

Report by the  
*Auditor General*

Public Accounts 2013

MALTA

National Audit Office

200  
1814 2014

years of state auditing



# Annual Audit Report

**Public Accounts 2013**

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## List of Abbreviations

AAR	Annual Audit Report(s)
AFM	Armed Forces of Malta
AG	Attorney General
AIMS	Automated Information Management System
ARR	Arrears of Revenue Return(s)
ARS	Accounts Receivable System
BOT	Board of Trustees
BOQ	Bill of Quantity
CBM	Central Bank of Malta
CEC	Chief Electoral Commission
CEO	Chief Executive Officer
COJ	Courts of Justice
COLA	Cost of Living Adjustment
CPSU	Central Procurement and Supplies Unit
CTD	Capital Transfer Duty
CVB	Conservatorio Vincenzo Bugeja
DAS	Departmental Accounting System
DC	Department of Contracts
DCEA	Department for Citizenship and Expatriate Affairs
DMD	Debt Management Directorate
DSS	Department of Social Security
DSP	Department of Social Policy
EC	Electoral Commission
ECCD	Elderly and Community Care Department
EDA	Extra Duty Allowance
EIB	European Investment Bank
EO	Electoral Office
EODR	End of Day Report
ESA95	1995 European System of Accounts
ESM	European Stability Mechanism
EU	European Union
FC	Financial Controller
FMCU	Financial Management and Control Unit
FMS	Foundation for Medical Services
FR	Financial Report
FSS	Final Settlement System
GCCL	Gozo Channel Company Ltd
GDP	Gross Domestic Product
GF	Gozo Ferries Company Ltd
GGH	Gozo General Hospital

GHQ	General Headquarters
GPD	Government Property Department
GPDMA	Government Borrowing and Public Debt Management Act
HO	Head Office
HoD	Head of Department
HM	Heritage Malta
HMSL	Heritage Malta Services Ltd
HR	Human Resources
HS	Harmonised System
IAS	International Accounting Standard(s)
IRD	Inland Revenue Department
IT	Information Technology
KMS	<i>Kunsill Malti għall-iSport</i>
LA	Letter of Acceptance
LGA	Lotteries and Gaming Authority
LN	Legal Notice
LPO	Local Purchase Order
MCA	Malta Communications Authority
MDH	Mater Dei Hospital
ME	Malta Enterprise Corporation Ltd
MEDE	Ministry of Education and Employment
MEPA	Malta Environment and Planning Authority
MFA	Ministry of Foreign Affairs
MFEI	Ministry of Finance, the Economy and Investment
MFIN	Ministry for Finance
MFSS	Ministry for the Family and Social Solidarity
MGI	Malta Government Investments Ltd
MGS	Malta Government Stocks
MITA	Malta Information Technology Agency
MOC	Malta Olympic Committee
MPF	Malta Police Force
MRRA	Ministry for Resources and Rural Affairs
MSD	Manufacturing and Services Directorate
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
NSO	National Statistics Office
OPM	Office of the Prime Minister
PACBU	Public Administration Collective Bargaining Unit
PAHRO	Public Administration Human Resources Office
PDMAC	Public Debt Management Advisory Committee
PPR	Public Procurement Regulations
PS	Permanent Secretary

PSCC	Public Service Concession Contract
PSMC	Public Service Management Code
PSO	Public Service Obligation
PV	Payment Voucher
RHKG	Rehabilitation Hospital Karin Grech
RPI	Retail Price Index
SABS	Social Assistance and Benefits System
SL	Sick Leave
SPBH	Sir Paul Boffa Hospital
SSC	Social Security Contributions
SVPR	Saint Vincent de Paul Residence
TEC	Tender Evaluation Committee
TM	Transport Malta
TOIL	Time Off <i>In Lieu</i>
TVLU	Television Licensing Unit
UHM	<i>Union Haddiema Magħqudin</i>
UoM	University of Malta
VAT	Value Added Tax
VL	Vacation Leave
VMS	Vessel Monitoring System
ZCH	Zammit Clapp Hospital

# Guide to using this Report

This Report summarises the conclusions reached following our Financial and Compliance audits. 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 attempted to make this Report as user friendly as possible and 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 2013, 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.

## Key Issues

Highlights 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 should exist 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

Outline our suggestions to the respective Ministries and Departments so as 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 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 14), incorporating Financial Statements and Accounts for the year 2013, was submitted by the 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 *circa* €1,258 million (against *circa* €1,243 million in 2012). These constitute Contingent Liabilities for Government;
- substantial excess of actual over budgeted figures of various items of Expenditure was once again reported, these being similar to those reported last year. Budget Office's explanations 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 settle such amounts; and
- following the enactment of the new legislation governing Government's borrowing and public debt management, a number of measures will be implemented 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.

All Ministries/Departments submitted the **Arrears of Revenue Return** for 2013, required in terms of Treasury Circular No. 3/2014. However, similar to previous years, a review of these returns revealed several issues in the collectability of outstanding balances. (page 62)

An audit of expenditure at the **Electoral Office**, with particular consideration to payments in connection with duties carried out during the election period, revealed excessive expenditure. This was evident in the substantial extra payments paid to officials for performing election duties, both during and after office hours, at times over and above overtime payments. Moreover, a considerable amount of overtime was performed, which in cases even reached an average of 90% of employees' basic pay. A review of a sample of transactions also indicated that procurement by direct order was common practice. (page 102)

A revenue audit at **Heritage Malta** revealed a weak internal control system whereby checks carried out are considered as ineffective in a number of areas, leaving ample room for abuse and other undetected shortcomings. The concerns include no independent ticket scanning, high level of dependence on the integrity of front office staff and significant number of cancellations not supported by the actual physical ticket and source documentation confirming the request for cancellation. (page 122)

Substantial payments for services rendered to the **Kunsill Malti għall-iSport** were not adequately substantiated with the necessary supporting documents. Furthermore, procurement of the related services was not made in line with the Public Procurement Regulations. (page 132)

The **University of Malta and Junior College** ended the year with an adverse variance of €1,275,271 in **Capital Expenditure** when compared to the original budget, and a higher variance of €2,075,271 when compared to the revised budget. Cash flow shortfalls were being temporarily funded by delaying amounts payable to the Inland Revenue, in respect of income tax collected from employees' salaries and

National Insurance Contributions. A number of purchases were intentionally fragmented to bypass the Procurement Regulations. (page 140)

A review of expenditure of the **Ministry for Sustainable Development, the Environment and Climate Change**, revealed lack of sufficient audit trail and documentation, which precluded NAO from obtaining a good understanding of the facts that took place. Other shortcomings consisted of a retrospective approval for a variation order, non-adherence to Procurement Regulations with respect to consultancy services, as well as concerns of a compliance nature. (page 150)

The financial sustainability and going concern of **Gozo Channel Company Ltd** were very critical. A weak control environment prevailed within a number of areas. These included several expired contracts, weak budgetary control, inefficient utilisation of personnel, lack of control on overtime, and lack of synergy between the Management team, as well as between the various Units within the Company. (page 176)

An audit in relation to expenditure disbursed by the **Department of Social Policy** revealed several control weaknesses in relation to carriage and security services, which services could be indefinitely extended beyond the agreed periods. Testing also showed other weaknesses, such as retrospective agreements and late approvals in relation to legal services, as well as expired Bank Guarantees. (page 200)

During a revenue audit on **Social Security Contributions** due to Government, lack of appropriate and timely enforcement action by the **Inland Revenue Department**, over both Class One and Class Two contributions, was identified. Another shortcoming consisted of the existence of insufficient monitoring and follow-up of settlement agreements entered into with taxpayers in default. With regards to Class Two defaulters, the lacking enforcement measures was a result of insufficient collaboration between the Inland Revenue and Social Security Departments, concerning those taxpayers having adjustments for credits or exemptions. (page 206)

**Overtime** at **St. Vincent de Paul Residence** was being resorted to consistently. Substantial amounts were also expensed on **Allowances** paid to employees. The audit also revealed several internal control deficiencies including, but not limited to, unreliable attendance records and high accumulation of balances of Time Off *in Lieu*. (page 222)

An analysis of the expenditure incurred by **St. Vincent de Paul Residence** within the **Elderly and Community Care Department**, revealed that procurement was not always compliant with standing regulations. Food items were often procured following repetitive calls for quotations instead of public calls. In addition, substantial payments for Operational and Maintenance Expenses made in 2013, related to invoices outstanding from the previous year. The audit also identified inadequate internal controls to ensure efficient administration of public funds. (page 235)

The lack of appropriate internal controls during the payroll process exposed the **Police Department** to a number of errors leading to overpayment of **Salaries**. In addition, payment for overtime, which is not even authorised by the respective Permanent Secretary, substantially exceeded the budgeted amount. (page 242)

Procurement Regulations were not followed by the **Ministry for Finance**, when a retrospective direct order approval was resorted to, in order to settle outstanding payments for integrated marketing communications services. Furthermore, additional payments were effected in respect of other related services, through a direct order. The lack of proper verification of invoices and supporting documentation, pertaining to cleaning services, led to an overpayment of public funds. Audit testing also revealed shortcomings related to Government-owned vehicles and inventory. (page 250)

Minimal action was taken by **VAT Department** during 2013 to recoup outstanding **Eco-Contributions** on products, which resulted in waste, as listed in the Eco-Contributions Act, 2004. An overview of the

collection process of this tax, also revealed a discrepancy between payments received, as extracted from the Department's system, compared with income recorded in the Government's Departmental Accounting System, such that the completeness of revenue could not be ascertained. Shortcomings in the investigation process were also noted. (page 256)

The significant changes to the original contractual agreement of the Car Park and Traffic Management and External Security Services at **Mater Dei Hospital** led to considerable loss of revenue to Government. This shortfall amounts to over one million euro per year. Another major concern related to the lack of control on expenditure related to cleaning services, on which the hospital paid close to six million euro in 2013. (page 264)

The majority of procurement by **Rehabilitation Hospital Karin Grech** was not made in line with standing regulations. Fundamental internal controls in the various areas reviewed were non-existent, resulting in the inefficient use of public funds. (page 277)

Lack of evidence on the selection process of service providers was identified, during an audit of the financial statements of the **Co-operatives Board** for the years ended 2011, 2012 and 2013. (page 298)



**Audit Opinion**

# Audit Report to the House of Representatives

## Audit Mandate

In terms of 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 statements and accounts prepared by the Accountant General in terms of Article 67 of the Financial Administration and Audit Act, 1962, for the Financial Year under review.

## 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.

## Basis of Opinion

The Opinion only draws on conclusions upon areas that have been examined.

International Standards on Auditing (ISAs) and International Standards of Supreme Audit Institutions (ISSAIs) were followed in the conduct of the audits. These Standards require that audits are planned and performed to obtain reasonable assurance whether statements and accounts of Government Ministries and Departments, as well as of other entities which were subject to NAO audits, are free from material error.

An audit involves performing procedures to obtain relevant, reasonable and reliable audit evidence about the statements and accounts under review. The procedures selected depend on the auditors' judgement, including risk assessment, as well as an evaluation of internal controls.

## Opinion

In my opinion, except for the comments contained in this Annual Audit Report, the statements and accounts subjected to our audit were fairly presented in accordance with the stated accounting policies of 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 findings of the Report, I received all the information and explanations required for the carrying out of my duties.



Anthony C. Mifsud  
Auditor General  
10<sup>th</sup> December 2014



# Financial Report

# Analysis of the Financial Report 2013

## Introduction

Statements of the Consolidated Fund Account, showing the comparative positions in 2012 and 2013, and the receipts and payments of funds created by law, were laid on the Table of the House of Representatives during Sitting No. 138 on 7 April 2014, 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 2013 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 National Audit Office Act, 1997. The Report was laid on the Table of the House of Representatives during Sitting No. 183 on 22 July 2014.

Further details of Government financial operations can be found by making reference to both the Annual Financial Statements and FR for 2013.

## Consolidated Fund Statement – 2013

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 Estimates.

After the House of Representatives approved the year 2013 Budget (Estimates) for an expenditure of €3,631,409,395, as authorised by Warrant No. 2<sup>1</sup> issued on 17 April 2013, and a further €166,624,000 approved by Supplementary Estimates Warrant No. 3 dated 4 December 2013, it was estimated that such spending was to exceed revenue by €89,192,000. However, following the closure of the 2013 Accounts, it resulted that in actual fact expenditure had exceeded revenue by €14,983,000, as detailed in *Table 1*, leading to an end-of-year consolidated negative balance of €95,106,000.

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<sup>1</sup> This Warrant incorporates monies issued through Warrant No. 1 of 2013, to make adequate provision for the purpose of meeting expenditure necessary for carrying on Government's activities during 2013 in anticipation of the Annual Appropriation Act.

