total of €6,036,857, representing approximately 60% of gross collectable arrears, was reported as not collectable. In reply to Treasury Circular No. 12/2016, TVLU stated that such balance was deemed as statute-barred, given that it is composed of dues outstanding for over five years.

Amounts written off

The sum of €13,992 was reported as being written off, however, no supporting documents were made available, and thus the necessary verifications could not be carried out by this Office.

Ageing Analysis

The ageing analysis of the net collectable balance of €4,024,572 could not be reported upon in this year's Report, since as stated above, no information was made available.

Commerce

The following is a sub-classification of the gross closing balance of arrears as reported by the Commerce Department in the 2015 ARR:

		€
a.	Trade Licences	2,769,236
b.	Miscellaneous Receipts	11,187
c.	Penalties by Students	7,549
	Gross Closing Balance	**2,787,972**

Out of the total gross outstanding arrears in relation to trading licences, the amount of €1,203,014 related to active licences, whilst the balance of €1,566,222 consisted of licences in the process of being withdrawn/ cancelled or already withdrawn.

Amounts considered as not collectable

It was noted that the amounts considered as not collectable in relation to trade licences have decreased during 2015 to €1,152,047, from the previous year's balance of €1,498,824.

The Department adopted the same technique for calculating these amounts as it did in previous years. Older debtors, which had a lower probability of collection, were linked to a lower percentage of collectability. In fact, it was estimated that 50% of the amounts due from 2002 to 2011 would not be collected. Lower percentages (20% to 40%) were provided on arrears relating to more recent years, denoting a larger probability of collection.

During 2015, a provision has also been made in relation to miscellaneous receipts. The amount estimated as not collectable of €4,697 related to travel claims for 2013 and 2014, which had not been reimbursed by the end of 2015.

A 100% provision, amounting to €7,549, was applied to fees relating to two students who had participated in a student-worker placement in the 1980s but who had resigned before the stipulated time, without ever refunding the relevant amounts.

Public Accounts Committee Request

Submissions by the Department following the requirements of Treasury Circular No. 12/2016, further revealed that out of gross collectable arrears, the amount of €763,843 is deemed to be statute-barred. As detailed above, this amount relates to 50% of the trade licences due for more than five years (€756,294), as well as the total balance of penalties by students (€7,549).

A further amount, equivalent to net collectable arrears (€1,623,678) was deemed as recoverable, whilst the remaining balance of €400,449 was deemed to be not statute-barred, in spite of the fact that it was reported in ARR as part of the amount estimated as not collectable.

Ageing Analysis

A detailed analysis of net collectable arrears was computed by NAO on the basis of information provided by the Commerce Department as follows:

	€
Amounts outstanding for less than one year (2015)	228,716
Amounts outstanding for over one but less than two years (2014)	202,924
Amounts outstanding for over two but less than five years (2011 – 2013)	435,743
Amounts outstanding for over five but less than ten years (2006 – 2010)	507,101
Amounts outstanding for over ten but less than fifteen years (2001 – 2005)	249,194
Net Closing Balance	**1,623,678**

Revisions

In the 2015 ARR, the Department declared total revisions of €815,497 in respect of Trading Licences, which was significantly larger than the same figure for 2014, reported as €19,230. Information provided revealed that the majority of this amount related to fees which were declared as not due during 2015 (€694,627), and fees which were never due as a result of a declaration regarding a reduction in footprint (€90,952), following amendments to the trade licensing legislation in 2012. Also, part of revisions were licences suspended during 2015 (€19,668), licences which were in the process of being written off (€1,593) and a balance of €8,658, which was attributed to the discrepancy between the 2015 net collectable arrears as stated in the ARR, and the actual arrears figure extracted from the Licensing Management System (LMS), net of provision for bad debts. The Department has also confirmed that the exercise to split arrears between fees which were actually due, and fees which were never due, was completed during 2015.

Amounts written off

Amounts written off during the year amounted to €9,808. Following an analysis of the related breakdown provided by the Department, it transpired that approvals in relation to write-offs amounting to €9,789 were made prior to 2015. Clarifications received revealed that LMS did not permit certain records to be kept. However, following an extensive exercise carried out over the years 2014 and 2015 where records were examined, LMS was updated accordingly.

Collectability of Trading Licences

During 2015, the trade licences website has been enhanced to allow licencees to update their correspondence details after a successful payment online or through a generic e-mail address. This enhancement also included the possibility of printing renewals in both the Maltese and English languages. Such improvements were intended to ensure that trade licence renewal notices are sent in an understandable language to the correct address, and help secure relevant payments. The total number of requests received through these channels amounted to 1,086.

Furthermore, a total of 16,192 renewal notices were also issued throughout 2015, whilst in November, 2,592 licencees who had failed to settle their fees in relation to 2015, were served with a letter from the AG, requesting arrears due.

During 2016, a total of 3,514 renewal notices were sent by e-mail and reminders were sent to those who failed to settle the amounts due.

Ministry for Home Affairs and National Security

Armed Forces of Malta

The gross closing balance as at 31 December 2015, disclosed by the Armed Forces of Malta in its amended ARR, stood at €599,556 and can be analysed as indicated hereafter:

		€
a.	Patrol Craft Conveyance	79,055
b.	Hire of Vehicles	173
c.	Security Duties	507,381
d.	Services Rendered	5,216
e.	Wages Refund	4,149
f.	Helicopter Services	361
g.	Sundry Services	3,221
	Gross Closing Balance	**599,556**

In line with Treasury Circular No. 12/2016, the majority of the outstanding balance, *i.e.* €590,346 is recoverable by department action, whilst €7,850 is under contestation and the remaining amount is estimated as not collectable since it is statute-barred. The remaining net closing balance of €598,196 can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	397,035
Amounts outstanding for over one but less than two years (2014)	96,967
Amounts outstanding for over two but less than five years (2011 – 2013)	11,301
Amounts outstanding for over five but less than ten years (2006 – 2010)	77,281
Amounts outstanding for over ten but less than fifteen years (2001 – 2005)	7,762
Amounts outstanding for over fifteen years (– 2000)	7,850
Net Closing Balance	**598,196**

Police Department

The Police Department reported a gross closing balance amounting to €362,079, for the year ended 31 December 2015, comprising:

		€
a.	Miscellaneous Fines (Airline and Shipping Companies)	17,995
b.	Services to Third Parties (Extra Duty)	12,760
c.	Sporting Licences (Weapons)	315,409
d.	Other Revenue	15,915
	Gross Closing Balance	**362,079**

With regard to sporting licences, NAO was advised that software for a new computer system was being tested as at time of audit, thus the ageing report was still not available. From the total of €315,409, an amount of €62,540 is estimated as not collectable, leaving a net closing balance of €252,869.

According to the Police Department, in 2016 letters were sent, requesting sporting licences falling in arrears to be paid by a specific date. The Department considers the amount of €157,896 from the gross closing balance to be recouped through department action, whilst €166,090 was reported as statute-barred and a further €22,405 pending Court action. The remaining balance is considered to be recouped without intervention.

NAO noted that individuals are still being invoiced for the annual fee for sporting licences even though they have outstanding amounts. However, the Police Department confirmed that the respective licence is not issued unless all arrears are settled.

Sporting licences totalling €62,540 were initially recorded in the Return as written-off in financial year 2015. A sample of 45 individuals with the highest amounts of debts was verified. However, the respective write-off approval was not sought as required by the General Financial Regulations. Therefore, upon NAO's recommendation the Return was amended accordingly.

Ministry for Finance

The gross/net closing balance as at 31 December 2015, as provided by MFIN, consists of:

		€
a.	Quality Assurance Unit	15,246
b.	Training	3,600
c.	Miscellaneous Reimbursement	967
	Gross/Net Closing Balance	**19,813**

As reported last year, the Department has yet to recover a prepayment of €3,600, made towards training courses which did not materialise during 2012, as well as €967 which has been outstanding for over 10 years. An amount of €8,641 was reported as newly accrued arrears. These pertained to registration fees for 2015.

An ageing analysis of the collectable arrears is as follows:

	€
Amounts outstanding for less than one year (2015)	8,641
Amounts outstanding for over one but less than two years (2014)	1,421
Amounts outstanding for over two but less than five years (2011 – 2013)	7,994
Amounts outstanding for over five but less than ten years (2006 – 2010)	790
Amounts outstanding for over ten years (– 2005)	967
Gross/Net Closing Balance	**19,813**

Treasury Department, Salaries and Pensions Section

The outstanding balance of arrears as at 31 December 2015, disclosed by the Treasury Department, Salaries and Pensions Section, consists of:

		€
a.	Cost sharing regarding Treasury Pension	34,382,609
b.	Refunds of Deceased Pensioners	25,868
c.	Special Cases	32,358
d.	Overpayments to Pensioners	11,858
	Gross Closing Balance	**34,452,693**

During the year, the sum of €1,028,626 was collected, representing 3.53% of the opening arrears balance as at 1 January 2015. This represents an increase over the equivalent amount collected in 2014, which represented 2.28% of the then opening balance.

Cost sharing

This consists of amounts due from Public Entities in respect of arrears from all Entities that employed officers, who on the date of retirement had the right for a Treasury Pension. The Department confirmed that statements of amounts due are being sent annually and payments are being received accordingly.

During testing, NAO noted that an amount of €2,575,722 was reported as an upward revision to this revenue category. To this effect, the Department confirmed that balances reported in the 2014 ARR were erroneously understated. Following a meeting at NAO, held on 3 October 2016, this Office was informed that as from 2016, the Department increased its efforts in order to minimise the possibility of such errors in the future.

Ageing of Debtors

The ageing of the Department's debtors is categorised as follows:

	€
Amounts outstanding for less than one year (2015)	3,710,724
Amounts outstanding for over one but less than two years (2014)	3,036,602
Amounts outstanding for over two but less than five years (2011 – 2013)	9,131,516
Amounts outstanding for over five but less than ten years (2006 – 2010)	15,143,591
Amounts outstanding for over ten years (– 2005)	3,430,260
Net Closing Balance	**34,452,693**

Inland Revenue Department

The Inland Revenue Department (IRD) reported a gross arrears balance of €965,462,462 in its ARR for the year ended 31 December 2015.

The gross opening balance reported in the 2015 ARR in relation to Tax Pre '99 and the Self-Assessment System, did not tally to the gross closing balances reported in the previous year by €3,929,807 and €33,130,021, respectively. According to correspondence from the Department, the re-statement of the opening balances was made as a consequence of changes in the Department's remits. In fact, as opposed to previous years, the Return does not include business carried out by the International Taxation Unit. All incoming funds, including collection of outstanding balances are carried out at that end. IRD stated that, "... *This segregation has already been discussed with the Accountant General vis-à-vis the exercise to change to Accrual Accounting* ...".

The following is a sub-classification of the gross closing balance of arrears as reported by the Department in its ARR:

	€
Pre '99 System (Up to Year of Assessment 1998)	157,179,926
Self-Assessment System (Post Year of Assessment 1998)	479,151,384
Final Settlement System (Employers)	90,034,103
Social Security Contributions Class 1 (Employers)	157,668,485
Social Security Contributions Class 2 (Self-Employed/Occupied)	81,428,564
Gross Closing Balance	**965,462,462**

Collectability of Arrears

Out of the gross balance, the amount of €750,976,374 was considered as not collectable, thus resulting in net collectable arrears of €214,486,088.

The highest instance of uncollectability related to the Self-Assessment System (Post Year of Assessment 1998). In fact, out of the gross arrears of €479,151,384, a total of €397,776,933 were deemed to be uncollectable. Workings provided by the Department showed that 70% of Assessed Tax and 90% of Estimations, were considered as amounts estimated as not collectable.

Pre '99 balances were also tagged with a high percentage of uncollectability amounting to 90%, which resulted in an estimated not collectible amount of €141,461,933. The percentage increased by 10% since last year's review denoting a lesser probability of collection.

With regards to the Final Settlement System and Social Security Contributions (Class 1), the non-collectability rate stood at 70% and 49.3% respectively and resulted in provisions for bad debts of €63,023,872 and €81,230,627. These percentages remained unchanged from last year's review. Furthermore, all balances owed in relation to Class 2 Contributions that are older than five years, were considered as not collectable.