**Table 1: Consolidated Fund 2013**

	Estimated (Original & Supplementary)		Actual	
	€'000's	€'000's	€'000's	€'000's
Opening Consolidated Balance as on 1 January 2013				(80,123)
<i>Revenue</i>				
Ordinary (incl. Grants)	3,030,496		2,992,104	
Extraordinary	678,345	3,708,841	655,494	3,647,598
<i>Expenditure</i>				
Recurrent	(2,675,610)		(2,632,649)	
Public Debt Servicing	(616,099)		(608,712)	
Capital	(506,324)	(3,798,033)	(421,219)	(3,662,580)
Net Cash Flow		(89,192)		(14,983)
<b>Closing Consolidated Balance as on 31 December 2013</b>				<b>(95,106)</b>

Figures in Statement may not add up due to rounding up.  
(Source: FR 2013, page xvi)

*Table 2* hereafter shows the same end-of-year consolidated negative balance of €95,106,000 as in the Table above, highlighting figures relating to the Recurrent Deficit for 2013, amounting to €223,135,000, as well as the financing of present Foreign and Local Loans, totalling €418,931,000. This led to a total Public Sector Borrowing Requirement of €642,066,000, which was partly financed with the issue of new Local Loans, amounting to €627,084,000.



**Table 2: Consolidated Fund 2013**

	2013	
	€'000's	€'000's
Total Recurrent Revenue		2,992,104
Total Recurrent Expenditure	(2,860,554)	
Capital Expenditure	(354,686)	
Overall Expenditure		(3,215,239)
Recurrent Deficit		(223,135)
Financing (excluding New Loans)		
Foreign	(6,465)	
Local	(412,466)	
Total Financing		(418,931)
Public Sector Borrowing Requirement		(642,066)
Opening Consolidated Balance as on 1 January 2013	(80,123)	
Local Loans Issuance	627,084	
		546,960
<b>Closing Consolidated Balance as on 31 December 2013</b>		<b>(95,106)</b>

Figures in Statement may not add up due to rounding up.  
(Source: FR 2013, page xviii)

## Revenue

Details of Revenue collected during 2013, classified by heads and subheads, as compared with the Estimates, are shown in FR pages xix to xxi. Explanatory comments regarding variations between actual and budgeted revenue, as forwarded by the Ministry for Finance (MFIN) follow these details.

NAO 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 2013. Some of the major recognised variances are listed in *Table 3*. This is followed with detailed explanations for these variances, as provided by both Treasury and Budget Office.

**Table 3: Major Variances in Revenue for Financial Year 2013**

Revenue	Budget Estimates	Actual	Variation
	€'000's	€'000's	€'000's
<i>Tax Revenue</i>			
Indirect:			
Customs and Excise Duties	236,850	178,401	(58,449)
Licences, Taxes and Fines	253,828	223,992	(29,836)
<i>Local Loans</i>	650,000	627,084	(22,916)

(Source: FR 2013, pages xxii-xxiv)

### *Reasons for Variations*

#### *Indirect Tax Revenue - Customs and Excise Duties*

Revenue collection from Customs and Excise Duties was lower than anticipated, mainly due to excise on fuel, which was collected by Enemalta Corporation, but not passed on to Government in time prior to the closure of financial year 2013. Such dues are expected to be passed on to Government by means of a Payment Re-scheduling Programme with the Corporation. In this regard, NAO requested from Treasury supporting evidence that the amount due of €47,731,000 was actually passed on to Government and featured on the receivables side of Government's books when reporting in terms of the 1995 European System of Accounts (ESA 95). However, up to the writing of this Report, this Office did not yet receive such confirmation, on the premise that Treasury "... are still waiting for an updated version from the Customs Department".

Moreover, MFIN is expecting that the receipts in respect of fuel excise will materialise by the end-of-year 2014.

On the other hand, an effective shortfall was registered in excise duty namely on Machine-made Cigarettes, totalling €8,551,000, which reflects the market activity in the sector.

#### *Indirect Tax Revenue - Licences, Taxes and Fines*

The shortfall in revenue collection from Licences, Taxes and Fines of €29,836,000 was mainly due to the following reasons:

- a. A decrease in revenue from Motor Vehicle Registration Tax was registered in 2013, despite the fact that an increase in the number of registration of second-hand vehicles occurred. This resulted in older vehicles being registered during the year, attracting a lower registration tax since the higher the mileage, the less registration tax is paid.
- b. The 'assumed growth' in Duty on Documents comprised in the 2013 original projections did not materialise.
- c. A shortfall in Gaming Taxes reflecting actual activity that occurred during the year.
- d. A downward revision of the Bunkering Tax rate from that originally proposed at the time of the budget preparation.

### Local Loans

The Debt Management Directorate (DMD) within Treasury confirmed that the adverse variance of €22,916,000 resulted from the following decisions:

- a. A Bond Switch Operation conducted in December 2013, by which the nominal amount of €150 million was exchanged for a total nominal value of €147.8 million by auction on a bid price basis, in accordance with the terms of exchange as set in the prospectus. After this transaction, the total nominal outstanding balance of Malta Government Stocks (MGS) was reduced by €2.2 million.
- b. The enactment of the Budget Measures Implementation Act authorised Treasury to issue up to €650 million MGS for financial year 2013. However, the actual amount of MGS issued amounted to *circa* €629.3 million, leading to a shortfall of *circa* €20.7 million. Prior to the launching of the last issue of MGS, which is normally held in the last quarter of the year, DMD undertook a comprehensive analysis to determine the borrowing requirements up to the end of the year to ensure that borrowing is, as far as possible, limited to the actual borrowing requirements.

Based on the cash flow position prevailing at that point in time, and following the assessment of other risks, a final decision was taken on the amount of issuance, whilst at the same time keeping within the parameters of the budgetary projections and limits set by the law.

DMD further remarked that, in cases where Treasury has the adequate funds, it will not borrow more than it is required. In fact, during the final quarter of 2013, Treasury had adequate funds available to meet Central Government's financial requirements up to the end of the year, such that the final issue was of €180 million rather than €200 million.

### Expenditure

The appropriations for expenditure during 2013, authorised by the issue of MFIN Warrant Nos. 2 and 3, were made under the following Statutes:

	€
a. Appropriation Act	2,267,026,783
b. In terms of Special Laws	1,528,052,395
c. In terms of the Constitution	2,954,217

### Analysis of Appropriations

#### a. Appropriation Act

	€
Appropriated by Act I of 2013 (Original Budget)	2,128,265,783
Appropriated by Act XVII of 2013 (Supplementary)	138,761,000

#### b. Special Laws

The following amounts (including Supplementary Estimates as detailed in Warrant No. 3 of 2013) were appropriated in terms of the various laws as indicated:

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

Description	2013	2012
	€	€
Expenses of the Electoral Commission – General Elections Act (Cap. 354)	450,000	450,000
Expenses of the Broadcasting Authority – Broadcasting Act, 1992 (Act XII of 1991 – Cap. 350)	620,000	650,000
Expenses under Re-letting of Urban Property Ordinance (Cap. 69) and Agriculture Leases (Re-letting) (Cap. 199)	71,000	71,000
Land Acquisition (Public Purposes) Ordinance (Cap. 88)	110,000	110,000
Social Security Act, 1987 (Act X of 1987 – Cap. 318)	815,318,000	782,700,000
Pensions Ordinance (Cap. 93)	87,500,000	86,380,000
Expenses of the Office of the Ombudsman (Cap. 385)	750,000	824,000
Expenses of the Permanent Commission Against Corruption (Act XXII of 1988 – Cap. 326)	55,000	58,000
Interest plus contribution to the Sinking Funds in respect of Local Government Stock – Registered Stock and Security Ordinance 1959 (Cap. 161)	599,646,460	732,661,000
Interest plus contribution to the Sinking Funds in respect of Foreign Loans (Cap. 213)	9,279,935	10,068,000
Malta Arbitration Centre (Act II of 1996 – Cap. 387)	67,000	70,000
Expenses of the NAO (Act XVII of 1997 – Cap. 396)	2,265,000	2,300,000
Refunds under Value Added Tax/Customs & Excise Tax Acts	1,618,000	1,398,000
Widows' and Orphans' Pensions Act (Cap. 58)	500,000	500,000
Personal Injuries (Emergency Provisions) Ordinance (Cap. 111)	55,000	55,000
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)	1,410,000	1,400,000
Short Term Borrowing – Treasury Bills Act (Cap. 133)	5,750,000	7,000,000
€56,378,732 Interest payable on ex Malta Drydocks/Malta Shipbuilding Co. Ltd Loans (Act XV of 2003)	2,247,000	2,253,000
Lease of Parliament Building – Budget Measures Implementation (Act V of 2012)	340,000	-
<b>Totals</b>	<b>1,528,052,395</b>	<b>1,628,948,000</b>

Following queries forwarded to the Budget Office, 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 €32,618,000 in 2013 over the previous year's budget was due to the natural increase in load of social benefits from one year to the following, and the €4.08 cost of living adjustment due to each of the beneficiaries.

*Pensions Ordinance (Cap. 93)*

A higher budgetary allocation over the previous year, totalling €1,120,000, was provided to cover the actual number of pensioners and beneficiaries.

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

When the 2013 Financial Estimates were compiled, a budgetary allocation amounting to €340,000 was provided to accrue for December 2013 lease of the new Parliament building. No such lease was due in 2012, and hence no budgetary allocation was required for the previous year.

*Refunds under Value Added Tax/Customs & Excise Tax Acts*

The 2013 total budgetary allocation of €1,618,000 also catered for refunds due to diplomats, third country tourists, and disability equipment programmes.

*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)*

The increase in budgetary allocation of €10,000 was necessary to cover the growth in the actual number of beneficiaries in 2013.

*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	73,203
The Attorney General	71,051
Judges and Magistrates	2,739,866
The Public Service Commission	<u>70,097</u>
	<b><u>2,954,217</u></b>

*Budgetary Procedure for 2013*

Following NAO query, Budget Office provided a detailed description of the main elements, comprising the 2013 budgetary process, as outlined below.

The top-down<sup>2</sup> approach for budgetary allocations has been adopted for the past years and continued being adopted in 2013. This process commenced through MFEI Circular No. 6/2012 ‘2013 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 for the year 2013.

To achieve the set target of reduction in the projected General Government deficit by a further 0.5 percentage points of Gross Domestic Product (GDP) in 2013, and given that Government 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.

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 Circular, would adversely impact the core workings of the respective Ministries, Departments and Entities.

<sup>2</sup> This means that the Ministry for Finance sets the overall expenditure ceiling and sub-ceilings, and delegates detailed resource allocation decisions to line Ministries.

### *Supplementary Expenditure*

Budget Office confirmed that the same procedure, which was explained in detail in last year's Annual Audit Report (AAR), was again followed in 2013.

As the financial year progresses, cases arise where, for line Ministries to be in a position to continue providing the public services for which they are responsible, following unforeseen and/or unavoidable financial requirements, supplementary funds are required to be provided in addition to the amounts voted in the Financial Estimates. Owing to the prevailing budgetary constraints, the first thrust is to identify savings within the same Vote, as contemplated in the Financial Administration and Audit Act, to offset such additional spending.

There are instances where the requesting Ministry is also asked to explore the possibility of savings within Votes pertaining to Departments within its portfolio. Furthermore, and as far as is possible, any additional funds are compensated by lower expenditure across Government, or improved revenue collection over the approved targets, so that the adverse effect of any supplementary funding is mitigated and kept within the parameters of the financial framework for that year.

Thus, supplementary funding is only provided as a last resort. It is presented to the House of Representatives in terms of the Financial Administration and Audit Act, generally immediately following the presentation of the Budgetary Estimates for the forthcoming year.

### *Excess of Expenditure over Estimates*

The Supplementary Estimates contributed in part to the overall fiscal outcome for 2013, with the other contributing element being revenue performance. *Table 5* portrays those votes whose expenditure exceeded budgeted figures, by well over €1 million.