Ageing Analysis

The ageing of the net collectable arrears can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	38,882,880
Amounts outstanding for over one but less than two years (2014)	27,697,928
Amounts outstanding for over two but less than five years (2011 – 2013)	53,883,970
Amounts outstanding for over five but less than ten years (2006 – 2010)	39,779,306
Amounts outstanding for over ten but less than twenty years (1996 – 2005)	45,086,013
Amounts outstanding for over twenty years (– 1995)	9,314,114
Net Closing Balance	**214,644,211**

The total of the ageing analysis differs from the net collectable arrears in the ARR by €158,123. This amount relates to payments collected by IRD in connection with the Pre '99 system collection schemes, which amount could not be set off against the balance due in any particular year, therefore it was omitted from the ageing analysis.

Efforts to Collect

The Department provided NAO with a detailed analysis of the gross arrears amount pertaining to the Self-Assessment System (€479,151,384) as a percentage of gross tax charged on a yearly basis since 1999. It was verified that in total, this percentage stood at 4.45%.

Moreover, IRD provided this Office with information in relation to its actions and planned efforts to collect the overdue amounts during the first six months of 2016. During this period, the Department issued a number of assessments (273), statements of pending balances (7,401), as well as notices in relation to Social Security Contributions (521) and the Final Settlement System (3,648). The Department has also issued a number of default notices in relation to existing repayment agreements.

Planned action also included sending notices with respect to repayment agreements which were in default, preparation for and attendance to Court sittings, as well as remitting interest agreements and other instalment plan agreements, involving the review by an internal Board to ascertain consistency and equity.

Capital Transfer Duty Department

The gross closing balance as reported by the Capital Transfer Duty Department in its ARR ending 31 December 2015 consists of:

		€
a.	Duty on Documents	24,575,306
b.	Death and Donation	4,623,441
	Gross Closing Balance	**29,198,747**

Out of this gross closing balance, of which €13,026,542 were reported as being under contestation, the amount of €21,990,892 was considered as not collectable, thus resulting in net collectable arrears pertaining to Duty on Documents and Death and Donation of €6,329,401 and €878,454 respectively.

Ageing Analysis

The outstanding balances can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	2,113,608
Amounts outstanding for over one but less than two years (2014)	75,972
Amounts outstanding for over two but less than five years (2011 – 2013)	247,206
Amounts outstanding for over five but less than ten years (2006 – 2010)	762,573
Amounts outstanding for over ten but less than fifteen years (2001 – 2005)	3,322,260
Amounts outstanding for over fifteen but less than twenty years (1996 – 2000)	27,884
Amounts outstanding for over twenty years (– 1995)	669,990
Net Closing Balance	**7,219,493**

The difference of €11,638 between the net closing balance included in the ARR and the ageing analysis provided to NAO was due to a timing difference between the issue of both reports.

Amounts under Contestation

Amounts under contestation amounting to €13,026,542, are mainly made up of Duty on Documents, for a total of €11,257,394, which majority are statue-barred. On the other hand, the remaining amount pertaining to Death and Donation Duty remained the same as in the previous year, since no new claims were issued. The likelihood that these amounts are collected is very remote.

Amounts considered as not collectable

The dues estimated as not collectable amounted to €21,990,892 in 2015. This consists of a provision of approximately 10% for newly accrued arrears that remained unpaid by the end of 2015, and a substantial 80% of the remaining arrears which are older than one year.

Collection Efforts

The Collection and Legal Sections within the Department are constantly monitoring the outstanding balances and taking necessary action. These balances are IT controlled, thus ensuring that timely action is taken and no legal steps are bypassed.

During 2015, numerous reminders (1,167), as well as 324 letters from the Legal Unit were sent to various debtors. Furthermore, the Department proceeded with 70 Garnishee Orders and 172 legal action warnings.

Value Added Tax Department

The following is a sub-classification of the gross closing balance of arrears as reported by the Value Added Tax (VAT) Department in its ARR for the year ending 2015:

		€
a.	VAT (1998)	1,444,494,614
b.	VAT (1995)	14,411,911
c.	Customs and Excise Tax	6,464,178
d.	Eco-Contribution	9,174,375
e.	Refund to Government on stocks – 1997	620,381
	Gross Closing Balance	**1,475,165,459**

The amount of €620,381 represents debts due to the Department, accruing from stock on which VAT was due following the changeover to Customs and Excise Tax in 1997. However, no breakdown of such amount was available, as was reported in previous year's Annual Audit Report. On further enquiry as to what action is being taken to recoup these amounts, the VAT Department claimed that during 2007, demand notices were sent to all defaulters, resulting in very few payments made. Due to the lack of resources at the time, coupled with the fees involved to take legal action, it was decided to focus on more recent and collectable amounts.

Net collectable arrears amounted to €72,775,406 after deducting a balance of €1,402,390,053, which is estimated as not collectable by the Department.

Whereas write-offs during the year amounted to €1,865, a total balance of €339,625,706 was reported as not due in the VAT Department's ARR, representing cancellations of assessments, penalties, estimations and interest, following the submission of declarations by taxpayers.

As reported in previous years, no ageing analysis of net collectible arrears could be provided. Moreover, the Department did not send any data in the end of year Debtors template sent to Treasury. Therefore, NAO could not note the link between such template and the ARR submitted by the VAT Department.

Public Accounts Committee Request

In reply to this request, the Department stated that the gross closing balance includes all the accumulated estimated, declared and assessed tax, as well as penalties and interest from 1999 to date. Moreover, all figures are approximate since they may fluctuate substantially due to the appropriation rules and the transfer of credits from one period to another. In the case of estimations, these are replaced with the declared amounts by taxpayers in their returns, which could vary considerably.

The VAT Department also confirmed that a total of €27,913,035 is pending Court action, whilst although it reported a total of €44,862,371 as recoverable by the Department, this figure also includes amounts relating to VAT (1995), Customs and Excise Tax and Refund to Government on stocks, "... *that are very remotely collectable as they are aged debts*".

Customs Department

The 2015 net closing balance of arrears, amounting to €13,236,938, as provided by the Customs Department, is analysed as follows:

		€
a.	Import and Export Duties	12,206,487
b.	Licences, Taxes and Fines	306,281
c.	Fees of Office	2,407
d.	Reimbursements	721,763
	Net Closing Balance	**13,236,938**

Past Arrears Collected

The Customs Department collected a total of €33,290,585 of which €32,766,683 pertained to excise duties on fuel.

Amounts under Contestation

The Department reported an aggregate amount of €6,890,109 for a number of cases whereby the related amounts were undergoing Court proceedings. Notwithstanding this, only a balance of €1,048 featured under 'Estimated Amount considered as not collectable'. The Department stated that "... *it is believed that contested amounts ought to be included with the collected amount*."

To this effect, the Customs Department also stated that since the majority of the amounts due relate to Court cases, including appeals on the original decision, it is very difficult to assess the likelihood of the collection or non-collection of dues. The Department further remarked that "... *Cases, particularly the ones involving hefty amounts, take decades to be decided* ..." and even when they are eventually won, the Department "... *would need to institute recovery proceedings dragging the collection process further* ...". Additionally, "... *When cases linger over decades, usually there will be no assets left to make recovery possible*".

Unless the amounts in arrears are being contested in the Courts, and reminders fail to be successful, Customs proceeds to block the Economic Operator Registration Identification number in the electronic systems, in order to disable the ability of the respective merchant to import or export any consignments. When even this measure proves to be futile, judicial action is instigated. Members of the Enforcement Unit call at the premises of the company/individual in cases where amounts are relatively small and judicial action is not deemed to be cost-effective.

Ageing Analysis

The ageing of the net collectable arrears can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	2,935,978
Amounts outstanding for over one but less than two years (2014)	198,744
Amounts outstanding for over two but less than five years (2011 – 2013)	2,848,642
Amounts outstanding for over five but less than ten years (2006 – 2010)	6,047,928
Amounts outstanding for over ten but less than fifteen years (2001 – 2005)	1,140,159
Amounts outstanding for over fifteen but less than twenty years (1996 – 2000)	25,571
Amounts outstanding for over twenty years (– 1995)	39,916
Net Closing Balance	**13,236,938**

Department of Contracts

The outstanding gross closing balance of €259,135, as reported by the Department of Contracts as at 31 December 2015, consisted of penalties and damages due by seven contractors.

Total dues of €13,579 were collected during the year from two contractors by means of monthly instalments, whilst an amount of €21,749 owed by another contractor was written off, after obtaining appropriate covering approval.

Estimated Amounts Considered as Not Collectable

A balance of €20,510, pertaining to only one contractor, was reported as considered as not collectable for 2015, even though in its submission to Treasury Circular No. 12/2016, the Department reported that a balance of €8,438 was statute-barred, and additional amounts due by two contractors, totalling €71,822, were pending Court action. When queried, the Department stated that, "*Considering that it is still not definite what course of action we shall take in the cases ... ... we opted to consider them as collectible, at least until we decide to request their writing off*".

Ageing Analysis

The resulting net collectable arrears of €238,625, as forwarded by the Department of Contracts is analysed as follows:

	€
Amounts outstanding for less than one year (2015)	105,865
Amounts outstanding for over one but less than two years (2014)	-
Amounts outstanding for over two but less than five years (2011 – 2013)	48,050
Amounts outstanding for over five but less than ten years (2006 – 2010)	33,823
Amounts outstanding for over ten years (– 2005)	50,887
Net Closing Balance	**238,625**

Ministry for Energy and Health

Health

The gross closing balance of €8,599,272 as at 31 December 2015, is made up of the following amounts:

		€
a.	Primary Health Care (PHC)	2,622
b.	Sir Anthony Mamo Oncology Centre (SAMOC)[4]	72,823
c.	Hospital Fees: St. Luke's Hospital	237,029
d.	Hospital Fees: Mater Dei Hospital (MDH)	3,422,905
e.	Sundry Bills: MDH	2,089,796
f.	Resignations and Overpayments: MDH	247,830
g.	Licences	38,219
h.	Ship Sanitation	13,987
i.	Breach of Contract	2,278
j.	European Union Countries E125 Claims	753,756
k.	European Union Countries E127 Claims	520,618
l.	Central Procurement and Supplies Unit (CPSU)	1,197,409
	Gross Closing Balance	**8,599,272**

From the gross receivable at year-end, an amount of €72,939 is being estimated as not collectable, leaving a net closing balance of €8,526,333, as analysed hereafter. However, considering that some dues are long outstanding and despite clear indications that there are more unrecoverable amounts, one can conclude that the provision, mainly relating to SAMOC, is understated. The Ministry is expected to determine the actual amount that is actually considered as unrecoverable.

The net collectable arrears forwarded by the Ministry can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	4,304,052
Amounts outstanding for over one but less than two years (2014)	1,737,601
Amounts outstanding for over two but less than five years (2011 – 2013)	1,442,110
Amounts outstanding for over five but less than ten years (2006 – 2010)	738,059
Amounts outstanding for over ten but less than fifteen years (2001 – 2005)	222,721
Amounts outstanding for over fifteen years (– 2000)	81,790
Net Closing Balance	**8,526,333**

Following testing carried out by NAO, four Returns namely that of CPSU, PHC, SAMOC and the Ministry were revised. Furthermore, amended versions of Appendix A as required by Treasury Circular No. 12/2016 had also to be resubmitted, for both PHC and the Ministry, following NAO's initial review. The consolidated data shows that €7,918,205 representing 92% of the total amount due was considered recoverable by departmental action. No intervention was required for the amount of €608,244 to be collected, whilst the majority of the amount considered as not collectable was statute-barred.

[4] Previously reported under Sir Paul Boffa Hospital.

Sir Anthony Mamo Oncology Centre

Out of the amount of €72,823 considered as not collectable, a total of €68,840 has been long outstanding. Although the respective five foreign patients are not traceable, the amounts in question have not yet been written off.

Mater Dei Hospital

The opening balances reported as at 1 January 2015 are not correct, since proposed adjustments made by this Office last year had not been taken into consideration. NAO still attempted to reconcile the ancillary data obtained from MDH to the amounts reported in the Return, but such process was futile since not all supporting documentation was submitted. An aged debtors report to corroborate the amounts recorded in the Debtors' Analysis was also not provided.