**Table 5: Excess of Expenditure over Original Budget by Vote**

<b>Vote</b>	<b>Original Budget 2013</b>	<b>Actual 2013</b>	<b>Variation Actual 2013/ Original Budget 2013</b>
	€	€	€
<b>Recurrent Expenditure</b>			
Vote 9: Electoral Office	5,825,000	8,156,142	2,331,142
Vote 16: Education	177,215,000	182,784,467	5,569,467
Vote 25: Social Policy	220,873,000	222,339,114	1,466,114
Vote 26: Social Security Benefits	787,700,000	814,457,236	26,757,236
Vote 28: Elderly and Community Care	62,578,000	66,433,915	3,855,915
Vote 37: Ministry for Finance	88,406,000	104,587,639	16,181,639
Vote 47: Ministry for Health	354,368,000	374,812,999	20,444,999
<b>Capital Expenditure</b>			
Vote I: Office of the Prime Minister	13,602,000	16,123,680	2,521,680
Vote II: Ministry for European Affairs and Implementation of the Electoral Manifesto	11,854,000	14,482,892	2,628,892
Vote IV: Ministry for Tourism	18,827,000	20,757,277	1,930,277
Vote V: Ministry for Education and Employment	41,168,000	51,114,740	9,946,740
Vote XIII: Ministry for Finance	71,456,000	83,648,416	12,192,416
Vote XIV: Ministry for Energy and the Conservation of Water	542,000	12,110,548	11,568,548
<b>Totals</b>	<b>1,854,414,000</b>	<b>1,971,809,065</b>	<b>117,395,065</b>

(Source: FR 2013, pages xi-xiv, 56-186)

Excess expenditure over original budgeted figures exceeding €1 million occurred in the Line Items shown in *Table 6*. The same Line Items experienced a similar excess of expenditure during 2012, as portrayed in the same Table.

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

Vote, Item	Original Budget 2013	Revised Estimates 2013 <sup>3</sup>	Actual 2013	Variation Actual 2013/ Revised Estimates 2013	Variation Actual 2013/ Original Budget 2013	Variation Actual 2012/ Original Budget 2012
	€	€	€	€	€	€
Vote 9: Electoral Office						
Item 5219: Electoral Commission Activities	4,000,000	6,400,000	6,349,605	(50,395)	2,349,605	1,352,144
Vote 16: Education						
Item 12: Salaries and Wages	136,540,000	139,240,200	139,625,238	385,238	3,085,238	2,266,719
Item 16: Allowances	8,220,000	12,220,000	10,118,585	(2,101,415)	1,898,585	1,299,947
Vote 26: Social Security Benefits						
Item 5141: Retirement Pensions	400,400,000	410,900,000	410,957,617	57,617	10,557,617	18,364,815
Item 5143: Bonus	56,300,000	59,710,000	59,456,128	(253,872)	3,156,128	10,548,788
Item 5145: Widows' Pensions	111,000,000	113,700,000	113,693,291	(6,709)	2,693,291	1,530,782
Item 5149: Social Assistance	70,000,000	74,570,000	75,317,345	747,345	5,317,345	3,714,332
Vote 28: Elderly and Community Care						
Item 16: Allowances	5,700,000	8,670,000	8,585,641	(84,359)	2,885,641	2,035,330
Vote 37: Ministry for Finance						
Item 5410: European Union Own Resources	67,000,000	86,200,000	86,126,175	(73,825)	19,126,175	1,459,701
Vote 47: Ministry for Health						
Item 16: Allowances	44,016,000	51,616,000	51,907,773	291,773	7,891,773	3,866,649
Item 30: Contractual Services	21,002,200	27,202,200	27,290,489	88,289	6,288,289	2,182,039
Item 5400: Medicines and Surgical Materials	68,000,000	75,000,000	76,980,807	1,980,807	8,980,807	7,669,743

<sup>3</sup> Revised Estimates are made up of the Original Budget 2013 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 2013	Revised Estimates 2013 <sup>3</sup>	Actual 2013	Variation Actual 2013/ Revised Estimates 2013	Variation Actual 2013/ Original Budget 2013	Variation Actual 2012/ Original Budget 2012
	€	€	€	€	€	€
Capital Vote V: Ministry for Education and Employment  Item 7211: European Union Structural Funds 2007 - 2013	24,814,000	37,814,000	41,615,864	3,801,864	16,801,864	2,767,740
Capital Vote VI: Ministry for Sustainable Development, the Environment and Climate Change  Item 7218: European Union Agricultural Fund for Rural Development	12,939,000	12,939,000	14,699,802	1,760,802	1,760,802	9,735,860
Capital Vote XIII: Ministry for Finance  Item 7235: Investment – Equity Acquisition	51,796,000	65,617,999	66,533,759	915,760	14,737,759	33,292,006

Budget Office submitted the following reasons for the repeated excess expenditure over original budgeted figures of the Line Items outlined in the Table above.

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

An additional amount of €2,400,000 was necessary in connection with the Electoral Commission's activities required during the year. The main reasons for the provision of additional funds included the cost of extra flights, communication facilities, as well as works and services by Government Departments and Entities; including Police, Works Department and Enemalta Corporation.

*Vote 16: Education - Item 12: Salaries and Wages*

Supplementary funds of €2,700,000 were resorted to provide emoluments in respect of staff in post, according to the respective Collective Agreements. The additional funds made available included the provision to cover recruitment effected by Education.

*Vote 16: Education - Item 16: Allowances*

Additional funds of €4 million were made available for the same reasons as in Salaries and Wages. However, as noted in FR and Tables, an amount of €2,101,415 out of these supplementary funds was not utilised by year-end.

*Vote 26: Social Security Benefits - Item 5141: Retirement Pensions; Item 5143: Bonus; Item 5145: Widows' Pensions and Item 5149: Social Assistance*

Additional aggregate funding amounting to €21,180,000 in respect of the above-mentioned Items were required to cover a higher expenditure according to the actual number of beneficiaries in receipt of the respective assistance. These amounts were appropriated in terms of the Social Security Act, 1987.

*Vote 28: Elderly and Community Care - Item 16: Allowances*

Owing to Public Service and Sectoral Collective Agreements' requirements, it transpired that additional funds of €2,970,000 were required to cover payment of clinical and non-clinical staff for the running of the sector, comprising also its residences for the elderly.

*Vote 37: Ministry for Finance - Item 5410: European Union Own Resources*

An additional amount of €19,200,000 was necessary to cover 'expected' payments due to the European Union (EU) up to year-end, according to latest claims and forecasts received. The main part of these supplementary funds provided were due to cover "VAT and Gross National Income based adjustments, the UK Correction and OPT-Out payable to the European Commission".

NAO thus questions why the Ministry had to resort to Supplementary funding, since the Ministry's justification stated that these payments were 'expected'.

*Vote 47: Ministry for Health - Item 16: Allowances*

Additional funds of €7,600,000 have been provided for amounts requested up to year-end in terms of Collective and Sectoral Agreements, as well as recurrent requirements.

*Vote 47: Ministry for Health - Item 30: Contractual Services*

An additional supplementary amount of €6,200,000 was approved to cover actual requirements under this Item for the provision of contractual services, comprising the provision of clerical services, security services, parking services, laundry services, patient meals, cleaning services, staff meals, social workers and carers.

*Vote 47: Ministry for Health - Item 5400: Medicines and Surgical Materials*

A total of €7 million supplementary amount was made available for the procurement of medicinal and surgical materials to meet ongoing commitments, as requested by the Health authorities.

*Capital Vote V: Ministry for Education and Employment - Item 7211: European Union Structural Funds 2007 - 2013*

Extra funds owing to absorption capacity and implementation rates resulting as the year progressed, were met through a supplementary amount of €13 million, together with offsetting unexpected funds anticipated under other Items within the same Capital Vote. Part of these funds were reimbursable from EU and the

projects involved included ‘Quality Education for the Society of Tomorrow’, ‘MCAST Master Plan’, ‘Employment Aid Programme’ and ‘Employability Programme’.

*Capital Vote VI: Ministry for Sustainable Development, the Environment and Climate Change - Item 7218: European Union Agricultural Fund for Rural Development*

An additional balance of €1,760,802 was actually spent during 2013, over and above the budgeted aggregate of €12,939,000. This additional amount, partly reimbursable by EU, was required due to absorption capacity and implementation rates occurring as the year progressed. The projects benefiting from these funds included ‘Modernisation of Agricultural Holdings’, ‘Natural Handicap Payments’, ‘Agri-Environment’, ‘Tourism Activities’, as well as ‘Conservation and Upgrading of the Rural Heritage’.

*Capital Vote XIII: Ministry for Finance - Item 7235: Investment – Equity Acquisition*

Additional funds of €13,821,999 were mainly provided to cover Government’s contribution to the European Stability Mechanism (ESM) and a transfer of the contribution towards the European Investment Bank (EIB), amounting to €11,704,000 and €2,118,000 respectively.

As regards the latter amount, Budget Office remarked that it previously featured under Item 5429 ‘European Investment Bank’ of the Ministry’s Recurrent Vote. A suppression of funds from the latter was carried out and an equivalent amount was made available under the Capital Vote.

Budget Office confirmed that all efforts shall continue to be made towards ensuring that such excesses are kept at a minimum. Containment of expenditure by line Ministries, Departments and Entities has also been given higher priority through the recently introduced Fiscal Responsibility Act (Cap. 534).

## **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 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**

	2013	2012
	€'000's	€'000's
<b>Public Credit</b>		
Shareholding	501,852	389,761
Other Investments	453,689	453,439
Loans	<u>108,145</u>	<u>108,175</u>
	<u>1,063,415</u>	<u>951,375</u>
<b>Investments held on behalf of</b>		
Sinking Funds (Local)	69,330	93,018
Sinking Funds (Foreign)	29,593	34,049
Trust Funds	<u>1,646</u>	<u>1,545</u>
	<u>100,569</u>	<u>128,612</u>
<b>Advances</b>		
Advances	<u>137,877</u>	<u>140,042</u>
<b>Bank and Cash</b>		
Banks <sup>4</sup>	5,742	4,179
Central Bank of Malta – Public Account	<u>86,396</u>	<u>7,108</u>
	<u>92,138</u>	<u>11,286</u>
<b>TOTAL ASSETS</b>	<b><u>1,393,998</u></b>	<b><u>1,231,315</u></b>

Figures in Statement may not add up due to rounding up.

(Source: FR 2013, page 212)

### Public Credit – Shareholding

The value of direct investments, as shown in FR as at 31 December 2013, stood at €501,581,806, as against €389,760,603 in 2012. This was made up of €242,588,512 paid-up part of unquoted shares valued at purchase cost, and €258,993,294 quoted shares, which have been valued at market price as at year-end. The nominal value of shares denominated in British Pounds (£41,339) and United States Dollars (\$138,630,753) remained unchanged from 2012.

The following were the major changes in Treasury Clearance Fund/Consolidated Fund investments during the year, as noted through comparison between data as per FR 2013 and the preceding year:

<sup>4</sup> Consists of bank accounts held by foreign Embassies/Commissions and the National Lottery Good Causes Fund bank account.

## ***New Investment***

### *Malta Public Transport Services Ltd*

Malta Public Transport Services Ltd was registered as a Limited Liability Company, as per Certificate of Registration dated 30 December 2013, to operate the bus service in Malta and Gozo.

According to the Memorandum and Articles of Association, the authorised and issued share capital of the company was one million Ordinary Shares of €1 each, divided into 999,999 Ordinary Shares of €1 each held by Government of Malta, and one Ordinary Share of €1 held by Malta Government Investments Ltd (MGI). As at year-end, Government fully paid up this investment.

## ***Increase in Investments***

### *Air Malta p.l.c.*

As part of the Restructuring Plan approved by the European Commission, approving the Government of Malta to take up €130 million shares in the company as restructuring aid, Government further subscribed to 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. The offer was subject to acceptance by 15 January 2013, and in accordance with the Subscription Agreement dated 6 October 2012 entered into between Government of Malta and Air Malta p.l.c. As a result, by end-of-year 2013, Government paid-in the cash sum of €24,024,000, equivalent to 46.2% 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 2013 in respect of the unpaid part of the aforementioned Ordinary Shares, led to an increase of €16 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 2013, reached 99.98%.

### *Bank of Valletta p.l.c.*

In a Board resolution dated 19 December 2012, 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 30 million fully paid Ordinary Shares with a nominal value of €1 per share.

On the basis of the allocation ratio of one bonus share for every nine shares held, a total amount of 7,569,035 Ordinary Shares were allotted to Government. To this effect, the nominal value of the investment as at 31 December 2013 amounted to €75,690,351.

### *European Investment Bank*

With reference to the decision of EIB's Board of Governors taken on 31 December 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 2013, the first instalment of €2,117,750 was paid, representing 50% of the total share of the capital increase, bringing Government's aggregate paid-in capital by the end of the year to €7,039,225.

Moreover, as per confirmation dated 19 February 2014, the nominal value of Malta's share in the subscribed capital of EIB as at end-of-year 2013 stood at €102,665,000.

### *European Stability Mechanism*

As established in ESM Treaty and subsequent decisions, ESM Members were requested to provide the third and fourth instalments of ESM paid-in capital during 2013.

To this effect, during the year under review, Malta effected a further two tranches due to ESM, which amounted in total to €23,392,000, as paid-in capital. As at year-end, the total paid-up share capital of €46,784,000 represented approximately 9% of the 5,117 authorised share capital, of which, 584.8 are paid-in shares and the remaining 4,532.2 shares are callable.

### *Movements in Values of Existing Investments*

During 2013, 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,

decreased by €438,253 due to changes in United States Dollar exchange rate.