It was noted that negative balances in the debtors' spreadsheet were being netted off with outstanding amounts, thus understating the year-end balance reported in the Return. No explanation was provided for such negative balances.

MDH also have amounts that, although their collectability is remote, no provision has been taken.

Department for Health Regulation - Licences

This Office was informed that in January 2015, action was taken by the Healthcare Standards Directorate in order to avoid the accumulation of further arrears in relation to licensing of establishments. The main changes include the introduction of online payment and that a licence is now only being issued to a client upon payment.

Entitlement Unit

Invoices raised and settled during the year under review, *i.e.* 2015, were incorrectly included under the columns of past arrears collected and newly accrued arrears, resulting in overstated figures. An exercise was then carried out by the officer in charge, assisted by an NAO official to submit a revised Return and Debtors' Analysis.

Central Procurement and Supplies Unit

As from 2015, CPSU started billing St. Vincent de Paul Residence for the supply of medicinal and surgical devices to its pharmacy, given that it now falls under the responsibility of a different Ministry.

From documentation provided, though CPSU made various attempts to recoup the outstanding balance of €1,197,409, no amounts were collected; as a result, these will eventually be written off.

Ministry for the Family and Social Solidarity

Social Security Benefits

The Department of Social Security (DSS) reported a figure of €24,030,448 as gross arrears in the ARR in relation to Social Security Benefits for the year ending 2015.

An analysis of the amounts pertaining to each benefit/assistance, as provided by DSS, can be summarised as follows:

		€
a.	Social Assistance	13,748,956
b.	Retirement Pension	2,371,401
c.	Widows Pension	1,930,230
d.	Children's Allowance	1,602,157
e.	Old Age Benefits	1,772,712
f.	Medical Assistance	1,334,711
g.	Invalidity Pension	569,194
h.	Disability Pension Benefits	315,811
i.	Short Term Benefits	249,833
j.	Contributory Bonus	44,995
	Total	**23,940,000**

When comparing the total figure of this analysis to the net collectable figure as *per* ARR, a discrepancy of €2,047,926 was noted. Follow-ups with DSS revealed that the reason behind this difference is that, "... *the running of the reports take some time to be processed in the SABS*[5] *system*. *In the meantime any user can be logged into the system and carrying out transactions*. *This results in the changes in debtors' balances and will affect the reports*."

Past Arrears Collected

Similar to last year's review, no breakdown was available in relation to past arrears collected, which amounted to €2,349,045. In fact, correspondence with DSS confirmed that this figure was taken from the summary report and that the detailed report in its regard was under development during 2016.

Revisions

Revisions featuring in the ARR amounted to €353,455. Of this, €273,232 has been recorded during 2015 as a downward revision since no source of information was found when the respective personal files were reviewed. This amount used to feature in previous years' Annual Audit Reports as a discrepancy between the net collectable arrears and the respective Debtors' templates since it related to past debtors, which were never included in SABS, but were included for reporting purposes in the Debtors' Listing.

Additional revisions amounting to €20,552 were also selected for the purposes of this review, with adjustments to the amounts due being duly justified.

Newly Accrued Arrears

Eight new overpayments, which in total amounted to €364,005 were selected for testing purposes.

In five of the selected instances, amounting in total to €241,714, the claimants were still in receipt of benefits even though they had undeclared property through which they exceeded the allowable capital. In a separate case, the overpayment amounting to €39,617, was created because the claimant had been employed whilst still in receipt of Unemployment Assistance.

[5] Social Assistance and Benefits System

Three of these six cases were not registering regular repayments, however the corresponding files and correspondence with DSS revealed that such cases are being followed-up accordingly either internally within the Department or by means of Legal Letters. Furthermore, in two separate cases, follow-ups with the Inferior Court of Appeal are being made.

A separate overpayment, amounting to €40,039, was created when an investigation revealed that the claimant had been employed since 2006 whilst still in receipt of various benefits. It also transpired that whilst a repayment plan has been set-up with the beneficiary, a balance of €39,539 remains pending. Furthermore, the last repayment date listed on SABS was in November 2015 and no further repayments were traced since then. Following enquiry with the Department, it transpired that the current monthly repayments are being set off against a separate overpayment in Unemployment Assistance, and that when this amount is fully repaid the amount due in relation to Invalidity Pension will start being reduced accordingly.

The Department's decision in relation to the remaining overpayment tested of €42,636 has been reversed on appeal.

Write-offs

A sample of five write-offs, totalling €58,586 was selected for testing purposes. This represented 48% of total write-offs of €122,334, as extracted by the Department at the end of December 2015.

NAO noted that in two instances, no formal approval by the Permanent Secretary and/or MFIN was sought by the Department prior to the write-off adjustment, as required by the General Financial Regulations, even though one of these write-offs, relating to Widows' Pensions, amounted to €9,881.

Estimated amounts considered as not collectable

The ARR reported a figure of €2,138,374 in relation to amounts estimated as not collectable. From DSS' submission in relation to Treasury Circular No. 12/2016, it transpired that this figure related to amounts, which are statute-barred.

Same submission also reported a figure of €1,042,246 in relation to amounts which were the subject of judicial letters issued during 2015 on overpayments created during 2014 and previous years, as well as a further €2,499,066, which was deemed to be recoverable after departmental action (through reminder letters and/or phone calls). The amounts making up the latter figure were also the subject of intimation letters issued during 2015.

Ageing Analysis

A detailed analysis of gross collectable arrears was provided by DSS as follows:

	€
Amounts outstanding for less than one year (2015)	6,572,753
Amounts outstanding for over one but less than two years (2014)	4,254,120
Amounts outstanding for over two but less than five years (2011 – 2013)	6,825,571
Amounts outstanding for over five but less than ten years (2006 – 2010)	4,807,284
Amounts outstanding for over ten years (– 2005)	1,570,720
Gross Closing Balance	**24,030,448**

Collection Efforts

In its submission relating to Treasury Circular No. 12/2016, DSS also reported a figure of €18,350,762 under the category of amounts that are recoverable without departmental action. This figure includes the amount of €13,185,057 relating to years 2011 until 2015, which is being recovered by instalments.

Additionally, DSS stated that in terms of the Social Security Act, the Department recoups the outstanding overpayments by withholding overpaid sums from the benefits or pensions payable to a beneficiary. The rate of recovery is restricted to be no less than the equivalent of 5% or 10% depending on the cause of the overpayment. In the case of fraud or misrepresentation by a beneficiary, the rate of recovery goes up to 30%.

Elderly and Community Care

The Elderly and Community Care Department (ECCD) reported a net collectable balance of €4,281,045, which balance was on the same line as the amount reported by the Department for the year ended 31 December 2014.

The ARR submitted by the Department incorporates the following revenue categories:

		€
a.	Staff Salaries reimbursement	4,179,799
b.	Revenue Account	99,216
c.	Telephone	949
d.	Training	776
e.	Commission receivable	305
	Net Closing Balance	**4,281,045**

Whilst no amounts were reported as estimated as not collectable in the 2015 ARR, only a balance of €24,935 was recouped during the year, which pertained to the Revenue Account.

Staff Salaries

The amount of €4,179,799, which represents 98% of total arrears as at 31 December 2015, relates to staff salaries due from various Government Departments in relation to staff seconded by ECCD. In reply to Treasury Circular No. 12/2016, ECCD stated that it is in the process of writing off this amount after seeking approval by the relative authorities.

Revenue Account

This account receives the amount of 60% collectable from residents in Public Private Partnership homes with respect to other income, in the form of interest, receivable by the residents. DSS identifies any other income earned by the various residents within said homes, and through a shared software, the ECCD is able to calculate the total amount due in line with the provisions of Legal Notice 259 of 2004.

As at December 2015, a total of €99,216 was due.

Newly Accrued Arrears

A breakdown of the newly accrued arrears for 2015 amounting to €77,683 was requested by NAO. However, this was unavailable from the Department's end.

A substantial decrease of this amount was noted when compared to the newly accrued arrears of 2014. This was due to the fact that in 2015, ECCD did not issue an invoice for the reimbursement of staff salaries for personnel who are on the payroll of St. Vincent de Paul Residence, but perform duties in other departments, such as Karin Grech Rehabilitation Hospital (KGRH). As from the coming year, ECCD and KGRH "... *agreed to transfer to KGRH books all the staff that perform duties there in order to avoid this hassle of invoicing*".

Ageing Analysis

The outstanding balances can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	102,527
Amounts outstanding for over one but less than two years (2014)	1,133,666
Amounts outstanding for over two but less than five years (2011 – 2013)	2,295,636
Amounts outstanding for over five but less than ten years (2006 – 2010)	749,216
Net Closing Balance	**4,281,045**

Ministry for Culture, Justice and Local Government

Judicial

The CoJ Department has informed this Office that as from January 2016, the new E-Fees system, relating to Court fees, was introduced instead of the CORTEX system. On the other hand, reports with respect to fines are still issued from the LECAM system.

From the opening balance of €11,008,493, the amount of €1,285,436 was collected (*i.e.* 12%), whilst the net downward revision amounted to €1,532,419. Details of such revision is given further down in this write-up. During the year under review, the newly accrued arrears totalled to €1,780,251.

Approvals were obtained to write off the total amount of €110,879. The majority of the amount consists of fines under €100 where in most cases, it was difficult to trace the defaulter or the time lapse made the amount difficult to recoup.

The gross closing balance as at 31 December 2015 reported in the Return and which have been analysed hereunder, amounted to €9,860,010. Further details are given separately further on in the Report, under the pertinent sub-title. The Department considers the amount of €6,787,856, *i.e.* 69% of the said gross closing balance, to be recouped through department action, whilst €163,483 (1.7%) was reported as statute-barred and €2,819,219 (29%) pending Court action. The Department should find no problem to recoup the remaining €89,452 without any intervention.

		€
a.	Fines: Criminal – Judges Superior Courts	3,606,123
b.	Fines: Criminal – Magistrates Inferior Courts	4,074,123
c.	Fines: Civil – Superior Registry	23,497
d.	Fines: Civil – Inferior Registry	29,337
e.	Fees	2,126,930
	Gross Closing Balance	**9,860,010**

An amount of €163,483 was considered uncollectable as at year-end, as explained further on in this Report, bringing the net collectable amount due from individuals down to €9,696,527, out of which, by end of January 2016, the amount of €115,575 was recouped. The ageing of net debtors as at year-end can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	1,780,250
Amounts outstanding for over one but less than two years (2014)	1,418,023
Amounts outstanding for over two but less than five years (2011 – 2013)	1,253,864
Amounts outstanding for over five but less than ten years (2006 – 2010)	856,862
Amounts outstanding for over ten but less than fifteen years (2001 – 2005)	846,325
Amounts outstanding for over fifteen but less than twenty years (1996 – 2000)	3,369,208
Amounts outstanding for over twenty years (1969 – 1995)	171,995
Net Closing Balance	**9,696,527**

Court Fines

Criminal – Judges Superior Courts

The opening balance of €4,762,454 for 2015, was revised downwards by €1,303,972. According to CoJ, this revision was mainly due to the reasons depicted in *Table 2*.

Table 2: Revisions

Reasons	Amounts
	€
5 fines erroneously omitted from last year's Return	47,831
6 fines relating to previous years but imposed in year 2015	8,901
34 fines, including one of €1,141,288, converted into imprisonment	(1,358,050)
A fine which is no longer due following Act No. XIV of 2013, an Act to amend the VAT Act, Cap. 406	(2,054)
A cancelled fine and a revoked fine	(600)
Net Downward Revision	**(1,303,972)**

During 2015, the amount of €133,081, *i.e.* less than 3%, was collected, whilst the newly accrued arrears amounted to €280,722. Out of the remaining €3,606,123 gross closing balance, the amount of €32,462 (*i.e.* 0.9%) relates to 11 fines due from untraceable debtors and hence, they are being considered as not possible to recoup, leaving a net collectable balance of €3,573,661.

From the outstanding balance, the amount of €2,819,219, *i.e.* 79%, is due from only three individuals, representing three fines imposed in 1998, each owing the sum of €939,740.

Criminal – Magistrate Inferior Courts

In its ARR for year 2015, CoJ indicated a downward revision of €145,354 to the opening balance of €3,960,586. The reasons for this variance are depicted in *Table 3*.