## **Public Credit – Other Investments**

### *Investment in Industry*

A Return submitted by MGI to the Accountant General showed that the total cost of investment in 38 companies amounted to €13,597,358 as at 31 December 2013.

MGI estimated that the net book value of these investments amounted to €11,884,399, after an accumulated provisional loss of €1,712,954. Further details are provided in *Table 8*.

**Table 8: Investments through Malta Government Investments Ltd**

<b>Investment Type</b>	<b>No. of Companies</b>	<b>Cost</b>	<b>Provisional Loss</b>	<b>Net Book Value</b>
		€	€	€
Subsidiary Companies	20	12,140,481	606,502	11,533,976
Associated Companies	2	1,455,858	1,106,452	349,406
Other Companies of Minority Interest	16	1,019	-	1,019

The Return also indicated that seven of these companies were undergoing liquidation procedures and another two never commenced operations.

At the end of 2013, the total of investment in industry, as reported by Treasury, amounted to €13,619,732 as against €13,369,735 on 31 December 2012, an increase of €249,997 over the previous year. Such movement was due to a further increase in the shareholding in Ricasoli Tank Cleaning Ltd.

It is to be noted that indirect investments at year-end, as reported by Treasury, amounting to €13,619,732, do not tally with MGI aggregate balances reported, standing at €13,597,358. The difference of €22,374

between Treasury's and MGI's records warrants mostly of an investment of €22,362 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 2013, the Central Bank of Malta (CBM) issued Euro Coin on behalf of Treasury totalling €5,181,000 bringing the total amount of Euro Coins in circulation as at 31 December 2013 to €55,279,000.

### ***Dividend/Profit Received***

#### ***Central Bank of Malta***

During the year under review, a total of €48 million was received in six tranches from CBM, consisting of 2012 Net Profits due to Government.

#### ***Investment in Industry***

During 2013, Treasury recorded an amount of €2,500,000 as dividend received. Out of this amount, €500,000 pertained to Malta Air Traffic Services Ltd.

#### ***Malta Financial Services Authority – Capital Fund***

Total surplus funds amounting to €10 million were received in two tranches from the Malta Financial Services Authority during 2013, in terms of Section 26(3) of the Malta Financial Services Act (Cap. 330).

Of this amount, €1,910,015 represented the remaining balance due out of surplus funds for the financial year 2012, whilst the balance of €8,089,985 related to payments on account in respect of surplus funds for 2013.

### ***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 Accountant General.

It is to be noted that Government Securities Board meetings, initially set on 25 August, 3 and 29 October, as well as 3 November 2014, were cancelled. The meeting was eventually held on 4 November 2014, in which the Board verified the correctness of security details against documents including, where available, official Stock Certificates issued by the company concerned, Malta Stock Exchange Statements, and other related documents maintained by Treasury. NAO observed that this meeting progressed with the absence of the Malta Investments Management Company Ltd representative. Nonetheless, he signed the List of Securities following the closure of the said meeting and in the absence of NAO officials.

## Public Credit – Loans made by Government and Repayments thereof

Balances and other details of all loans issued by Government as on 31 December 2013 as reported in Appendix E of FR 2013, are summarised as follows:

	€
a. Loans under Act II of 1956	23,099
b. Other Loans	108,121,999

Other Loans at (b) consist of the following:

	€
Aids to Industries Scheme	3,718
Agriculture – Assistance to Co-Operatives	66,620
Water Services Corporation	4,967,885
Loan Facility Agreement with the Hellenic Republic	50,683,923
Loan Facility Agreement with Air Malta plc	52,000,000
Loan – Mariam Al Batool	399,854

(Source: FR 2013, page 194)

### *Decrease in Loans*

#### *Agriculture – Assistance to Co-Operatives*

A repayment of €30,282 was made by the Farmers (Wine) Co-Operative Society Ltd during 2013, prior to initiation of the Society's liquidation process. This repayment was incorrectly classified under 'Issues' in the Statement of Loans made by Government in FR. However, since entry under the 'Issues' column was made as a negative amount, this classification error did not affect the balance of the loan as at year-end.

A total remaining 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.

### *Existing Loan Agreement*

#### *Water Services Corporation*

The loan to the Water Services Corporation 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 Government's subvention is still required. The initial amount of the loan was of €10,482,180.

No loan repayments were effected in the years 2008 to 2013. Furthermore, previous repayments were, either charged from grants to the Water Services Corporation or set-off against the Corporation's bills, mainly from the then Malta Drydocks.

#### *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 2013 amounted to €50,683,923. The principal repayments are scheduled 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 falls due in January 2015, whilst the remainder sum of €12 million is payable a year after.

Moreover, the Government is committed to take up 130 million ordinary shares of €1 each, in two tranches of 78 million and 52 million respectively. 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 28 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 are scheduled at a rate of €25,000 at end of each quarter for the period March 2014 to December 2017.

## **Investments held on behalf of Sinking Funds**

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

**Table 9: Sinking Funds Investments**

<b>Investment</b>	<b>Sinking Funds – Local</b>	<b>Sinking Funds – Foreign</b>
	€	€
Central Bank of Malta Deposit Accounts	27,685,043	29,592,519
Malta Government Stocks	41,645,008	-
<b>Totals</b>	<b>69,330,051</b>	<b>29,592,519</b>

(Source: FR 2013, page 207)

## **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 2013, in respect of advances made to various Government Departments, Agencies and Organisations.

Pending advances were reported as amounting to €137,876,589 as on 31 December 2013, as against €140,042,146 outstanding by the end of the previous year.

*New Advance*

According to FR 2013, Appendix L, three new Advance Warrants for the amount totalling €23,585,464 were issued during 2013. The following table refers:

**Table 10: New Advances**

Description	Amount
	€
Social Security Benefits	11,860,092
European Union Own Resources	10,913,238
Payments of Termination Benefits to Holders of Political Office and Secretariats Staff	812,132
<b>Total</b>	<b>23,585,462</b>

Figures in Statement may not add up due to rounding up.

*Advances Repaid*

Three advances amounting to €18,725,554 were fully repaid during the year. The following table refers:

**Table 11: Advances Repaid**

Description	Amount
	€
Malta Drydocks Corporation – 1999	7,000,184
European Union Own Resources	10,913,238
Payments to Termination Benefits to Holders of Political Office and Secretariats Staff	812,132
<b>Total</b>	<b>18,725,554</b>

### Outstanding Advances

Outstanding advances as at 31 December 2013, apart from advances forwarded to the former Malta Drydocks Corporation and Malta Shipbuilding Co. Ltd, were the following:

**Table 12: 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	2,099,539
Commissioner of Inland Revenue, to meet loans in terms of Article 4 of the Monte Di Pietà' Act (No. XXXIX) of 1976	330,751
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, in the first instance, out of proceeds forthcoming from the eventual privatisation of the same Company, immediately such proceeds become available to Government. In the second instance, in the event that such funds are not sufficiently available, out of funds made available from the Consolidated Fund upon the privatisation of the Company	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	10,977,644
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	2,014,927
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 for Information Technology and Investment, to enable Gozo Channel Co. Ltd to settle urgent debts, including social security contributions and income tax (FSS) payments	291,172
Ministry of Finance, the Economy and Investment for the purpose of extending loan Facilities to Mariam Al Batool School	399,854
Ministry for the Family and Social Solidarity, for the payment in advance of social security benefits	11,860,092
<b>Total</b>	<b>64,622,071</b>

### 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 Corporation Ltd (ME) as due to Government.

This advance will continue to be pursued within the context of pending legal proceedings that were initiated against a local holding company. This company entered into a deed of sale in 1997. Legal proceedings covered outstanding dues to ME and the unfulfilled obligations for the development and operation of a new hotel complex. MFIN confirmed that this matter is still being pursued by ME, and there were no further developments during the year under review.

*Bank of Valletta Employees Foundation - €2,099,539*

MFIN stated that the Ministry continued to pursue the repayment of this advance by means of various communications.

*Loans in terms of the Monte Di Pieta' Act, 1976 - €330,751*

This advance is administered by the Capital Transfer Duty Department in terms of the Monte Di Pieta' Act, 1976. During 2013, repayments made in respect of this Advance totalled €25,650.

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

MFIN confirmed that the situation as reported last year in AAR still prevails. This means that the amount advanced is planned to be repaid out of the proceeds forthcoming from the eventual privatisation of the Mediterranean Offshore Bunkering Co. Ltd.

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

MFIN informed NAO that it is continuing to pursue the repayment of this Advance through annual installments, together with possible renegotiation with the Foundation of the original terms under which the Advance was granted.

*Malta Freeport Loan Servicing - €10,977,644*

According to MFIN, this Advance will continue to be repaid out of the annual budgetary provision under Item 7189 'Contribution towards Treasury Clearance Fund' of MFIN Capital Vote. During 2013, a repayment was made in respect of this Advance, amounting to €3,000,000.

*Malta Freeport Privatisation Process, Malta Freeport Equipment Claims and Purchase of Medigrain Shares from Mid-Med Bank p.l.c. - €2,118,836, €10,482,180 and €2,014,927 respectively*

As confirmed in last year's AAR, MFIN restated that these advances are planned to be repaid out of an 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.

*Gozo Channel Co. Ltd - €291,172*

Originally, the Advance Warrant had to be repaid by 31 March 2005, as stipulated by the same Warrant.

In July 2004, MFIN, in agreement with Gozo Channel Co. Ltd, compiled a new schedule of interest and capital repayments, for the Advance amount of €1,164,687, which was to be completely repaid by 2013.

As reported in last year's AAR, no payments were affected by Gozo Channel Co. Ltd to honour its dues, even though reminders were sent by the Ministry. MFIN stated that it will continue to pursue repayment of this Advance within the context of the financial position of the Company.

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

Following last year's issue of a new advance in favour of Mariam Al Batool School for the purpose of extending loan facilities, resulting in a total amount advanced of €399,854, MFIN stated that Government's programme is being kept in view when considering the outstanding amount due on this Advance.

#### **Other Outstanding Advances**

Pending advances to be repaid out of the 'Contribution towards Treasury Clearance Fund' are listed in *Table 13*.

**Table 13: 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 – 2000	21,623,291
Malta Drydocks Corporation – 2001	29,987,336
<b>Total</b>	<b>73,254,517</b>

MFIN confirmed that the above advances will continue to be repaid out of an annual budgetary provision under Item 7189 'Contribution towards Treasury Clearance Fund' of MFIN Capital Vote. In fact, as indicated in the 2013 FR, an amount of €14,000,000 has been repaid. This amount included €7,000,184 towards the settlement of the advance of Malta Drydocks Corporation – 1999.

#### **Central Bank of Malta Public Account**

As regards the Reconciliation for the Public Account for the period June 1992 to December 2001, Treasury's position remained the same as detailed in the 2010 AAR.<sup>5</sup>

The €5.5 million discrepancy between the reconciled balance as per CBM statement and the balance as per Cash Book, noted in the May 2013 Bank Reconciliation Statement, is, according to Treasury, due to "... *fixes consisting of amounts reconciled across databases (prior Euro) and close-offs*". The last monthly Reconciliation Statement for the Public Account submitted by Treasury, was in respect of May 2013.

<sup>5</sup> 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.

### ***Developments on the ‘new’ Bank Reconciliation Statement***

As at beginning of October 2014, Treasury confirmed that the new Bank Reconciliation Report was introduced for the reconciliation month of January 2012 and that the multiple matching facility was up and running as from the reconciliation month of November 2012.

Treasury pointed out that the ‘new’ Bank Reconciliation Statement is currently being used to identify past discrepancies and enable users to reconcile balances in a more effective manner. It also provides details with regards to unreconciled items, thus facilitating the identification of discrepancies. The value of cancelled cheques in the accounting system is now also being disclosed.

### ***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 2013.

This Office received the Report prepared by the Board of Survey at the Ministry for Gozo, on 4 March 2014. The Board had no adverse remarks to make.

On the other hand, the Board of Survey at Treasury met in mid-November 2014 to certify the correctness of the relevant statements since the Government Securities Board approved the 2013 List of Securities held at Treasury late in the year on 4 November 2014. The former Board confirmed that the Cash Book balance and the bank balance in the report agree with DAS and the Public Account bank statement balance respectively.

### ***Ministerial/Departmental Bank Accounts***

Treasury Circular No. 1/2014, ‘End of Year (2013) Statements of Account Cash and Bank Balances held at Commercial Banks and Central Bank of Malta’, issued on 16 January 2014, 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 2013, 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. It is to be noted that officers were instructed not to input the requested information in the previous Bank Accounts Database.

The respective balances were published in FR 2013 (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 noted in respect of the latter, was reported in the FR, in relation to the Education Department, which had overdrawn balances on some of its accounts.