Table 3: Revisions

Reasons	Amounts
	€
34 fines relating to previous years but imposed in year 2015	38,288
26 fines that were inflicted in the past but were erroneously not recorded in the system	9,139
5 fines which were revised upwards, mainly because they were paid but ultimately revoked	3,167
166 fines converted into imprisonment	(143,163)
116 revoked fines, one of which amounted to €23,294	(38,891)
Various adjustments to the opening balance, mainly due to problems encountered in the faulty system	(11,565)
6 cancelled fines	(2,329)
Net Downward Revision	**(145,354)**

During the year under review, CoJ collected the amount of €914,620, whilst the newly accrued debtors amounted to €1,267,718. Write-off approvals were obtained for the amount of €94,207.

The gross closing balance of €4,074,123 included the amount of €131,022 relating to fines that are considered as not possible to be recouped, since the majority of them are due from untraceable debtors, leaving a net collectable balance of €3,943,101.

Civil – Superior Registry

The opening balance of €27,781, was revised downwards by €4,200, mainly due to 31 revoked fines by a Court decree.

During the year under review, the amount of €2,974 was collected whilst €2,890 was newly accrued, resulting in an outstanding balance of €23,497 as at year-end.

Civil – Inferior Registry

Twenty-nine fines (€7,320) that relate to previous years but were entered in the system in 2015, as well as 17 fines (€3,570) revoked by a Court decree, were the main reasons for the upward revision by €3,507 to the opening balance of €32,009. During the year under review, the amount of €15,669 was collected, whilst newly accrued arrears amounted to €9,490, leaving a net closing balance of €29,337.

Court Fees

The spreadsheet reflecting the amendments to the figures, as issued from the CORTEX system forwarded to this Office, indicated an opening balance of outstanding Court fees of €2,225,661. However, this amount was revised downwards by €82,400 due to various anomalies in the malfunctioning computerised system.

During 2015, the amount of €219,090 was collected, and €16,672 was written off following approval. Arrears newly accrued amounted to €219,431, leaving a net collectable balance of €2,126,930 as at 31 December 2015.

Attorney General

On NAO's recommendation, the opening balance of €24,110 reported in the original Return by the AG's Office was revised upwards to €26,875, since a number of debtors were inadvertently omitted.

The net collectable balance of €52,418 by year-end relates to 67 debtors, which is recoverable by department action. However, from a sample of 15 files reviewed, it transpired that in nine cases, the respective amounts reported were not correct. The main reason was due to arrears dated prior to year 2015 which were not accounted for. An amended Return was resubmitted. However, considering the frequency of errors encountered, NAO does not have the comfort that the amounts quoted are correct.

From documentation provided, the reported net closing balance can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	22,164
Amounts outstanding for over one but less than two years (2014)	5,464
Amounts outstanding for over two but less than five years (2011 – 2013)	22,329
Amounts outstanding for over five years (– 2010)	2,461
Net Closing Balance	**52,418**

Notary to Government

The opening balance of €17,988 reported in the original Return by the Notary to the Government's Office was revised upwards to €22,029 after testing by NAO revealed that outstanding invoices issued prior to 2015 were omitted from the opening balance.

Ministry for Tourism

The Ministry for Tourism reported a gross closing balance of €1,573,782 for the year ended 31 December 2015, comprising dues to:

		€
a.	Malta Tourism Authority (MTA)	1,519,417
b.	Ex-White Rocks Holiday Complex	54,365
	Gross Closing Balance	**1,573,782**

The amount owed to ex-White Rocks Holiday Complex is considered as difficult to recoup. The balance due to MTA is recoverable by department action and relates to unpaid licences. This can be categorised as shown below:

	€
Amounts outstanding for less than one year (2015)	379,202
Amounts outstanding for over one but less than two years (2014)	218,506
Amounts outstanding for over two but less than three years (2013)	181,790
Amounts outstanding for over four years (– 2012)	739,919
Net Closing Balance	**1,519,417**

Shortcomings encountered when reviewing the respective amounts are outlined hereafter.

Malta Tourism Authority

The current reporting system generates an aged debtors list; however, given that the process to extract such reports is rather cumbersome, all the debts relating to 2012 and prior years are shown as one aggregate figure.

Management indicated a number of initiatives taken over the past year, in order to accelerate collection of arrears, namely:

a. Monthly statements are being sent to all outstanding establishment operators.
b. Registered letters signed by both Financial Controller and Legal Officer are being sent to operators, advising them to settle their dues.
c. Set-offs with creditor balances, where possible.
d. Agreements with operators binding them to settle their arrears within a specified period.
e. Continuous communication and monitoring is performed on all arrears due from the tourism-related operators, aiming at collecting all dues.
f. A full-time clerk is fully dedicated to chase debtors *via* e-mails and telephone calls.
g. The enforcement inspectors have been made aware and trained to chase the operators for arrears due during their routine inspections.
h. MTA is developing a new licensing-management system whereby credit control can be exercised more efficiently and effectively.

However, it was noted that licences were still being issued to operators even though prior dues are not settled. According to the Financial Controller, "... *given that this culture had been embedded in the industry for a number of years, suddenly reversing this decision would have serious economic implications on the whole industry*".

Ex-White Rocks Holiday Complex

The amount of €54,365 which has been outstanding for over 20 years, is due from five agencies for services rendered by ex-White Rocks Holiday Complex. The defaulting operators are no longer in operation and the amounts in question are considered to be irrecoverable. In September 2016, following NAO's enquiry, the Ministry for Tourism requested the relevant write-off approval from MFIN.

Institute of Tourism Studies

Last year, NAO could not verify the ARR submitted by the Institute of Tourism Studies as at end December 2014, due to the auditee admitting that they were incorrectly compiled. As a result, no verification was carried out with regard to the gross closing balance amounting to €270,366 as at 31 December 2014.

Breakdowns of the said closing balance and the downward revision of €18,883 indicated in the Return were not provided. Furthermore, a note in the Return justifying such revision was not included.

Similarly, no particular reason was given for a provision of €200,182, representing all amounts due prior to 31 December 2013. This amount includes an outstanding balance of €159,279 due from the then Employment and Training Corporation.

The net closing balance of €63,281, considered recoverable without intervention can be analysed as follows:

	€
Amounts outstanding for less than one year (2015)	11,981
Amounts outstanding for over one but less than two years (2014)	51,300
Net Closing Balance	**63,281**

Arrears of Revenue 2015 [a]

Ministry/Department		Gross Outstanding on 31/12/2014 [b]	Collected during 2015	Written off 2015	Revisions 2015	Arrears 2015
Office of the Prime Minister	€	14,239	2,581	-	-	6,700
Department of Information	€	64,420	59,168	-	-	43,997
Government Printing Press	€	447,559	192,371	-	-	211,635
Government Property Division	€	27,364,302	7,266,287	8,925	-1,364	8,291,260
Ministry for Foreign Affairs	€	61,299	28,774	-	34,774	188,033
Ministry for Education and Employment	€	677,122	63,603	548	-97,071	214,564
Ministry for Sustainable Development, the Environment and Climate Change	€	1,570,886	936,426	3,775	144,281	836,625
Ministry for Transport and Infrastructure	€	1,323,975	111,399	1,461	-30	524,128
Transport Malta [c]	€	c	c	c	c	c
Ministry for Gozo	€	293,975	7,644	-	-	31,679
Gozo Judicial Courts	€	631,968	140,986	-	2,129	240,947
Gozo General Hospital [d]	€	146,054	6,362	-	-1,654	25,589
Ministry for Social Dialogue, Consumer Affairs and Civil Liberties	€	13,917	-	-	-723	13,612
Industrial and Employment Relations	€	306,461	2,953	-	-	-
Ministry for the Economy, Investment and Small Business	€	425,465	203,034	-	-	235,392
Malta Gaming Authority [d]	€	1,977,923	1,292,627	-	-	3,435,006
Malta Communications Authority	€	227,711	227,711	-	-	879,120
Television Licensing Unit	€	10,156,016	81,195	13,992	600	-
Commerce	€	3,628,528	294,568	9,808	-820,649	284,468
Ministry for Home Affairs and National Security	€	-	-	-	2,746	-
Armed Forces of Malta	€	696,704	492,942	1,839	597	397,036
Police	€	396,408	93,929	-	2,652	56,947
Civil Protection	€	16,000	9,910	-	-	302
Ministry for Finance	€	2,147,507	2,136,335	-	-	8,641
Treasury (Pensions Section)	€	29,160,290	1,028,626	-	2,604,538	3,716,491
Inland Revenue						
Income Tax [d]	€	572,182,012	14,332,874	-	-160,115,716	238,597,888
Social Security Contributions: Class 1 and Class 2	€	220,283,203	68,612,675	-	-1,204,534	88,631,055
Final Settlement System	€	81,012,206	56,042,600	-	-620,028	65,684,525
Capital Transfer Duty:						
Duty on Documents	€	24,801,055	854,141	1,901	-1,546,561	2,176,854
Death and Donation Duty	€	4,623,516	3,555	-	-	3,480
V.A.T. [d]	€	1,136,825,743	11,385,266	1,865	-339,625,706	689,352,553
Customs	€	43,968,031	33,290,585	2,879	79,452	2,483,967
Contracts	€	294,463	13,579	21,749	-	-
Economic Policy	€	9,564	9,564	-	-	3,763
Ministry for Energy and Health						
Health	€	5,195,627	871,051	-	-33,340	4,308,036
Ministry for the Family and Social Solidarity						
Social Security Benefits	€	21,439,800	2,349,045	122,334	-353,455	5,415,482
Social Welfare Standards	€	2,690	2,690	-	-	-
Elderly and Community Care [d]	€	4,228,297	24,935	-	-	77,683

Gross Outstanding on 31/12/2015	Gross Variation	Amounts Est. as not Collectable	Net collectable arrears as at 31/12/2015	Net collectable arrears as at 31/12/2014	Net Variation	Due from Govt. Depts. & Para. Bodies	Due from Individuals & Private Cos.	Amounts coll. during January 2016	Balance as at 31/01/2016
18,358	4,119	-	18,358	14,239	4,119	-	18,358	100	18,258
49,249	-15,171	-	49,249	64,420	-15,171	49,249	-	31,578	17,671
466,823	19,264	-	466,823	447,559	19,264	466,567	256	-	466,823
28,378,986	1,014,684	-	28,378,986	27,364,302	1,014,684	9,746,003	18,632,983	1,137,902	27,241,084
255,332	194,033	2,648	252,684	48,340	204,344	163,412	89,272	63,706	188,978
730,464	53,342	132,711	597,753	536,559	61,194	17,616	580,137	11,516	586,237
1,611,591	40,705	29,762	1,581,829	1,541,126	40,703	15,278	1,566,551	252,732	1,329,097
1,735,213	411,238	37,196	1,698,017	1,267,498	430,519	1,619,046	78,971	3,307	1,694,710
c	c	c	c	23,662,372	c	c	c	c	c
317,910	24,035	85,062	232,848	265,693	-32,845	85,308	147,540	-	232,848
734,058	102,090	51,530	682,528	578,625	103,903	-	682,528	-	682,528
163,627	17,573	65,549	98,078	80,406	17,672	-	98,078	3,084	94,994
26,806	12,889	-	26,806	13,917	12,889	26,806	-	-	26,806
303,508	-2,953	195,686	107,822	110,776	-2,954	-	107,822	350	107,472
457,823	32,358	207,201	250,622	-	250,622	235,392	15,230	-	250,622
4,120,302	2,142,379	142,166	3,978,136	3,058,998	919,138	-	3,978,136	2,938,182	1,039,954
879,120	651,409	-	879,120	156,462	722,658	40,295	838,825	20,909	858,211
10,061,429	-94,587	6,036,857	4,024,572	4,077,213	-52,641	139,000	3,885,572	3,640	4,020,932
2,787,971	-840,557	1,164,292	1,623,679	2,122,155	-498,476	-	1,623,679	20,211	1,603,468
2,746	2,746	-	2,746	-	2,746	-	2,746	867	1,879
599,556	-97,148	1,360	598,196	599,815	-1,619	153,381	444,815	400,002	198,194
362,078	-34,330	62,540	299,538	364,298	-64,760	8,855	290,683	5,915	293,623
6,392	-9,608	5,589	803	9,750	-8,947	-	803	-	803
19,813	-2,127,694	-	19,813	2,147,507	-2,127,694	-	19,813	-	19,813
34,452,693	5,292,403	-	34,452,693	29,160,291	5,292,402	34,382,609	70,084	-	34,452,693
636,331,310	64,149,298	539,238,866	97,092,444	129,127,815	-32,035,371	-	97,092,444	3,097,989	93,994,455
239,097,049	18,813,846	148,713,636	90,383,413	85,748,809	4,634,604	-	90,383,413	13,537,260	76,846,153
90,034,103	9,021,897	63,023,872	27,010,231	24,303,662	2,706,569	-	27,010,231	9,451,617	17,558,614
24,575,306	-225,749	18,245,905	6,329,401	6,838,106	-508,705	-	6,329,401	205,677	6,123,724
4,623,441	-75	3,744,987	878,454	443,428	435,026	-	878,454	2,795	875,659
1,475,165,459	338,339,716	1,402,390,053	72,775,406	70,145,048	2,630,358	-	72,775,406	-	72,775,406
13,237,986	-30,730,045	1,048	13,236,938	37,074,216	-23,837,278	2,339,302	10,897,636	1,403,077	11,833,861
259,135	-35,328	20,510	238,625	125,828	112,797	-	238,625	-	238,625
3,763	-5,801	-	3,763	9,564	-5,801	3,526	237	848	2,915
8,599,272	3,403,645	72,939	8,526,333	5,126,787	3,399,546	3,081,177	5,445,156	48,189	8,478,144
24,030,448	2,590,648	2,138,374	21,892,074	21,439,800	452,274	-	21,892,074	144,277	21,747,797
-	-2,690	-	-	2,690	-2,690	-	-	-	-
4,281,045	52,748	-	4,281,045	4,227,992	53,053	4,180,748	100,297	14,822	4,266,223

Arrears of Revenue 2015 [a] *cont./*

Ministry/Department		Gross Outstanding on 31/12/2014 [b]	Collected during 2015	Written off 2015	Revisions 2015	Arrears 2015
Ministry for Justice, Culture and Local Government	€	-	17,208	-	17,263	50,255
Judicial [e]	€	11,008,493	1,285,436	110,879	-1,532,419	1,780,251
Local Government Department [f]	€	3,150	3,150	-	-	2,398
Attorney General [e]	€	26,875	10,744	1,005	15,127	22,165
Notary to Government [e]	€	17,988	22,029	-	4,041	3,678
Ministry for Tourism	€	1,720,325	476,101	-	-49,644	379,202
Institute of Tourism Studies	€	270,366	-	-	-18,883	11,980
TOTAL [g]	**€**	**2,209,662,033**	**204,286,659**	**302,960**	**-503,113,577**	**1,118,627,387**

a) Figures may not add up due to rounding-up.
b) Opening Balances reported as featuring in last year's AAR, unless otherwise specified.
c) Did not submit Return of Arrears 2015.
d) Opening Balance 2015 does not tally with Closing Balance 2014 (*vide* comments).
e) Featured in 2014 under the Office of the Prime Minister.
f) Featured in 2014 under the Ministry for Tourism.
g) Totals are incomplete in view of c), and d) above.

Gross Outstanding on 31/12/2015	Gross Variation	Amounts Est. as not Collectable	Net collectable arrears as at 31/12/2015	Net collectable arrears as at 31/12/2014	Net Variation	Due from Govt. Depts. & Para. Bodies	Due from Individuals & Private Cos.	Amounts coll. during January 2016	Balance as at 31/01/16
50,310	50,310	2,599	47,711	-	47,711	37,750	9,961	9,401	38,310
9,860,010	-1,148,483	163,483	9,696,527	10,905,731	-1,209,204	-	9,696,527	115,575	9,580,952
2,398	-752	-	2,398	3,150	-752	2,398	-	1,035	1,363
52,418	25,543	-	52,418	26,304	26,114	-	52,418	2,151	50,267
3,678	-14,310	-	3,678	17,987	-14,309	3,678	-	129	3,549
1,573,782	-146,543	54,365	1,519,417	1,665,960	-146,543	-	1,519,417	142,951	1,376,466
263,463	-6,903	200,182	63,281	270,366	-207,085	45,118	18,163	-	63,281
2,620,586,224	**410,924,191**	**2,186,230,968**	**434,355,256**	**495,195,564**	**-37,177,936**	**56,842,514**	**377,512,742**	**33,071,794**	**401,283,462**

Submissions as per Treasury Circular No. 12/2016 – 'PAC Specific Request' [a]

Ministry/Department		Net collectable arrears as at 31/12/2015	Amounts Est. as not Collectable	Gross Outstanding on 31/12/2015	Analysed as follows:			
					Statute-barred	Pending Court action	Recoverable by Dept. action	No Dept. action required
Office of the Prime Minister	€	18,358	-	18,358	-	-	3,760	14,598
Department of Information	€	49,249	-	49,249	-	-	-	49,249
Government Printing Press	€	466,823	-	466,823	-	-	224,032	242,791
Government Property Division [d]	€	28,378,986	-	28,378,986	3,167,795	4,963,174	19,355,901	892,116
Ministry for Foreign Affairs	€	252,684	2,648	255,332	2,648	-	188,978	63,706
Ministry for Education and Employment	€	597,753	132,711	730,464	-	27,118	685,730	17,616
Ministry for Sustainable Development, the Environment and Climate Change [b]	€	1,581,829	29,762	1,611,591	29,762	181,768	1,077,164	323,200
Ministry for Transport and Infrastructure [d]	€	1,698,017	37,196	1,735,213	63,836	5,535	1,366,177	299,665
Transport Malta [c]	€	c	c	c	c	c	c	c
Ministry for Gozo	€	232,848	85,062	317,910	-	-	293,482	24,428
Gozo Judicial Courts	€	682,528	51,530	734,058	24,487	23,687	439,039	246,845
Gozo General Hospital	€	98,078	65,549	163,627	65,549	-	88,768	9,310
Ministry for Social Dialogue, Consumer Affairs and Civil Liberties	€	26,806	-	26,806	-	-	22,283	4,523
Industrial and Employment Relations	€	107,822	195,686	303,508	-	4,135	265,183	34,190
Ministry for the Economy, Investment and Small Business	€	250,622	207,201	457,823	207,201	15,230	-	235,392
Malta Gaming Authority	€	3,978,136	142,166	4,120,302	-	122,581	1,722,565	2,275,156
Malta Communications Authority	€	879,120	-	879,120	-	-	-	879,120
Television Licensing Unit	€	4,024,572	6,036,857	10,061,429	6,036,857	-	4,024,572	-
Commerce [b]	€	1,623,679	1,164,292	2,787,971	763,843	-	1,623,678	-
Ministry for Home Affairs and National Security	€	2,746	-	2,746	-	-	2,746	-
Armed Forces of Malta	€	598,196	1,360	599,556	1,360	7,850	590,346	-
Police [d]	€	299,538	62,540	362,078	166,090	22,405	157,895	15,688
Civil Protection	€	803	5,589	6,392	5,589	-	-	803
Ministry for Finance	€	19,813	-	19,813	-	-	19,831	-
Treasury (Pensions Section)	€	34,452,693	-	34,452,693	-	-	34,452,693	-
Inland Revenue (including Capital Transfer Duty)	€	221,693,943	772,967,266	994,661,209	144,946,204	77,484,120	162,167,409	610,063,476
V.A.T.	€	72,775,406	1,402,390,053	1,475,165,459	1,402,390,053	27,913,035	44,862,371	-
Customs [d]	€	13,236,938	1,048	13,237,986	28,813	6,892,767	1,460,357	4,856,049
Contracts	€	238,625	20,510	259,135	8,438	92,332	118,753	39,612
Economic Policy	€	3,763	-	3,763	-	-	3,763	-
Ministry for Energy and Health								
Health	€	8,526,333	72,939	8,599,272	72,823	-	7,918,205	608,244
Ministry for the Family and Social Solidarity								
Social Security Benefits	€	21,892,074	2,138,374	24,030,448	2,138,374	1,042,246	2,499,066	18,350,762
Social Welfare Standards	€	-	-	-	-	-	-	-
Elderly and Community Care [b]	€	4,281,045	-	4,281,045	-	-	101,245	-

Submissions as per Treasury Circular No. 12/2016 – 'PAC Specific Request' [a] *cont./*

Ministry/Department		Net collectable arrears as at 31/12/2015	Amounts Est. as not Collectable	Gross Outstanding on 31/12/2015	Analysed as follows:			
					Statute-barred	Pending Court action	Recoverable by Dept. action	No Dept. action required
Ministry for Justice, Culture and Local Government	€	47,711	2,599	50,310	2,599	-	47,711	-
Judicial	€	9,696,527	163,483	9,860,010	163,483	2,819,219	6,787,856	89,452
Local Government Department	€	2,398	-	2,398	-	-	760	1,638
Attorney General	€	52,418	-	52,418	-	-	52,418	-
Notary to Government	€	3,678	-	3,678	-	-	3,678	-
Ministry for Tourism	€	1,519,417	54,365	1,573,782	54,365	-	1,519,417	-
Institute of Tourism Studies	€	63,281	200,182	263,463	200,182	-	-	63,281
TOTALS [e]	**€**	**434,355,256**	**2,186,230,968**	**2,620,586,224**	**1,560,540,351**	**121,617,202**	**294,147,832**	**639,700,910**

a) Figures may not add up due to rounding-up.
b) Amount submitted as *per* Treasury Circular No. 12/2016 does not tally to Return of Arrears 2015 (*vide* comments).
c) Did not submit Return of Arrears 2015 and submissions required by Treasury Circular No. 12/2016.
d) Refer to comments under respective heading in relation to figures reported as statute-barred exceeding amounts estimated as not collectable.
e) Totals are incomplete in view of b) and c) above.

Malta Police General Fund

Background

The Malta Police General Fund (MPGF) was set-up in November 1919 and has been, to-date, maintained by the Commissioner of Police (CoP) for the general benefit of the Force. In line with S.L. 164.01 Article 12 (1 and 2), all members of the Force, who joined after 30 November 1919, shall make a mandatory contribution of €13.98 every three months.

The aforementioned legislation also stipulates that the accounts related to the Fund shall be audited annually by the Auditor General. However, no records were ever forwarded to the National Audit Office (NAO) prior to the year under review.

In addition to the MPGF, in line with Article 11 of the same legislation CoP keeps two accounts, namely an Officers' Mess, as well as another mess referred to as Other Ranks' Canteen (ORC). In the former case, which covers contributions from those members of the Force not below the rank of Inspector, membership is compulsory. On the other hand, the ORC comprises all the members below the grade of Inspector, and subscription is voluntary. These two accounts, however, were outside the scope of the audit.

A number of internal circulars, dating back to 1978, were provided in relation to the amount to be contributed, with the latest issued in December 1998. The respective contributions payable by members of the Force with effect from 1 January 1999 are being reproduced in *Table 1*.

Table 1: Contributions Payable as per Circular No. 91/98

Rank	Amount payable per Quarter
	€
CoP, Deputy Commissioner and Assistant Commissioner	23.41
Superintendent	21.66
Inspector	20.96
Major, Sergeant and Constable	13.98

The collected amounts are then apportioned as indicated in *Table 2*.

Table 2: Apportionment of Contributions

Fund Name	Rank	Amount of Contribution
		€
MPGF	n/a	6.99[1]
Malta Police Mutual Help Association Fund	n/a	3.50[2]
Malta Police Association (MPA) Fund	n/a	3.49[3]
Officers' Mess Fund[4]	CoP, Deputy Commissioner and Assistant Commissioner	9.43
	Superintendent	7.68
	Inspector	6.98

Auditors were verbally informed that members of the Force are also given the option to continue paying a standard contribution of €13.98 *per annum* once they retire from the Force. However, no documentation was provided during the audit to substantiate this rate.

Internal Circular No. 79, dated 23 July 1980, highlighted the principal aim of the MPGF as follows:

a. The welfare of officials who, for some reason or other, pass through hard times and would require assistance.

b. Other activities for the benefit of the Force, such as the learning of foreign languages.