Despite that Treasury sent a number of reminders to the Ministry for Health, to submit the above mentioned soft and hard copies of the cash and bank balances as at 31 December 2013, the latter still failed to comply. This was reported as a defaulter in FR accordingly.

NAO noted that with respect to a bank account held by the Ministry for Foreign Affairs, a balance of €185,949 was reported as a credit balance in the list of foreign bank accounts, as per Return submitted to Treasury for 2013. However, the bank statement as at 31 December 2013 showed a ‘Nil’ balance. Consequently, the amount of €185,949 was erroneously featured in FR, as confirmed by the Ministry for Foreign Affairs. Upon enquiry, the Ministry confirmed that the Euro Cash Book of the Consulate is ‘Nil’.

In 2011 AAR, NAO reported that Treasury had plans to discuss their data with the National Statistics Office, within the context of the System of National Accounts and the Financial Accounts that the latter produces on a quarterly basis. To this effect, Treasury once again confirmed that it could not undertake a thorough analysis of such data due to the high turnover of staff that occurred at the beginning of the year under review, which necessitated the redistribution of work in accordance with departmental priorities and critical processes.

## Liabilities

Table 14 features the Statement of Liabilities.

**Table 14: Statement of Liabilities**

	2013	2012
	€'000's	€'000's
<b>Public Debt</b>	<b>4,718,202</b>	<b>4,469,988</b>
<b>Euro Coins issued on behalf of Treasury</b>	<b>55,279</b>	<b>50,098</b>
<b>Treasury Bills</b>	<b>247,407</b>	<b>153,224</b>
<b>Deposits</b>		
Court and Other Deposits	76,462	76,975
Other	23	23
	<b>76,486</b>	<b>76,998</b>
<b>Funds</b>		
Sinking Funds	98,923	127,068
Contingencies Fund	1,165	1,165
Trust Funds	1,708	1,609
	<b>101,796</b>	<b>129,842</b>
<b>Total Liabilities</b>	<b><u>5,199,169</u></b>	<b><u>4,880,150</u></b>
<b>Excess of Total Liabilities over Total Assets</b>	<b><u>(3,805,171)</u></b>	<b><u>(3,648,835)</u></b>
<b>Accumulated Fund</b>		
Consolidated Fund at year end	(95,106)	(80,123)
Net Public Debt/Public Credit	<u>(3,710,065)</u>	<u>(3,568,711)</u>
	<b><u>(3,805,171)</u></b>	<b><u>(3,648,835)</u></b>

Figures in Statement may not add up due to rounding up.

(Source: FR 2013, page 213)

## Public Debt

### Debt Composition

In general, Government's borrowing programme includes MGS, Treasury Bills and Foreign Loans. 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 future Government's borrowing.

Debt Composition as at 31 December 2013 stood as follows (*Tables 15 and 16* refer):

**Table 15: Debt Composition**

Domestic Debt	External Debt
%	%
98.98	1.02

(Source: FR 2013, pages 195-197 – see *Table 16* below for percentage calculations)

**Table 16: Domestic and External Debt Composition**

Type of Debt	Amount	Percentage of Total Debt
	€	%
Malta Government Stocks	4,610,859,277	91.83
Other Local Loans	56,378,732	1.12
Treasury Bills	247,407,166	4.93
Euro Coins	55,279,000	1.10
Foreign Loans	50,963,565	1.02
<b>Total Debt</b>	<b>5,020,887,740</b>	

(Source: FR 2013, pages 195-197)

### Public Debt Percentages

*Table 17* portrays debt as a percentage of GBP.

**Table 17: Debt as a Percentage of Gross Domestic Product**

Public Debt as at 31 December 2013	Gross Domestic Product 2013	Ratio Public Debt to Gross Domestic Product
€	€	%
5,020,887,740 <sup>6</sup>	7,262,645,000 <sup>7</sup>	69.13

<sup>6</sup> Source: FR 2013, page 197

<sup>7</sup> Source: Gross Domestic Product Q2/2014 – National Statistics Office News Release No. 159/2014



### **Local Loans**

On 31 December 2013, the local Public Debt as reported in Appendix F of FR amounted to €4,969,924,175, representing an increase of €358,583,937 over the corresponding reported figure for 2012. The closing Public Debt balance is inclusive of Treasury Bills outstanding at year-end, Euro Coins and Other Local Loans with a local commercial bank, amounting to €247,407,166, €55,279,000 and €56,378,732 respectively.

This increase works out as follows:

	€
Total New Loans	1,748,955,481
Currency Issue	5,181,000
Total Repayments	<u>(1,395,552,544)</u>
<b>Net Increase in Public Debt</b>	<b><u>358,583,937</u></b>

### **Foreign Loans**

As reported in last year's AAR, 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 the economic development of the country.

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 existing foreign loans due, which as at end 2013 stood at €50,963,565, is provided in *Table 18*:

**Table 18: Foreign Loans Analysis**

Foreign Loan	Financing Purpose	Year of Issue	Amount Disbursed	Interest Rate	Date of Maturity	Balance due as at 31 December 2013
				%		€
Council of Europe Fund for Development 2003	Mater Dei Hospital	2003	€75.5 million	4.65	07/05/2018	37,750,000
Council of Europe Fund for Development 2002	Mater Dei Hospital	2002	€25.5 million	5.06	11/12/2017	10,200,000
European Union Loan C	Solid Waste Composting Project	1987	€3 million	1.00	15/09/2027	1,512,300
European Union Loan B	Improvements in the Grand Harbour	1979	€5 million	1.00	15/11/2018	941,500
U.S.A. Government	Tug boat, cranes and spare parts related to projects	1973	\$5 million	3.00	13/11/2015	350,777
Government of Canada	Telephone cables and equipment	1974	CAD 1 million	-	31/05/2024	178,924
Republic of Italy 1991	Supply of Italian goods and services related to projects approved by the Italian and Maltese Governments	1993	ITL 50 billion	2.50	09/12/2014	30,063
<b>Total</b>						<b>50,963,565</b>

Figures in Statement may not add up due to rounding up.  
(Source: DMD)

### **Debt Management**

During June and July 2014, NAO was invited to attend two meetings, organised by Treasury and the Debt Management Advisory Division of the Commonwealth Secretariat, on a new legal framework that will govern the issue of new debt and Debt Management.

The Advisors from the Commonwealth Secretariat expressed the need for an annual external audit on Public Debt. The five main issues of Debt Management that need to be audited, as part of International Best Practices, were outlined as follows:

- a. Policy
- b. Operations

- c. Risk Control Procedures
- d. Information Technology (IT) Systems
- e. Financial Aspect

NAO remarked that this Office reviewed these aspects with the exception of IT Systems requirements,<sup>8</sup> during last year's Analysis of the 2012 FR, and that for this year's Analysis a more detailed review of Public Debt Management was carried out. In fact, as part of this year's analysis of Public Debt, NAO deemed it appropriate to forward to DMD a number of queries, based on the latest Revised Guidelines for Public Debt Management dated 1 April 2014, as prepared by the World Bank and the International Monetary Fund. In this regard, DMD provided a detailed description of the main elements comprising the 2013 Debt Management, as outlined below.

### *Malta Government Stocks – Strategy and Implementation*

Government's 2013 borrowing strategy was broadly on the same lines to 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.

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 lessen the impact from the volatility and uncertainty prevailing in the international capital markets. Following consultations held with institutional investors, Treasury targeted not only the demand coming from credit institutions, but also retail and insurance investors in search of attractive yields in today's low interest rate environment. The Treasury's overall objective is to meet demand, and at the same time provide the right balance between new issuances and existing ones.

The strong demand from the retail investors in 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 2013, including the level of overall participation by domestic investors.

**Table 19: 2013 Malta Government Stocks Issuance Performance**

Date	On offer (plus over-allotment)	Total participation
	€'million	€'million
February	120 + 80	293.0
May	100 + 70	282.5
September (floating-rate) <sup>9</sup>	50 + 30	107.8
November	120 + 60	229.5
<b>Totals</b>	<b>390 + 240</b>	<b>912.8</b>

(Source: DMD)

<sup>8</sup> Further details are provided under 'Information Technology Systems in place' and relevant 'Concluding Remarks' in this Analysis.

<sup>9</sup> The two issues in September were of Floating-Rate Stocks linked to the six-month Euribor, *i.e.* the Euro Interbank Offered Rate is based on the average interest rates at which a large panel of European Banks borrow funds from one another.

### *Treasury Bills – Strategy and Implementation*

Over the past few years, DMD's policy has been to change the composition of debt away from short-term instruments in the form of Treasury Bills and in favour of more medium-to-long term MGS. However, this trend has not materialised to the full in 2013, as for the first time in recent years, the closing balance of outstanding Treasury Bills registered an increase of €94 million over the opening balance of the same year, reaching €247 million.

NAO noted that most of this increase is reflected in a larger bank balance held in the Government's account held at CBM. It is interesting to note that the increase over the previous year's Public Account balance as against the bank account's 2013 closing balance was of 91.8%. It is also to be noted that MGS issuance was lower than originally planned.

### *Operational Planning*

Gantt Charts and Timetables are issued prior to every new issuance of MGS to minimise operational risks. These would include a series of actions that would need to be taken at different points in time, in preparation for, and during a MGS issue.

An event calendar is 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.

### *Risk Control Plan and Procedures*

The main risks faced by DMD relate to market risk, amongst which interest rate and exchange rate risks, refinancing risk, liquidity risk and credit risk. The risk exposures of a public debt portfolio are determined by the composition of the debt 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 market risk mainly lies in that all MGS and Treasury Bills are being issued on the local market, and thus any change in market conditions can affect the demand for Government paper.<sup>10</sup>

A decrease in demand would require DMD to increase the coupon<sup>11</sup> offered to make Government paper more attractive. To mitigate this risk, DMD, as earlier described in this Analysis, is currently working with the Debt Management Advisory Unit of the Commonwealth Secretariat on a new legislation that will govern the issue of new debt and Debt Management. If approved, the new Act will bring about a mechanism whereby Government can resort to the international markets to raise funds 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. In this regard, DMD basis the coupon of stocks to be issued in the primary market on the yields in the secondary market. The final decision on the coupon is taken by the Public Debt Management

<sup>10</sup> 'Government Paper' refers to debt securities that are issued or guaranteed by a sovereign Government.

<sup>11</sup> A 'coupon' represents the interest rate stated on a bond when it is issued.

Advisory Committee (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 August 2014, such ratio stood at 4.5%. 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 shall continue monitoring 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 €529,701, out of a total debt of €5,020,887,740 as at year-end 2013, representing only 1% of the latter, and therefore such risk is not material.

#### 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. DMD has an internal policy that the outstanding balance of MGS shall not exceed €450 million. Consequently, from time to time, DMD reviews MGS portfolio and when the outstanding balance in a particular year lies in the region of €450 million, it recommends to PDMAC to evaluate the conduct of a bond switch transaction.

This auction is earmarked only for financial institutions holding a particular stock, which normally matures within a year, to exchange it with a stock of longer maturity. The aim of this type of issuance is to lengthen and smoothen the interest and redemption profile of the existing MGS debt portfolio, and to provide an opportunity for institutional investors to diversify the maturity of their bond portfolios. More details about a Bond Switch Operation conducted in December 2013 was earlier reported under the 'Revenue Section' in this Analysis.

The Directorate stated that it shall continue to evaluate MGS portfolio on a yearly basis, to identify whether bond switch programs should be launched when the redemption amount in a particular year is high.

#### 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 and serve to smooth the latter over a longer period of time. At the same time, it allows Treasury to manage better the refinancing risk of Treasury Bills, which is further analysed in the context of average market participation. In this regard, when planning the monthly Treasury Bills' calendar, DMD officials take into consideration various factors, such as the redemptions due in a particular week and the target balance of

Treasury Bills at the end of the year.

This system is fundamental for DMD to project all funding needs and to meet other expenditure whether expected or not. DMD plans to improve this system by including other sources of revenue and expenditure, if made available, in order to get a better picture of all funding requirements.

#### 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. Since Treasury does not have any interest rate swap agreements or any other financial contracts directly related to the risk management of its debt portfolio, such risks pertinent to counterparties do not arise. Moreover, DMD stated that the risk management associated with Investments held by Government does not fall within its remit.

#### g. Settlement Risk

Settlement risk relates to the possibility that a counterparty does 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 in the case where investors who were successful at the auction and allotted Treasury Bills or MGS, fail to pay the amounts due, DMD 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.

#### *Assessment of Risks*

To assess risk, debt managers should regularly conduct stress tests of the debt portfolio on the basis of the economic and financial shocks to which the Government is potentially exposed. In this regard, DMD explained that it does not hold any of such tests. However, the Directorate stated that the Economic Policy Department performs Debt Sustainability Analysis during the year, presenting alternative debt paths,<sup>12</sup> based on alternative GDP forecasts, interest rates and primary balance,<sup>13</sup> and a scenario with a call of contingent liabilities of 2% of GDP.