This was followed by another circular dated 9 June 1981, setting out the payment of €2,329.37 (Lm1,000) to the dependants of Police Officers who die while in service. Moreover, although not included in any of the circulars provided, heirs of Police Officers who pass away after their retirement receive the amount of €1,560.68.

Up to December 2015, the upkeep of financial records related to the MPGF fell under the responsibility of a civil servant, who was since transferred to another Department. With effect from 1 January 2016, such responsibility was taken over by a police constable, referred to as the Accounting Officer throughout this Report. The Final Accounts of the MPGF for the year 2015 were drawn up and forwarded to NAO for audit.

Financial Background

The Final Accounts referred to above included two separate Income and Expenditure Statements; one based on cash receipts and payments and one that included income and expenditure amounts that were still outstanding at year-end. A Cash Movement Statement and Notes to the Accounts were also presented.

[1] Used by CoP to finance the Christmas parties organised by the individual districts, branches or sections of the Force.
[2] This amount is allocated for Mutual Help payments, but the respective funds are retained in the MPGF.
[3] Before February 2015, Police Officers were not allowed to join any trade unions, but would automatically become members of the MPA upon taking their oath of office. For the year under review, the Association received the sum of €3.49 for each Police Officer paying the contribution. This payment was effected up to February 2015 and is since being retained in the MPGF.
[4] The amount transferred to this Fund is the difference between the rates paid by higher officials, as indicated in *Table 1*, and the standard contribution rate of €13.98.

Income

Actual aggregate income received in 2015 amounted to €166,089. This comprised the amounts indicated in *Table 3*.

Table 3: Income

Source	Amount
	€
Contribution by serving members	83,693
Contribution by retired members	14,029
Extraordinary one-time deposit	64,225
Payment from MPA	3,980
Donations	162
Total	**166,089**

The one-time deposit of €64,225 made into the MPGF came from the transfer of proceeds from a number of other bank accounts administered by CoP[5], which were closed during the year under review. This transfer was considered necessary since the funds available in the MPGF were not enough to cover all the expenses.

Further to the above, an aggregate amount of €62,406 was shown as outstanding income, as reported in *Table 4*.

Table 4: Outstanding Income

Source	Amount
	€
Estimate of outstanding contributions from December 2014 to December 2015	44,214
Income related to 2015 contributions received as at 4 February 2016	15,476
Monies collected from members of the Force in respect of donation to *Istrina*[6]	2,716
Total	**62,406**

[5] It was pointed out that these monies are not public funds, but were put aside from past activities organised by CoP and were not being utilised.
[6] Donation was made to *Istrina* on 26 December 2015, however most of the funds were deposited in the MPGF in the subsequent year.

Expenditure

Aggregate expenditure paid during the year under review totalled €107,508 and comprised the amounts shown in *Table 5*.

Table 5: Expenditure

Source	Amount	Percentage of Expenditure
	€	%
Christmas and Police Day social activities	43,866	41
Mutual Help payments to heirs of serving and non-serving members	43,486	40
Contribution to Officers for Christmas parties	10,939[7]	10
Payment made to MPA	6,090	6
Donation to *Istrina*	2,946[8]	3
Others: emoluments, bank charges and fund raising activities	181	–
Totals	**107,508**	**100**

A further amount of €145,096 was recorded as outstanding expenditure, including the items in *Table 6*.

Table 6: Outstanding Expenditure

Source	Amount
	€
Balance payable to the ORC, covering Christmas and Police Day social activities organised between 2012 and 2015	84,230
Mutual Help payments to heirs of non-serving members	29,913
Payment to MPA	19,174
Payment to the Malta Police Officers' Mess Committee	7,159
Contribution for Christmas parties in individual districts and stations	4,620
Total	**145,096**

Taking into consideration the opening cash balance of €18,890 and assuming that all the outstanding income recorded in the Statement is received, the above expenditure still leaves the MPGF in a deficit position of €5,219 as at 31 December 2015.

Audit Scope and Methodology

The main scope of the audit was to assess the level of internal controls prevailing in the management of the MPGF, and to determine whether day-to-day operations reflect efficient administration of the monies, in line with applicable regulations. Other objectives of the audit were to:

a. obtain reasonable assurance that all monies were accurately recorded and are duly covered by supporting documentation enabling independent verification;

[7] This amount excludes cheques for 2015 Christmas parties that were not cashed by 31 December 2015.

[8] Whilst the amount of €2,716 was collected from members of the Force or initiatives taken for the cause in question, the remaining balance of €230 comprised the foregone allowance of €6.99 payable by CoP for the organisation of Christmas parties.

b. identify any concerns with the procedures in place for receiving, handling, safeguarding, and depositing of monies, and providing recommendations thereto; and

c. determine the degree of compliance with applicable rules and regulations.

Initial meetings held with the Accounting Officer, as well as the officer in charge of the contributions' collections revealed that adequate audit trail for the collection of such amounts did not exist. Accounting records were also incomplete and no safeguards were in place to prevent or detect material misstatement.

As a result, a risk-based approach was adopted for audit purpose, whereby testing was largely focused on the revenue collection system in place to determine the level of internal controls and reliability of records. Testing carried out was focused on the following areas:

i. Contributions by serving members.
ii. Mutual Help payments to pensioners.
iii. Payments to heirs of serving and non-serving members.
iv. Contribution for Christmas parties.
v. Amounts transferred to MPA and the Police Officers' Mess.

Limitation on Scope of Audit

Adequate books of account were not in place as at time of audit. The only records provided for audit purposes were two spreadsheets, both comprising payments and receipts, one drawn up by the current Accounting Officer following the assignment of his new responsibilities, while the other one was drawn up by the outgoing officer during her tenure. The latter record contained material discrepancies, highlighted further down in the Report, and which data was considered unreliable. Thus, a new one was drawn up by the Accounting Officer. However, this was solely based on deposits and payments showing in the bank statements, with no consideration for unreconciled deposits and cheques as at year-end.

Given the lack of official documentation supporting the contribution of €6.99 made for each member of the Force for the organisation of Christmas parties, the payments effected to heirs of non-serving members, as well as other disbursements relating to hospitality, the regularity of such transactions could not be ascertained. For the same reasons, completeness of the amount of €3,980, recorded as received from MPA for the 2014 children's Christmas party, could not be confirmed.

Inadequate audit trail and the lack of a unique receipt number also hindered reconciliations between amounts forwarded to the Accounting Officer and the deposits in bank. This shortcoming has since been partly addressed, as a numbered receipt was then being given by the new Accounting Officer every time money is received.

Key Issues

Financial Sustainability of the Malta Police General Fund

Despite the one-time deposit of €64,225 transferred to MPGF from several dormant bank accounts to cover part of the expenditure incurred during the year, when taking into consideration both outstanding income and expenditure, as well as cash available from previous year, the Fund still ends the year in a net deficit of €5,219.

This situation has been partly triggered by the fact that whilst the amount received from retired officers during the year under review amounted to €14,028, contributions due to heirs in respect of non-serving officers who passed away during 2015 amounted to €40,577[9]. This also indicates that the scheme is not sustainable and, unless changes to the present contribution and payment system are established, the Malta Police Force (MPF) may not be in a position to settle outstanding debt relating to the Fund in question in the very near future, if the current level of expenditure is maintained.

Lack of Internal Controls

The audit revealed that the internal control structure, over the receipt and handling of cash in particular, is inadequate and of considerable concern to the NAO. Checks carried out made it amply clear that no monitoring was in place to ensure that controls are properly designed, executed and effective. Below is a list of internal control failures identified during the audit, which will be discussed in more detail further on in the Report.

a. No proper accounting records maintained.

b. No segregation of duties.

c. Lack of audit trail of cash and cheques received.

d. Receipt books used to record income from pensioners without a sequential number.

e. Financial records of prior years not submitted for auditing, in breach of standing regulations.

f. Lack of official documentation to indicate which expenses can be covered by the Fund.

g. Accrued income and expenditure omitted from the Final Accounts.

h. Cancelled receipts not supported by original copies.

Control Issues

Unclear Purpose of the Fund

Circular No. 79 of 1980 stipulated that the principal purpose of the MPGF is the welfare of officials who for some reason or other pass through hard times and would require assistance. It also indicated that other activities of benefit to members of the Force, though not connected to personal hardships, can also be financed through this Fund, highlighting as a case in point the learning of foreign languages. In addition, the contributions paid shall cover the Malta Police Mutual Help Association, the MPA, the MPGF and the Officers' Mess.

a. Except for the highlighted circumstances, no other documentation was provided in connection with the operation of the funds retained in the MPGF. In view of the vague information available *vis-à-vis* the expenses that may be paid out of the MPGF, it could not be ascertained that amounts charged to the Fund are actually for the general benefit of the Force as indicated in S.L. and Circular No. 79 of 1980.

[9] The amount covers 26 claims of which eight, amounting in total to €12,485, were settled in 2015. Another 18 claims, totalling €28,092 were still outstanding as at 31 December 2015. On the other hand, 10 claims relating to 2014, in aggregate amounting to €15,607, were settled in 2015 but are excluded from the figure of €40,577.

b. An analysis of the expenditure charged to the MPGF during 2015, totalling €107,508, revealed that 51% related to hospitality. The total amount of €54,805 comprised different social activities and parties organised by CoP (€43,866), and the contribution paid for parties to members of the Force held in the individual districts and stations (€10,939).

   On the other hand, as at 31 December 2015, payments to the heirs of non-serving members, amounting to €29,913, were still outstanding.

In the absence of guidelines clearly setting out the purpose of the Fund, as well as its specific use, the possibility that monies deposited therein are used as an extension of the budgeted allocation, for purposes other than those intended for, is significantly increased. Moreover, given that priority is being given to hospitality related payments, MPF may not be in a position to meet other obligatory commitments in the future.

Amounts Payable from the Fund not duly approved

a. The amount of €3,144.65 payable to the heirs of each serving member, exceeds that of €2,329.37 stipulated in Internal Circular No. 57 of 1981 by €815.28. This higher rate was not supported by documentation evidencing approval.

b. No official documentation was provided to substantiate the payment, as well as the rate of €1,560.68 payable to heirs of non-serving members.

c. Similarly, the payment of €6.99 paid by CoP on behalf of each member of the Force, for the organisation of Christmas parties at the respective districts and stations, is also not covered by any documentation, confirming its approval.

Completeness of Income Receivable not ensured

Completeness of the amount of €3,980, recorded as received in MPGF from MPA, could not be ascertained since an agreement between both parties was not available for audit purposes. Moreover, although Auditors were informed that payments due to MPA covered the period up to February 2015, *i.e.* the period when such contribution stopped being transferred to the latter, this was not formalised.

Revenue Collection Process

Serving Members

General collection of the contribution due takes place every quarter, where cash is collected by all districts, units and divisions under their charge from every serving member of the Force. Each of these sections has a receipt book, with five receipts in every sheet. However, only the sheet is numbered, with the individual receipts having no specific reference. The receipts come in triplicate format, with the original given to the paying officer, a copy kept by the officer in charge of the contributions together with the money at the Police General Headquarters, while the last copy retained by the individual sections.

Pensioners' Contributions

The contribution of €13.98 *per annum* by non-serving members is payable on a voluntary basis. Respective receipts, which are not numbered, are printed every year by the officer in charge of the contributions.

a. Lack of Segregation of Duties

Despite the significant amounts collected from contributions which, as per the financial records provided, amounted to €97,722[10] in 2015, only two officers were involved in the cash handling process, namely the officer in charge of the contributions and the Accounting Officer. The former collected the monies, retained custody thereof, issued receipts, carried out reconciliations, as well as maintained the respective records, while the latter was responsible for preparing the bank deposit slips, the remittance of money into the bank and updating the spreadsheet. Thus, segregation of duties was lacking and is of a major concern to NAO.

Furthermore, given that both officers were doing this over and above their normal duties, they were receiving a quarterly allowance[11] for the extra work involved.

b. Lack of Basic Accounting Records

Proper books of account were not maintained; neither by the officer in charge of contributions nor by the Accounting Officer. The latter kept a spreadsheet; however, this merely indicated the transactions as reflected in the bank statement, including expenses such as bank charges. Furthermore, it contained a number of errors as highlighted in the next observation. Moreover, because of a computer problem in 2014, which resulted in a loss of records pertaining to the last six weeks of that year, the opening balance for 2015 was also taken to be that of the respective bank statement.

c. Discrepancies in Records

As already indicated, the spreadsheet kept by the previous Accounting Officer was deemed to be unreliable. The following shortcomings were identified during the audit:

i. A cheque amounting to €4,129.80, was included twice in the said spreadsheet.

ii. Deposit of €140 related to the contribution collected for quarters March, June and September 2015, was recorded in the said spreadsheet as €1,400.

iii. Revenue entries, amounting in total to €1,916.60, as well as proceeds transferred from other accounts, totalling €64,225, were not traced in the spreadsheet.

iv. A total amount of €2,174.66 remitted to bank between 11 and 12 February 2015 was indicated in the previous Accounting Officer's records as deposits by Gozo. However, this was neither supported by bank deposit slips nor confirmed by the Gozo Superintendent.

While acknowledging that these shortcomings were already identified by the new Accounting Officer, and a new spreadsheet eventually drawn up, the relevant record created was only based on the bank statements and cheque stubs traced in retrospect, thus still lacking completeness.

Furthermore, despite that the date of payment of the respective contribution constitutes a main audit trail, it transpired that not all receipts were dated.

[10] This amount is made up of contribution paid by serving members (€83,693) and non-serving members (€14,029) as at 31 December 2015. It does not include income relating to 2015 but which was received after year-end.

[11] During 2015, the quarterly allowance payable to the previous Accounting Officer and the officer in charge of the contributions amounted to €420 and €141 respectively. However, in the same year, only the €141, pertaining to the last quarter was charged to the MPGF and included in the financial records. The allowance for the same quarter payable to the previous Accounting Officer was charged to MPGF in January 2016. On the other hand, the amounts related to the other three quarters were charged to other accounts held by CoP. With effect from January 2016, the rates payable have been reviewed and now stand at €400 and €139.76, payable every quarter to the Accounting Officer and the officer in charge of contributions respectively.

d. Weakness in the Pensioners' Contribution Collection Process

The only records related to the contributions paid by pensioners are the receipts, indicating the date of payment on the stub. This does not provide the required level of comfort as regards completeness of income.

e. Serving Members' Contributions

The fact that receipts given on the collection of contribution from serving members are not individually numbered, and thus, no reference to this could be made in the manual records drawn up, does not promote transparency and also lacks audit trail.

Eleven contributions related to the sampled period, *i.e.* September quarter, were not traced in the records. It transpired that three of the said receipts were omitted from the 2015 records. These were then included in 2016, after being pointed out during the audit. In the other remaining eight cases, these were still not traced in amounts forwarded to the Accounting Officer for the eventual deposit.

Several instances were also noted where cancelled receipts were not supported by their originals. Furthermore, it transpired that the officer in charge of contributions was signing the receipts in advance.

f. Handing over of Cash not substantiated

Besides the lack of segregation of duties, it also transpired that the transfer of money to the Accounting Officer was not supported by any documentation. During the year under review, the then Accounting Officer only endorsed the amounts indicated in the manual records maintained by the officer in charge of contributions. With effect from 1 January 2016, a receipt started being issued by the Accounting Officer once money is handed over; however, completeness of the said amounts is still not being checked.

g. Discrepancies between Monies Collected and Bank Deposits

As per information gathered by NAO, monies collected in respect of the 2015 annual contribution payable by pensioners amounted to €14,418, of which €6,256 was prepaid in 2014.

It was established that a total of €10,582 from the amount in question was deposited in bank in 2015. However, total amount actually deposited in 2014 could not be reliably determined, in view of the lost data pertaining to the said period, as indicated further up in this Report. As a result, completeness of such remittance could not be ascertained.

The officer in charge of contributions remitted a total of €77,655 covering contributions received from serving members between 6 January and 24 December 2015. On the other hand, deposits in bank between 8 January and 28 December 2015 totalled €80,958. Again, a reconciliation could not be performed because amounts received in previous year which were not deposited could not be separately identified. Furthermore, without a unique reference, such as a receipt number, attempts to reconcile individual quarter deposits also proved very difficult.

Contributions paid in Cash

Despite that the payment of contribution is a statutory requirement and has to be paid by all members of the Force, the settlement thereof is still being effected by cash, rather than through more effective options available, such as direct deduction from the respective salaries. As a result, the officer in charge of contributions is ending up with significant amounts of cash in hand.

In addition to the risks prevailing with cash handling, this method does not ensure that all contributions due are collected in a timely manner, if at all. It also results in a significant unnecessary workload.

Inaccurate Balance of Funds at Year-end

As highlighted under 'Background', the difference between the amounts paid by higher ranks and the €13.98 is initially paid into the MPGF, and eventually transferred out to the Officers' Mess account. Similarly, the contribution of €3.49 per officer, payable to MPA up to February 2015, was also being deposited to the MPGF and then transferred to the Association. By the end of 2015, the aggregate balance which was not yet transferred amounted to €26,333, out of which €19,174 pertained to MPA for the last two quarters of 2014, and €7,159 due to the Officers' Mess. As a result, the bank balance as shown in the account prior to the said transfers is theoretically inflated. This might result in MPF entering into commitments based on the said financial information, which in fact will not be able to be met out of the actual funds available.

Insufficient Control over Income for Mutual Help

In line with Internal Circular No. 91 of 1998, €3.50 of the contribution paid shall be used for Mutual Help. However, given that this money is not segregated, it cannot be ensured that the portion of contribution intended for such assistance is actually being retained and used for its intended purpose, particularly in view of the limited controls over the said Fund.

Incorrect Payments and Other Administrative Shortcomings

a. The amount of €37,196 reported in the Income and Expenditure statement as 'Payments to heirs of non-serving members' was overstated by €1,300 and €2,861 when compared to the amounts indicated in the spreadsheet supporting the accounts and the list of cheques respectively. It transpired that part of the latter discrepancy was due to the fact that a cheque, amounting to €1,561, was included in the spreadsheet but not in the list of cheques provided with the same record.

b. A variance of €7,804 was also noted between the amount paid to heirs of non-serving members, as per information obtained from the officer in charge of contributions (€28,092) and the amount of €35,896 indicated as paid in the spreadsheet.

c. According to a spreadsheet provided by the officer in charge of contributions, a total of 1,656 officers paid the contribution due for the said period by the 25 November 2014, being the date of cheque to MPA. Based on this information, the related payment to MPA should amount to €5,779[12] and not €6,090 as shown in the financial records.

d. As indicated earlier on in this Report, the CoP makes a contribution of €6.99 per officer towards Christmas parties organised in the individual districts and stations. It transpired that while the payments effected tallied with the amount in the financial records, the number of officers showing in the calculation of contribution differed from those included in Human Resources (HR) records, despite that the list of contributions payable is drawn up by the same HR Section.

   Moreover, it was noted that the amount paid in 2015 was €10,939; however, only €4,977 related to that year and just covered the contribution of 712 of the 2,162 employed as at 31 December 2015. As a result, the amount of €4,620, being outstanding contribution featuring in the accounts, which covers only 661 employees, is significantly understated as this should be increased by an additional €5,284[13].

[12] Made up of 1,656 officers at the rate of €3.49.

[13] This amount covers 756 officers, with the remaining 33 opting to leave the contribution as a donation to *Istrina* and Community Chest Fund, and thus, not taken into consideration for the computation.

e. As per NAO's workings, the payment due to MPA (€21,481), and that reported in the financial records (€19,174) varied by €2,307. However, given that information provided indicated only the deposit date rather than the collection date, the accurate amount could not be established.

Misleading Accounting Information

As highlighted in the 'Financial Background', the records provided were fragmented and a combination of cash and accrual accounting. Whilst acknowledging that this is the first time that financial records were drawn up, the method adopted shows a misleading picture for the year under review. It is also considered an unreliable basis for strategic decisions that may be taken thereupon.

Christmas and Police Day Social Activities

a. A total of €43,866, being 41% of the expenditure incurred during 2015 from the MPGF, related to Christmas and Police Day social activities. From this amount, €7,562 covered the acquisition of presents for children for the 2014 Christmas party. It was also noted that the respective invoice, as well as another bill amounting to €398, raised by ORC in connection with the same party, were both addressed to the Entertainment Committee MPA. However, both invoices were charged to MPGF.

b. An amount of €3,980 was eventually received from MPA in respect of the said Christmas party. Since no documentation was provided by CoP, reflecting the agreement between MPA and the Police Force, correctness and regularity of the amounts in question could not be ascertained.

c. Another €35,763 out of the aforementioned amount of €43,866 covered payments to ORC in respect of food and beverages, provided for the various receptions and other social activities hosted by CoPs in 2014 and 2015. On analysing the respective records, it was noted that certain items were not individually priced, hindering verification. However, the manual invoice was still endorsed.

d. Moreover, while the quantities did not change much from one reception to another, prices were rather inconsistent. This also applied for the 'Miscellaneous' charge, which was included in each and every invoice, to cover all disposables, comprising amongst others, napkins, tooth-picks, plates, cups, tumblers, dishes, forks and table covers.

Compliance Issue

Financial Records not submitted to NAO for Auditing Purposes

Despite that it is clearly stipulated in the law that records related to MPGF shall be audited by the Auditor General on an annual basis, no financial records were ever submitted to NAO prior to the year under review. In addition to non-compliance with the law, this has enabled a culture of lack of controls to prevail, allowing the highlighted malpractices to become embedded in daily operations, and which now may be hard to change.

Recommendations

Key Issues

Financial Sustainability of the Malta Police General Fund

A thorough exercise, to establish the contribution to be paid and to identify any unnecessary expenses, is recommended. Related expenditure is also to be controlled through strict budgetary measures, taking immediate action in case of deviations.

Lack of Internal Controls

CoP is urgently expected to review and strengthen the internal control systems in order to ensure sound financial management. Such controls are fundamental to the successful operation and day-to-day running of the Fund. To this effect, Management is to develop its own procedures having regard to its specific circumstances and characteristics. Ideally, controls are to be embedded in the operations and form part of the overall culture, be capable of responding quickly to evolving risks, and include procedures for reporting immediately to appropriate levels any identified weaknesses and significant control failures. This would ensure timely corrective action.

Notwithstanding the above, sound internal controls cannot eliminate the possibility of processes being deliberately circumvented by the collusion of employees or poor judgement in decision-making. Thus, staff and operations should be duly supervised by competent officers who understand the processes and procedures that are in place, and who are ready to query as necessary, and take the required action to address any shortcomings in a timely manner.

Control Issues

Unclear Purpose of the Fund

MPF is expected to prioritise expenditure, leaving aside enough funds to cover committed disbursements. After consultation with the trade unions representing the members of the Force, a circular to this effect can be drawn up, highlighting the nature of expense that is to rank before hospitality.

Amounts Payable from the Fund not duly approved

It is recommended that an official policy is drawn up, indicating what may be charged to the MPGF, as well as the respective amounts.

Completeness of Income Receivable not ensured

Another policy should highlight the nature, frequency and amounts receivable, enabling independent parties to carry out verifications intended to ascertain completeness of income.

Revenue Collection Process

Lack of Segregation of Duties

Segregation of duties constitutes a critical component of an effective internal control system. The main idea is that of maintaining checks and balances by preventing any one person from having access to the asset, as well as having the responsibility for maintaining its accountability. It is thus recommended that key tasks, particularly those relating to the receipt of cash, custody, record keeping and reconciliations, are assigned to different individuals.

In view of the above, NAO recommends that, as far as possible, more staff is involved in the revenue collection process. Another officer should thus keep independent records of such revenue. On a daily basis, all income together with the respective receipts is to be forwarded to the latter who shall record it in a cashbook. Once cash is remitted to the Accounting Officer, he shall also record the money received in a separate cashbook. Ideally, the money is handed over to a different officer who shall prepare the bank deposit slip and remit the amount to bank. The Accounting Officer shall then carry out regular bank reconciliations to ensure completeness. It is also recommended that such key tasks are covered by Standard Operating Procedures, clearly highlighting the established course of action and roles of the respective officers.