#### *Monitoring of Government Debt and the Debt Portfolio*

The monitoring of the Government Debt and 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 where 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 to issue fixed-rate MGS rather than floating-rate euro-denominated securities. DMD also monitors investors' behaviour, both in the primary and secondary markets, to issue MGS in accordance to demand.

#### *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.

<sup>12</sup> Technically referred to as 'Trajectories'.

<sup>13</sup> 'Primary balance' represents Government's net borrowing or net lending, excluding interest payments, on consolidated Government's liabilities.

With regards to monetary authorities, DMD communicates regularly with CBM. Preceding every issue, CBM officers are informed with the current funding requirements and maturity profiles of the Government debt portfolio. CBM also assists DMD in the pricing of the new issuance of MGS. In addition, DMD is invited by CBM to attend and participate in the Financial Markets Committee meetings, which gathers all credit institutions operating in Malta. DMD explains its strategies to the banking community, gives presentations on issued debt, besides communicating other planned initiatives of DMD.

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. The expected securities to be issued 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 and Treasury Bills' take-ups. Moreover, DMD updates the Budget Office 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. The Budget Office 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.

### *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, this Office was informed by DMD that the latter does not yet have such a code in place. However, 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. The price is fixed following discussions with CBM, and after analysing the information that the latter forwards on a daily basis, in respect of the expected price of the stock with that particular coupon. Moreover, the pricing mechanism of CBM is based on prices in the secondary market that would reflect secondary market conditions.

### *Information Technology Systems in place*

DMD keeps all data in respect of MGS issuance, Treasury Bills, and interest payable, on spreadsheets, which were specifically compiled to accommodate DMD requirements. Furthermore, DMD has online access (viewing facility) to MGS Register maintained by MSE and to the Public Account held at CBM.

### *Business Recovery Procedures*

A back up of all data and information held on the aforementioned spreadsheets is kept by the Malta Information Technology Agency (MITA) in accordance with Government policy. 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 MSE. In addition, DMD holds a hardcopy of all the applications received in respect of all stocks issued, even after a particular security matures.

### *Internal Audit Function*

DMD stated that even though it does not have an Internal Auditor, there are a number of functions inbuilt 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. Furthermore, as with all Departments, DMD is subject to any internal audits that the Internal Audit and Investigations Department may wish to undertake.

### *Financial Aspect*

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

**Table 20: Government Debt Interest Expense**

Description	2013	2012	Variance
	€	€	€
Local Loans:			
Treasury Bills	2,576,605	3,547,107	(970,502)
Malta Government Stock	220,278,947	216,658,845	3,620,102
Ex-Malta Drydocks/Malta Shipbuilding Co. Ltd Loan	2,246,458	2,252,612	(6,154)
<b>Sub-Totals (Local)</b>	<b>225,102,010</b>	<b>222,458,564</b>	<b>2,643,446</b>
Foreign Loans	2,802,836	3,349,045	(546,209)
<b>Totals</b>	<b>227,904,846</b>	<b>225,807,609</b>	<b>2,097,237</b>

(Source: FR 2013, pages 148-151)

During year 2013, the overall servicing cost of Government's debt totalled €227.9 million, resulting in an increase of €2.1 million over the previous year. The low interest rate environment, prevailing particularly in the money markets during 2013, contributed towards a reduction of nearly €1 million in short-term local debt servicing cost (Treasury Bills) when compared with 2012.

On the other hand, the cost on local long-term debt increased by €3.6 million over that of the previous year, partly reflecting Government's issuance policy, which was predisposed towards borrowing through long-term bonds to extend the Weighted Average Maturity profile of Central Government debt, as well as ending up with higher outstanding levels of MGS at the end of 2013.

Finally, the servicing cost of foreign loans marked a decrease of €0.5 million over 2012, as a result of the decrease in foreign loans balances as at end-of-year 2013, including the maturity of one of the loans (European Union Loan F) on 30 April 2013.

### *Contingent Liabilities*

As recommended by the Debt Management Advisors of the Commonwealth Secretariat, risk assessment needs to be carried out by DMD prior to a Guarantee being issued to an entity. Moreover, where contingent liabilities exist, information on their cost and risk aspects should be disclosed in the Public Accounts.

Currently, Government Guarantees are not managed by DMD, but reside within the Ministry for Finance.



## *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 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 the 12-month financial year. 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.

DMD has also developed a spreadsheet model which forecasts Government's financing needs for the three months ahead. Such forecasts are derived using a hybrid approach, by basing forecasts on previous years' trend of actual revenue and expenditure. 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 co-ordination 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.

## ***Concluding Remarks***

### *Code-of-conduct*

Treasury is to implement a code-of-conduct and conflict-of-interest rules for debt management officers. This requirement, as recommended by the Revised Guidelines for Public Debt Management, will assist DMD in relieving concerns that staff's personal financial interests may undermine sound debt management practices.

### *Risk Management Framework*

NAO recommends that an implicit risk management framework is 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.

### *Contingent Liabilities*

This Office is of the opinion that there should be a link between Treasury and MFIN with regards to Government Guarantees. DMD should be properly equipped to be able to assess the risks associated with a particular guarantee before it is actually granted.

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.

### *Information Technology Systems*

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 ensure 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.

### *Accountability and Assurance*

Treasury ought to consider introducing regular internal audits of debt management activities, systems and control procedures.

### ***Correction of the Excessive Deficit***

(Source: Malta: Update of Stability Programme 2014 – 2017)

In 2012, Malta recorded a general Government deficit of 3.3% of GDP, above the reference value of 3%. Accordingly, on 6 June 2013, EU Council decided that an excessive deficit situation existed in Malta. The Council established a deadline, being 1 October 2013, for Malta to take effective action and to report in detail the consolidation strategy that is envisaged to achieve the targets. In particular, the Council recommended that Malta should reach a deficit target of 3.4% of GDP in 2013 and 2.7% of GDP in 2014.

In this regard, Government took effective action to bring down the deficit below the 3% threshold by the end of 2013, a year prior to the deadline set by the European Commission, but in line with the Stability

Program's projections of the previous year. In fact, the Deficit-to-GDP ratio for 2013 improved by 0.5 percentage points to 2.8% of GDP.

As a result, on 15 November 2013, the Commission communicated to the Council that it considered that Malta had taken effective action and that no further steps in the excessive deficit procedure were required.

Furthermore, in 2013, Government achieved an annual structural improvement of 0.7% of GDP, consistent with the requirements of the corrective arm of the Stability and Growth Pact and the Council Recommendation to correct the excessive deficit. Indeed, Malta managed to reach the stipulated deficit targets in the absence of similar extraordinary receipts in 2013, and in spite of a one-off equity injection of €40 million to Air Malta p.l.c.

Other challenges are foreseen in order to ensure long-term public finance sustainability. In fact, the ultimate target of Government's Stability Programme is to further consolidate public finances to reach a balanced structural budget balance.

### *Fiscal Outlook and the Medium-Term Fiscal Strategy*

(Source: Malta: Update of Stability Programme 2014 – 2017)

By the end of 2014, Government is aiming to reach a deficit target of 2.1% of GDP and achieve a structural effort of slightly more than 0.5 percentage points of GDP. The Debt-to-GDP ratio is expected to decline to 69.5% in 2014, partly due to the strength of economic growth, and also in view of the expected payment of arrears by Enemalta, as earlier explained under the 'Revenue Section' in this write-up.

Over the medium-term, Government is aiming to reduce the structural budget deficit by an average of 0.6 percentage points of GDP *per annum*, and by the end of the Programme period it is targeting a structural deficit of 0.5% of GDP. Thus, as stated in the 'Update of Stability Programme 2014 - 2017' by the end of the Programme period, Malta would have almost reached the minimum Medium-Term Budgetary Objective stipulated for a Euro Area country, which is signatory to the Treaty on Stability, Coordination and Governance. Public debt is expected to embark on a downward trend and is projected to go below 64% of GDP by 2017, thus converging to the 60% threshold at a satisfactory pace.

Furthermore, the decline in general Government Deficit-to-GDP ratio is expected to be sustained such that the fiscal imbalance is projected to be reduced further from 2.8% in 2013 to 0.3% by year 2017.

### *Fiscal Responsibility Act*

Government has recently 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 Fiscal Responsibility Act establishes the Medium-Term Budgetary Objective as defined in Council Regulation (EC) No. 1466/97, Article 2.

In summary, the Fiscal Responsibility Act 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 Fiscal Advisory Council to perform the functions conferred or imposed on it by the Fiscal Responsibility Act. 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.

## **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.

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.

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.

Furthermore, the Ministry has a Manual of Procedures, which, according to the Ministry was used for the year under review for the issue, extension, cancellation and compilation of data on Letters of Guarantee/

Comfort. NAO however did not carry out detailed tests to ascertain that this Manual is being fully adhered to.

The position of Contingent Liabilities as at 31 December 2013, as reported upon in Part I of FR 2013 and comparative figures for 2012 are reproduced in *Table 21*, a breakdown of which can be found in *Table 22*.

**Table 21: Contingent Liabilities**

	<b>2013</b>	<b>2012</b>
	€	€
Government Guarantees:		
Local	591,631,859	570,353,969
Foreign	<u>586,393,032</u>	<u>591,804,504</u>
	1,178,024,891	1,162,158,473
Letters of Comfort	<u>79,904,546</u>	<u>80,516,598</u>
<b>Totals</b>	<b>1,257,929,437</b>	<b>1,242,675,071</b>

**Table 22: Actual Guarantees made by Government**

<b>Beneficiary</b>	<b>31 Dec 2013</b>	<b>31 Dec 2012</b>	<b>Remarks</b>
	€	€	
Enemalta Corporation	75,000,000	75,000,000	This loan was taken up by Enemalta Corporation to repay all its existing Government secured facilities with local banks and foreign financial institutions.
	21,250,000	26,250,000	This Guarantee secures loan taken on 13 December 2007 to finance part of its capital expenditure programme for the period 2007 to 2013.
	9,538,514	10,000,000	A Letter of Guarantee was issued for an amount of €10 million on 5 January 2009, to secure overdraft facility.
	20,000,000	20,000,000	A Letter of Guarantee was issued for this amount, on 27 November 2008, to secure temporary short-term overdraft facility.
	16,000,000	16,000,000	A Letter of Guarantee was issued on 9 July 2009, for this amount to cover General Banking Facility, which will cover the issuance of a stand-by Letter of Credit.
	22,754,238	24,475,725	This Letter of Guarantee, originally issued on 9 July 2009 and amounting to €27 million, was issued to cover loan facility.
	150,000,000	150,000,000	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.
	50,000,000	50,000,000	A Letter of Guarantee was issued for this amount, on 9 December 2010, to secure loan facility in connection with the construction of interconnector between Malta and Sicily.
	24,305,556	-	This Letter of Guarantee, originally issued on 14 December 2010 and amounting to €50 million, was issued to secure loan facility in connection with the construction of interconnector between Malta and Sicily.
	100,000,000	100,000,000	This Guarantee secures loan for €100 million, taken on 20 December 2010, to part-finance the construction of the interconnector between Malta and Italy.
	<b>488,848,308</b>	<b>471,725,725</b>	

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

<b>Beneficiary</b>	<b>31 Dec 2013</b>	<b>31 Dec 2012</b>	<b>Remarks</b>
	<b>€</b>	<b>€</b>	
Malta Enterprise Corporation (ex Malta Development Corporation)	1,444,467	1,698,912	The Letters of Comfort issued to cover the Loan Guarantee Scheme taken over from IPSE 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.
	1,454,517	883,146	Letter of Guarantee issued on 6 July 2001 to secure loan/credit facilities made available to the Corporation. The limit of this Guarantee was reduced from €4,658,747 to €2,500,000 in 2012.
	2,112,571	908,834	A Letter of Guarantee issued on 21 October 1991 for the amount of €5,823,433 was reduced to €2,500,000 in 2012. The remaining Letter of Guarantee of €3,494,060 issued on 21 October 1993 was cancelled during the year.
	<b>5,011,555</b>	<b>3,490,892</b>	
Water Services Corporation	62,194,946	62,598,088	Three Letters of Guarantee issued on 30 April 2007 in connection with Loan 1 and Loan 2 Facility, and to secure general banking facility. Another Letter of Guarantee was issued on 1 October 2008, originally for €37,269,974, to cover general banking facility.
	39,388,194	39,799,666	On 30 November 2007, Water Services Corporation entered into a Guarantee agreement with a foreign bank for €40 million to undertake a project concerning investments in the sector of water supply and wastewater collection and treatment.
	<b>101,583,140</b>	<b>102,397,754</b>	
Malta Freeport Corporation Ltd	-	535,952	This overdraft facility taken over from Malta Freeport Terminals Ltd as a result of the privatisation process, which was converted into a loan facility repayable over a 10-year period. This was cancelled during the year.
	60,503	58,091	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 \$250 million). 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.
	<b>200,815,341</b>	<b>201,348,881</b>	