Lack of Basic Accounting Records

NAO reiterates the importance of keeping proper books of account at each point where money is received, including the use of a cashbook. It can be maintained in either manual or electronic format. However, in order to be effective, besides the amount, the cashbook must contain at least the date and nature of transaction. Ideally, it is also to include a reference to underlying documents such as receipts, as well as a signature of the officer recording the transaction.

In the case of the officer in charge of contributions, such record will only include the income received on specific days, the source and the amount forwarded to the Accounting Officer. To ensure an adequate audit trail, receipt numbers are to be indicated. A separate entry should also be made when the monies are forwarded to the Accounting Officer.

The cashbook of the Accounting Officer is expected to include any income received and payments issued from the account, as well as relevant details and bank deposits. This record shall then be reconciled to the bank statement on a regular basis and a bank reconciliation statement drawn up.

Discrepancies in Records

MPF is encouraged to implement the recommendations provided under the previous observations as soon as possible. Furthermore, it is important that someone with a basic accounting knowledge oversees their implementation and explain the importance of such changes while ensuring that they are embraced by all.

Weakness in the Pensioners' Contribution Collection Process

An urgent overhaul of the current system is recommended. A standard application form can be drawn up to be filled by non-serving members interested in paying the contribution and recorded accordingly in a spreadsheet, where payments and their respective dates are to be indicated. Details shall be verified on a regular basis with records obtained from the HR Section. Furthermore, the use of pre-printed, sequentially numbered receipts is recommended. It would also be ideal if both the paying and the receiving officer endorse the receipts. All transactions are to be recorded in a cashbook, clearly showing income received and bank deposits.

Serving Members' Contributions

As already indicated, both Head Office and the individual sections are to use pre-printed general receipts which are individually numbered. It is also recommended that all payments received at a specific section, with receipts issued there from, are remitted accordingly. A reconciliation exercise is to be carried out on a regular basis to ensure completeness. If need be, separate records may be kept to show the employees allocated to their specific units, and whether contribution has been paid or not.

Handing over of Cash not substantiated

The handing over of money is to be accompanied by a record showing a detailed breakdown of the amounts in question. Surprise checks are also to be carried out on the receipts maintained by the officer in charge of the contributions to ensure accuracy of records and amounts submitted to the Accounting Officer.

Discrepancies between Monies Collected and Bank Deposits

Records are to be maintained in a way that enable reconciliation between the different sets of documents. It is recommended that the receipt number is used as a unique reference. This would provide a full audit trail from the collection of cash to its eventual deposit in bank. The cashbook shall also clearly indicate the receipt numbers supporting both the income received and the deposits effected.

Contributions paid in Cash

Management is encouraged to consider collecting the contribution through bank transfers simply by deducting the necessary amounts from the respective salaries. In addition to ensuring that all the monies are collected as they fall due, this will reduce significantly the workload of the officer in charge of contributions, since most of the tasks identified previously will be eliminated, while mitigating the risk of errors and abuse that very often is associated with cash.

Inaccurate Balance of Funds at Year-end

In order to have accurate and reliable information, enabling efficient and effective decision-making, it is recommended that funds that do not relate to the MPGF are remitted directly into the respective accounts.

Insufficient Control over Income for Mutual Help

Money intended for specific purposes is to be kept in separate accounts, ideally managed by different officers. Hence, more control will be exercised over the said funds, reducing the possibility that they are used for reasons other than those intended. Furthermore, this will also result in more accurate, reliable and up-to-date information, translating into effective and efficient decision-making.

Incorrect Payments and Other Administrative Shortcomings

Payments are to be computed on the basis of reliable and updated information, providing adequate audit trail to enable independent verification.

Misleading Accounting Information

It is recommended that financial records are drawn up in line with International Accounting Standards. Expenditure shall be accounted for in full, reporting one end figure of surplus or deficit. Ideally, a Statement of Financial Position, wherein all assets and liabilities, including prepayments, accruals, receivables and payables amongst others, shall accompany such financial records.

Christmas and Police Day Social Activities

It is recommended that expenditure incurred during such activities should be invariably contained within the limits of available financial resources.

As regards ORC, it is recommended that a thorough review of the items provided and respective prices is carried out, ideally after obtaining quotations from other commercial entities in order to ensure that the prices being charged are fair and reasonable. Orders are also to be placed in writing, enabling reconciliation of the invoice at a later stage. It is also recommended that thorough checks are carried out prior to effecting payment.

Compliance Issue

Financial Records not submitted to NAO for Auditing Purposes

The provisions of the law are to be complied with and records are expected to be submitted to NAO in a timely manner. Such a review is also to be considered as an exercise aimed at identifying areas for improvement. Actions to implement the recommendations provided in this Report are to be taken, thus ensuring that best practices are incorporated in day-to-day operations.

Management Comments

As at date of publication of this Report, no Management comments were submitted.

Co-operatives Board

Audit for Financial Year 2015

Background

The Co-operatives Board was established by virtue of Article 3 of the Co-operative Societies Act, 2001 (Cap. 442) of the Laws of Malta, as a statutory body having distinct legal personality. This Board consists of a Chairman and a number of members, appointed by the Minister for the Economy, Investment and Small Business, who is responsible for Co-operative Societies. The functions of the Board are to:

a. register, monitor and exercise supervision over Co-operative Societies and to ensure compliance with the provisions of the Co-operative Societies Act;
b. support and assist the establishment of Co-operative Societies in all sections of the economy and society; and
c. furnish information regarding co-operative principles, practices and management.

Article 9(2) of the aforementioned Act requires the Co-operatives Board to submit to the Minister and the Minister responsible for Finance, a statement of accounts duly audited by the Auditor General, and a report of its activities, by not later than three months after the end of each financial year.

The allocated budget of the Co-operatives Board for the financial year 2015 totalled €100,000.

Audit Scope

The scope of the audit was to ensure that the Financial Statements for the year ended 31 December 2015 show a true and fair view of the financial position of the Co-operatives Board as at that date, and of its financial performance and cash flows for the year then ended. Compliance with the Co-operative Societies Act, 2001, as well as the existence of adequate internal controls, was also ascertained.

Control Issues

Incorrect Accounting Treatment of Compensation due to a Former Employee

In 2014, a former employee of the Co-operatives Board sought remedy from the Grievances Unit, which was set up to investigate claims arising within the Ministry for the Economy, Investment and Small Business, for an injustice he allegedly suffered during his employment with the Board. The Grievances Unit upheld the employee's claim and communicated its decision to the Board on 19 October 2015, for the latter to pay

a compensation of €5,000. The Board immediately forwarded a part-payment of €1,000 to the aggrieved former employee, who was notified that the remaining balance of €4,000 would be settled in January 2016.

Although by the time of issuing the Financial Statements, the Co-operatives Board was aware that the total amount due to its former employee was of €5,000, only an expense of €1,000, representing the actual payment made in 2015, was recorded in the accounts. This resulted in the value of the Grievances Unit Compensation expense being understated by €4,000, with the Board's liability towards its former employee for the outstanding amount being completely omitted.

This accounting treatment was in conflict with the provisions of the International Financial Reporting Standards Conceptual Framework, which specifically requires liabilities to be "... *recognised in the balance sheet when it is probable that an outflow of resources ... ... will result from the settlement of a present obligation and the amount at which the settlement will take place can be measured reliably*". Similarly, the Framework also states that expenses are to be "... *recognised in the income statement when a decrease in future economic benefits ... ... can be measured reliably*".

Insufficient Documentation supporting Honoraria paid

Following a request for documentation in support of the *honoraria* paid to the Co-operatives Board's Members, the National Audit Office (NAO) was forwarded with a letter, dated 28 March 1996, issued by the Parliamentary Secretary within the then Ministry of Education and Human Resources. Through this letter, the Board was authorised to pay a total of Lm5,000 (equivalent to €11,647) as *honoraria* to its Members.

Furthermore, the Board forwarded correspondence exchanged with the former Ministry for Social Policy on 25 March 2003. This communication confirmed that the Chairperson received an annual remuneration of Lm2,000 (€4,659) and the remaining six Board Members were paid Lm500 (€1,165) each, whilst no *honorarium* was paid to the Secretary of the Board.

Since no further documentation was traced in relation to Board Members' *honoraria*, it was unclear whether the amount of €1,631 paid to the Secretary during the year under review was accurate and justifiable, and covered with appropriate approvals.

Shortcomings in the Engagement of a Financial Accounts Service Provider

On 1 March 2015, an Expression of Interest was issued for the provision of accountancy and audit services to the Co-operatives Board for a period of one year, which contract could be renewed. In a meeting held on 13 April 2015, the Board decided to retain the services of the incumbent financial accounts service provider, who was also one of the four applicants responding to the call, and whose offer was considered to be the most advantageous. The contract for a value of €4,000, covering the period 1 April 2015 to 31 March 2016, was signed on 11 May 2015, *i.e.* after its effective date. Furthermore, the agreement came into force prior to the Board's decision on the selection of the service provider. The agreement included a clause allowing the contracting parties to unanimously extend the contract, subject to approval by the Board.

Recommendations

Control Issues

Incorrect Accounting Treatment of Compensation due to a Former Employee

In order to comply with the respective provisions of the International Financial Reporting Standards Conceptual Framework, the Co-operatives Board is to adjust the Financial Statements to reflect the actual amount payable to its former employee, as well as the total compensation due.

Insufficient Documentation supporting *Honoraria* paid

The Co-operatives Board is to ascertain that it is in possession of official documentation confirming the total *honorarium* payable to each Board Member, including the Secretary to the Board, to ensure that the correct amounts are being paid.

Shortcomings in the Engagement of a Financial Accounts Service Provider

The Board is to ensure that any contracts with service providers are approved and signed before the engagement actually commences, thus ascertaining that all the applicable terms and conditions have been appropriately agreed beforehand.

Management Comments

Management concurred with most of NAO's observations and forwarded the following comments:

- Whilst reporting that the remaining balance of €4,000 was paid to the former employee in January 2016, the Board stated that the proposed audit adjustment would be reflected in the Financial Statements for the year ended 31 December 2015.

- To support the *honorarium* paid to the Board's Secretary, Management provided NAO with correspondence, dated 18 January 2011, between the Co-operatives Board and the former Ministry of Finance, the Economy and Investment. In the mentioned correspondence, the Board communicated the *honoraria* amounts of the Chairperson, Secretary and Members of the Co-operatives Board, with that pertaining to the Secretary amounting to €1,631 *per annum*.

- Management confirmed that a call for Expressions of Interest for the provision of accountancy and audit services, for the period 1 April 2016 to 31 March 2017, was issued on 14 February 2016. The Board's decision was taken on 30 March 2016 *i.e.* before the effective date, although the contract with the service provider was signed on 26 April 2016. The Board also commented that "... *Every effort will be made so that the recommendations are followed through for the period 2017 - 2018*".

- The Co-operatives Board confirmed that the clause allowing the contracting parties to unanimously extend the contract for the provision of accountancy and audit services was removed from the contract covering the period 1 April 2016 to 31 March 2017.

RECENT AUDIT REPORTS ISSUED BY THE NAO

NAO Audit Reports

November 2015	An Investigation into the Issuance of Encroachment Permits between December 2012 and March 2013
December 2015	Annual Audit Report of the Auditor General - Public Accounts 2014
December 2015	Annual Audit Report of the Auditor General - Local Government 2014
January 2016	An Investigation of Government's Expropriation of Two One - Fourth Undivided Shares of the Property at 36 Old Mint Street, Valletta
February 2016	Performance Audit: Agreements between Government and Conservatorio Vincenzo Bugeja on Jeanne Antide and Fejda Homes
February 2016	Performance Audit: Service Agreements between Government and INSPIRE Foundation
April 2016	Performance Audit: An Analysis on OHSA's Operations - A Case Study on the Construction Industry
May 2016	Information Technology Audit: Mater Dei Hospital
June 2016	The General Practitioner function - The core of primary health care
July 2016	An Investigation of the 2015 Local Councils' Capital Projects Fund
July 2016	An Investigation of Local Councils Funding Schemes launched between 2008 and 2013
September 2016	Performance Audit: Service Agreements between Government and Richmond Foundation Malta
October 2016	Performance Audit: Agreements between Government and YMCA Valletta
November 2016	Performance Audit: Managing and Monitoring the State Schools' Transport Service

NAO Work and Activities Report

March 2016	Work and Activities of the National Audit Office 2015