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

<b>Beneficiary</b>	<b>31 Dec 2013</b>	<b>31 Dec 2012</b>	<b>Remarks</b>
	€	€	
Malta Industrial Parks Ltd	14,723,849	16,318,497	On 3 December 2008, Letter of Guarantee was issued to secure loan facility in replacement of Letter of Comfort for €25,623,107 dated 28 April 2005. This Letter of Comfort was amended to €18 million in 2012.
	6,988,120	6,988,120	Letter of Comfort issued on 5 March 2007 in connection with the expropriation of Land at Ricasoli.
	20,451,478	22,689,402	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 million, and again superseded on 10 July 2012.
	3,321,656	4,203,554	Letter of Comfort dated 10 March 2011 for €6 million 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.
	10,941,698	11,443,639	A Letter of Guarantee, originally amounting to €13 million, was issued to secure loan facility. This was superseded by Letter of Guarantee dated 10 July 2012 for €11,650,000.
	1,997,496	2,890,794	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.
	25,000,000	25,000,000	Letter of Guarantee was issued for this amount, on 5 October 2012, to secure loan facility to finance the acquisition of property from Air Malta p.l.c.
	4,903,963	985,128	On 9 August 2012, Letter of Guarantee was issued to secure loan facility of €12 million.
	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.
	1,503,008	-	Letter of Guarantee issued on 3 January 2013 with a local bank to secure loan facility of €3 million.
	<b>90,426,268</b>	<b>91,114,134</b>	



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

<b>Beneficiary</b>	<b>31 Dec 2013</b>	<b>31 Dec 2012</b>	<b>Remarks</b>
	<b>€</b>	<b>€</b>	
Malta Government Technology and Investment	499,491	611,438	A Letter of Comfort was issued for €1 million 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	6,565,952	6,389,826	Two Letters of Guarantee were issued on 23 December 2005 to cover working capital and other financing requirements. The limit of one guarantee was reduced to €6,700,000 on 24 August 2012.
Foundation for Tomorrow's Schools	-	60,036,775	These two Letters of Guarantee were cancelled during 2013.
	66,216,520	-	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.
	<b>66,216,520</b>	<b>60,036,775</b>	
Property Management Services Ltd	5,012,644	6,000,000	This Letter of Guarantee, originally amounting to €9 million, was issued to secure loan facility. This was reduced to €6 million in 2012.
Authority for Transport in Malta	6,895,873	8,064,020	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.
	45,085,039	43,745,866	A Letter of Comfort was issued on 9 February 2011 for €56 million to secure loan facility, to finance its capital expenditure and to pay for the licences and buses from present bus owners.
	<b>51,980,912</b>	<b>51,809,886</b>	
Grand Harbour Regeneration Corporation	328,056	1,228,420	A Letter of Comfort issued on 31 October 2012, to secure overdraft facility and finance services/works associated with the City Gate project.
Housing Authority	320,341	-	A Letter of Guarantee was issued with a local bank for €4,658,747 to secure overdraft facilities.
Malta Air Traffic Services	436	104	A Letter of Guarantee was issued on 11 August 2011 for €14,631,000 to secure loan facility, to finance shortfall in liquidity and capital expenditure to upgrade the air traffic management system and surveillance capacity.
Gozo Ferries	1,256,683	1,360,000	Letter of Guarantee issued for €1,360,000 on 18 December 2012 to secure loan facility.

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

Beneficiary	31 Dec 2013	31 Dec 2012	Remarks
	€	€	
Public Broadcasting Services	3,730,197	1,661,236	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.
Vault Finance Ltd	235,333,594	243,500,000	Letter of Guarantee issued on 31 December 2012 to secure loan facility for €318,500,000 and replace existing Enemalta Guarantees.
<b>Totals</b>	<b><u>1,257,929,437</u></b>	<b><u>1,242,675,071</u></b>	

The above Letters of Comfort and Bank Guarantees may translate into dues up to €1,257,929,437 by Government, should the companies call upon the Government to make good for their debts.

### Creditors' Analysis

Fifty-six Ministries and Departments submitted to Treasury an 'Analysis of Creditors' as at 31 December 2013, in the required accruals' template. Total creditors reported in this analysis amounted to €198,213,704, as at year-end. The opening balance as at 1 January 2013 was made up of balances submitted by 49 Ministries and Departments, with an aggregate amount of €181,714,713.

At the end of the year, 12 Ministries and Departments reported a 'Nil' creditors balance in their Returns. Moreover, €347,005 of total creditors (equal to 0.18%) related to contested amounts. *Table 23* shows an ageing analysis of the remaining creditors' balances as at 31 December 2013:

**Table 23: Ageing of Remaining Creditors**

Days Overdue	2013		2012	
	Amount Due	Percentage	Amount Due	Percentage
	€	%	€	%
01 – 30	71,314,791	36.04	66,684,313	36.74
31 – 60	14,427,771	7.29	9,985,699	5.50
61 – 90	14,671,414	7.41	19,505,601	10.74
91 – 180	25,510,645	12.89	24,749,684	13.63
181 – 360	16,571,322	8.38	8,285,345	4.56
Over 360	55,370,757	27.99	52,326,773	28.83
<b>Totals</b>	<b>197,866,700</b>	<b>100</b>	<b>181,537,415</b>	<b>100</b>

Credit balances overdue by over 360 days related mainly to the Government Property Department, the Ministry for Education and Employment, and the Ministry for Sustainable Development, the Environment and Climate Change, with aggregate amounts of €45,079,502, €4,231,364, and €2,452,582, respectively.

## School Council Fund

The opening balance in the 2013 Statement of Revenue and Expenditure pertaining to the School Council Fund of the Ministry for Education and Employment, as reported in Part I of FR, stood at €900,639. This figure did not agree with the closing balance reported in the previous year of €1,695,029, with the difference totalling €794,390.

Consequently, Treasury requested a Report from the Ministry to explain such variance. The latter presented a detailed Report to Treasury on 3 June 2014, following an investigation about the substantial difference between the closing balance of the Fund for 2012 and the 2013 opening balance of same.

This Report concluded that the discrepancy was the result of a mathematical error in the computation of balances of the 2012 list, resulting in double counting of the opening balance figure for 2012 in the 'Total Revenue' column. To this effect, NAO recalculated the closing balance for the financial year 2012, which amounted to €786,180. However, this balance still differs from the 2013 opening balance figure reported in the 2013 FR, amounting to €900,639, by €114,459. Moreover, when taking into account those schools that failed to submit the relative bank information during 2012, but who submitted the details for 2013, the discrepancy is still material, in the range of €88,000.

As a result, NAO requested the Ministry for Education and Employment to provide a detailed explanation for this difference, and to confirm whether the Report included school balances as at 31 December 2013. This Office also required the Ministry to state whether each school reported figures as per their respective Cash Book, rather than as per bank statements. However, up to the writing of this Report, no reply was received in this respect.

## Management Comments

Both Treasury and the Budget Affairs Division agreed with the contents of this Analysis. Additional comments submitted are outlined below:

### *Excess of Expenditure over Estimates*

With regards to the additional amount of €19,200,000 provided for under MFIN Vote, in respect of European Union Own Resources, the Budget Affairs Division replied that by the end of the year, the payment for which the supplementary funds were provided, did in fact materialise. Hence, supplementary funds were resorted to, given that due provision was not made in the original approved estimates.

### *Central Bank of Malta Public Account*

Treasury stated that it is currently working on the July 2013 Bank Reconciliation Statement.

### *Public Debt*

#### Concluding Remarks

#### *Code-of-conduct*

A provision shall be made in the new legislation governing Government's borrowing and public debt management to introduce a code-of-conduct for officers employed in the management of public debt. To this effect, in the near future, DMD shall start working on the drafting and implementation of a code-of-conduct and conflict-of-interest rules for debt management officers.

### *Risk Management Framework*

The draft Government Borrowing and Public Debt Management Act (GPDMA) requires that for every financial year, the Minister shall prepare a medium-term debt management strategy. This 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 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.

### *Contingent Liabilities*

The draft GPDMA shall address the issue of contingent liabilities in a more holistic way in accordance with international best practice for debt management. Currently, the issuance, evaluation, monitoring and recording of Government guarantees are being carried out by MFIN.

### *Information Technology Systems*

Following the completion and enactment of the new Government borrowing and public debt management draft bill, Treasury shall start working on the implementation of the new information technology systems for debt management activities.

### *Accountability and Assurance*

DMD shall be introducing internal audit assignments in respect of debt management activities. However, in order to take the full benefits from such assignments, these should take place following the enactment of the new Act and the implementation of the above issues. Moreover, one needs to discuss such assignments with the Internal Audit and Investigations Department.





# Corporate Issues

# Arrears of Revenue 2013

## 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. 3/2014 also required officers to forward Returns, including 'Nil' Returns.

All Returns were to reach Treasury by not later than 4 April 2014. As per the foregoing Circular, officers 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"*.

For the year under review, Departments were additionally required to submit details of payments received during January 2014 relating to balances due as at 31 December 2013. This data allows for the calculation of amounts due as at 31 December 2013 still unpaid on 31 January 2014. Information submitted revealed that an amount of €9,749,359<sup>1</sup> was collected during January 2014, with a resulting unpaid balance of €404,946,945 pertaining to amounts due as at 31 December 2013.

## Returns

Details of Arrears of Revenue included in the Table on page 98 have been compiled only from Returns forwarded to the National Audit Office (NAO) by Treasury. The following Departments submitted 'Nil' Returns:

- Office of the President
- House of Representatives

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<sup>1</sup> This amount does not take into consideration any receipts by the Government Property Department on rent due from Government Departments, Entities and Local Councils.

- Office of the Prime Minister (OPM)
  - Public Service Commission
  - Electoral Office
- Ministry for European Affairs and Implementation of the Electoral Manifesto
- Ministry for Foreign Affairs
- Ministry for Social Dialogue, Consumer Affairs and Civil Liberties
  - Department of Corporate Services
  - Consumer Affairs
- Ministry for the Family and Social Solidarity
  - Department of Corporate Services
  - Department of Social Policy (DSP)
  - Social Welfare Standards
- Ministry for Home Affairs and National Security
  - Department of Corporate Services
  - Corradino Correctional Facility
  - Probation and Parole
  - Public Registry
  - Civil Registry
- Ministry for Finance
  - Treasury Department
  - Economic Policy
- Ministry for Energy and the Conservation of Water
  - Department of Corporate Services

In contrast with previous years, Part I of the 2013 Financial Report did not report any defaulters in compliance with the Circular in force.

## Notes and Comments on Arrears of Revenue

### Office of the Prime Minister

The net closing balance as at 31 December 2013, reported by OPM in its ARR, amounted to €7,027. This outstanding balance is due from six individuals, and is made up as follows:

- a. €983 is due from a debtor who breached his Contract of Undertaking in 2007;
- b. €2,091 is in respect of overpaid salaries to two employees;
- c. €2,238 is to be reimbursed from an employee after failing to resume her duties and work the stipulated uninterrupted period of six months, after availing herself of Maternity Leave; and
- d. the amount of €1,715 is to be refunded from two employees who failed to fulfil their obligations in connection with a sponsorship of a Masters Degree.

Except for the balance of €2,238, which fell due in 2010, all pending amounts are being gradually paid.



Ageing of debtors is classified as follows:

	€
Amounts outstanding for over five but less than ten years (2004 – 2008)	983
Amounts outstanding for over two but less than five years (2009 – 2011)	4,329
Amounts outstanding for over one but less than two years (2012)	900
Amounts outstanding for less than one year (2013)	<u>815</u>
<b>Net Closing Balance</b>	<b>7,027</b>

### *Department of Information*

The outstanding balance of arrears as at 31 December 2013, disclosed by the Department of Information, amounting to €77,902, is all due from Government Departments and Entities, out of which the amount of €56,046, *i.e.* 72%, is in respect of Government Gazette adverts.

	€
Amounts outstanding for less than one year (2013)	70,851
Amounts outstanding for over one but less than two years (2012)	4,520
Amounts outstanding for over two but less than five years (2009 – 2011)	281
Amounts outstanding for over five but less than ten years (2004 – 2008)	<u>2,250</u>
<b>Net Closing Balance</b>	<b>77,902</b>

By the end of January 2014, a total of €26,450 had already been recouped.

### *Government Printing Press*

The net closing balance as at 31 December 2013, as provided by the Government Printing Press consists of:

	€
a. Revenue	315,634
b. Revolving	<u>346,725</u>
<b>Net Closing Balance</b>	<b>662,359</b>

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 (2013)	258,490
Amounts outstanding for over one but less than two years (2012)	69,002
Amounts outstanding for over two but less than five years (2009 – 2011)	252,957
Amounts outstanding for over five but less than ten years (2004 – 2008)	<u>81,910</u>
<b>Net Closing Balance</b>	<b>662,359</b>

### *Government Property Department*

The gross closing balance as at 31 December 2013 reported in ARR of the Government Property Department (GPD), amounted to €32,685,650, an increase of 16% over the same figure for 2012, which stood at €28,253,080.

An amount of €9,458,542 was not collectable as at year-end, bringing the net collectable arrears figure down to €23,227,108. The estimated amount considered uncollectable pertains to rent payable to GPD on property held by Government Departments, Parastatal Entities and Local Councils.

In 2012, Treasury Department directed GPD to only report the sum of €2,000,000 as net collectable in relation to these properties, leaving the remaining balance of €9,458,542 as not collectable. These amounts were again reported in the 2013 ARR, even though relevant supporting documentation shows a gross balance of €14,191,900.

GPD confirmed that the exercise that started during 2013 to ascertain the correct amounts due from the various Government Departments, Entities and Local Councils, is still underway. Through this exercise, the relevant arrears, which at the end of 2013 were reported at about €14 million, were adjusted to just over €5 million by the time of writing this report. The Department explained that this amount may increase or decrease depending on the adjustments required on each of the remaining accounts.

### Difference between the Arrears of Revenue Return and the Debtors' Template

A difference of €2,000,000 was also noted between ARR and the Debtors' Template provided by GPD. The Department confirmed that no amounts in relation to arrears from Government property were included in the Debtors' Template, therefore such difference relates to the amount reported with respect to these dues in ARR.

### Revisions

A total of €3,841,162 was reported as revisions in the 2013 ARR. This amount was meant to adjust the opening 2013 balance, since up to October 2013, GPD was still using the old version of the Land and Estate Management Information System software, which recognised invoices on the commencement date of the related rent period rather than on the date when said invoices were issued. Consequently, the discrepancies that arose whenever transactions that related to 2012 were posted in 2013, had to be adjusted in the 2013 ARR.

### Write-offs

GPD also reported write-offs of €17,116 in its ARR. Of these, an amount of €7,754 was written off in relation to a lease agreement for a property in Valletta. The write-off approval in this regard was granted by the then Commissioner of Lands. Further inquiry revealed that this property was first leased for a period of 15 years on 2 October 2008, but then experienced various structural damages, which rendered it unusable. In fact, Government pursued legal action in its regard. In light of this, GPD decided to waive off the amount of €7,754 for the period from 2 April 2009 to 31 May 2011 since the property had not been in use during that time. A new lease agreement, effective from 1 June 2011, was subsequently signed.

### Below-the-line Account – Malta Tourism Authority Fees

Reported arrears pertaining to fees due to the Malta Tourism Authority (MTA), featured for the first time in the 2013 GPD ARR. According to explanations provided by the Department, these fees emanate from a condition in the Deed of Concession pertaining to the Vittoriosa Waterfront, where the lessee must pay along with the rent payment, an annual fee to MTA amounting to 10% of the original ground rent. This fee is collected by GPD and passed on to MTA.

### Collection Efforts

In an effort to collect the outstanding dues, the Revenue Section within GPD is resorting to the issue of periodic reminders, as well as to placing phone calls to defaulters. The Department is also sending Enforcement Officers to deliver claims to defaulters, as well as issuing a number of Judicial Letters, and attempting to draw up Repayment Agreements.

Furthermore, as from 2014, different officers have been assigned the duties of monitoring a specific revenue code. This allows each officer to fully concentrate on chasing defaulters of that particular category.

### Ageing Analysis

The net collectable arrears can be analysed as follows:

	€
Amounts outstanding for less than one year (2013)	6,623,623
Amounts outstanding for over one but less than five years (2009 – 2012)	8,329,699
Amounts outstanding for over five years (– 2008)	<u>6,386,091</u>
	21,339,413
Less unallocated credit	<u>(112,305)</u>
<b>Total</b>	<b>21,227,108</b>

This analysis excludes the balance of €2,000,000, pertaining to the unsupported net collectable arrears due from Government Departments, Entities and Local Councils.

Additionally, the amount of €112,305, 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 rent due before the invoice is issued. GPD is currently carrying out an exercise to reconcile these credits to their relative invoices. The exercise is currently targeting Joint Office’s properties, and will focus on other revenue heads once it is completed.

## Ministry for Tourism

### Breakdown of Gross/Net Closing Balance

The gross closing balance of €1,679,678 as reported in the Ministry for Tourism ARR for the year ending 31 December 2013 is made up of the following:

	€
a. Dues to MTA	1,625,313
b. Dues to ex-White Rocks Complex	<u>54,365</u>
<b>Gross Closing Balance</b>	<b>1,679,678</b>

From the gross receivables at year-end, the amount due to ex-White Rocks Complex, which has been pending before 1995, is estimated as not collectable and is in the process of being written off. The net closing balance due to MTA relates to unpaid licences and can be analysed as follows:

	€
Amounts outstanding for less than one year (2013)	605,042
Amounts outstanding for over one but less than two years (2012)	314,823
Amounts outstanding for over two but less than three years (2011)	213,480
Amounts outstanding for over four years (– 2010)	<u>491,968</u>
<b>Net Closing Balance</b>	<b>1,625,313</b>

Although the reporting function generates an ageing analysis, the oldest group for MTA is shown as ‘2010 and prior’. As a result, NAO could not establish the exact period for which these amounts have been outstanding.

## Revisions

Revisions of the previous year's closing balance, totalling €32,169, related to credit notes raised for invoices issued in 2012 in respect of establishments which stopped operating, or had their licences suspended. However, this figure could not be verified by NAO, as a breakdown of the amount could not be generated.

## Write-offs

Last year, NAO reported that amounts due from four Local Councils for Beach Cleaning Services were considered as not collectable, given that the relative claims to the value of €181,735 had been outstanding for over 16 years. Although these debtors are shown as written-off during the year, proper write-off approval, if any, from the Ministry of Finance, the Economy and Investment, in line with Article 80 of the General Financial Regulations 1966, was not made available to NAO.

## Other Weaknesses

The following shortcomings also emerged from a systems review of debtors and debt collection:

- a. The reporting function of MTA's system administering licences has a number of limitations, and thus, is not considered adequate by the Ministry itself. In this respect, a new comprehensive system was in the process of being procured.
- b. The aged debtors list contains multiple negative balances which, according to Management, are created where a particular establishment has more than one licence. However, due to the reporting limitations of the system, satisfactory audit testing could not be performed to verify the accuracy of debtors' balances.
- c. The position of a Credit Controller has been vacant for a number of years. According to Management, a call for applications was planned to be issued by the end of 2014.
- d. No evidence was presented to NAO confirming that reminders for amounts due are regularly sent. Moreover, the invoices sent by MTA to claim payment comprise only the amount due with respect to that particular year, without referring to amounts still pending from previous periods. This poses the risk that ARR comprises amounts which are prescribed.

## *Institute of Tourism Studies*

### Amounts Collected

From the gross closing balance of €361,503 as reported by the Institute of Tourism Studies in ARR for the previous year, the Employment and Training Corporation was the main debtor, with an outstanding balance of €181,935. NAO was informed that the Institute provided courses on behalf of the Corporation, which sessions were eventually stopped as the latter was not issuing the related payments. Management stated that amounts due were being recouped gradually, following an agreement reached between the two entities.

## Revisions

The closing balance as reported in the previous year was revised downward to correct misstated invoices.

## Amounts Estimated as Not Collectable

The amount of €17,000, estimated as not collectable in the original 2013 ARR, did not reconcile with the supporting breakdown. The Return was subsequently revised to portray the correct figure of €12,921.

This revised amount relates to stipends due by nine students who resigned from their studies between 1995 and 2007. These amounts, which were already considered as not collectable in the previous year, are intended to be written off.

## Ministry for Education and Employment

The gross closing balance of €636,481 as reported by the Ministry for Education and Employment is made up of the following:

		€
a.	Director Corporate Services	
	<i>Breach of Contract</i>	125,325
	<i>Overpayment in Salaries</i>	157,918
	<i>Running of Tuck-shops</i>	7,851
b.	Ministry - Administration	<i>Allowance Overpayment</i> 233
c.	Examinations Department	<i>External Examinations</i> 3,353
d.	Breach of Contract	4,120
e.	Maintenance Grants Section	
	• Malta College of Arts, Science and Technology	69,234
	• Junior College	<i>Stipends Overpayment</i> 11,050
	• University	177,656
f.	Travel Expenses' Refund	62,693
g.	STEPS	<u>17,048</u>
	<b>Total</b>	<b>636,481</b>

The opening balance of €867,632 brought forward from last year was revised upwards by an aggregate amount of €53,293, due to various omissions in the Return of the previous year. The arrears relating to the Institute of Tourism Studies, which were previously included within this Return, are now included within

the Return submitted by the Ministry for Tourism.

There were no amounts written off during 2013. However, an amount of €56,389, including €48,081 relating to Breach of Contracts with the Directorate for Educational Services, were considered as not collectable.

### Limitations of Scope

Despite a number of requests for documentation required for audit purposes, no response was received by NAO from the Directorate of Finance within the Department for Education and Employment. Various reminders were also sent, but still to no avail. As a result, no verification could be performed on the arrears of revenue reported by the Ministry as at end December 2013.

## 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 €1,560,008. Of this, an amount of €26,391 was reported as not collectable, leaving a net balance of €1,533,617, which latter amount was split under the following categories:

	€
a. Veterinary Services	204,467
b. Paying Agency	11,105
c. Sundry Revenue	1,120
d. Salaries	26,822
e. Fisheries	716,738
f. Plant Quarantine	1,948
g. Other Revenue	16,300
h. Aquaculture	<u>555,117</u>
<b>Total</b>	<b>1,533,617</b>

No testing in relation to the figures reported in ARR, could be conducted by this Office, since the requested information from this Ministry was not made available, in spite of numerous reminders.

## Ministry for Transport and Infrastructure

The Return submitted by the Ministry for Transport and Infrastructure (MTI) for 2013, incorporates the following revenue categories and the net closing balance of €556,161 comprises dues:

	€
a. from Local Councils issued by the Central Districts Department	87,732
b. from Local Councils issued by the Cleansing Services Department	193,171
c. to Manufacturing Services Department	201,610
d. from Breach of Contracts, Damages, Maintenance and others	54,337
e. to Salaries Section	<u>19,311</u>
<b>Total</b>	<b>556,161</b>

Ageing of net collectable arrears at the end of the year, can be analysed as follows:

	€
Amounts outstanding for less than one year (2013)	246,262
Amounts outstanding for over one but less than two years (2012)	107,598
Amounts outstanding for over two but less than five years (2009 – 2011)	44,198
Amounts outstanding for over five but less than ten years (2004 – 2008)	76,725
Amounts outstanding for over ten years ( – 2003)	<u>81,378</u>
<b>Net Closing Balance</b>	<b>556,161</b>

The gross arrears balance of €658,050, as at 31 December 2012, as shown in MTI's ARR for 2013, differs from that in the 2012 Return prepared by the former Ministry for Resources and Rural Affairs (MRRA), which stood at €1,784,837. In fact, following the split of MRRA upon change in administration, some dues were transferred to the Ministry for Sustainable Development, the Environment and Climate Change, whilst others remained within the remit of MTI.

### Past Arrears Collected

Past arrears collected during 2013 amounted to €100,245. Of this amount, €69,944 (70%) related to the collection of 'Dues from Local Councils issued by The Cleansing Services Department' in respect of years 2011 and 2012.

### Newly Accrued Arrears

Out of the total newly accrued arrears of €246,262, €158,522 (64%) related to 'Dues to Manufacturing Services Department'. Out of the latter amount, €100,010 was due by a particular co-operative society in respect of wages for the period from January to June 2013. In 2014, €88,732 was set off with dues by MTI to the same society, whilst the remaining €11,278 was duly settled in the same year. The balance of €58,512, which was not related to the said co-operative society, consisted of newly accrued claims.

An amount of €70,330 was also accrued for during 2013 in relation to 'Dues from Local Councils issued by The Cleansing Services Department'.

### Write-offs

Out of total write-offs of €190,236 during 2013, an amount of €187,273 (98%) related to 'Dues from Deposit of Waste and Rubble – Cleansing Services Department'. This amount, which was due from a particular co-operative society in the process of liquidation, was included with amounts estimated as not collectable in the previous years' ARRs.

Although the then Ministry of Finance, the Economy and Investment had approved the write-off of this amount on 25 August 2008, no action had been taken in this regard. It transpired that the relative file was retained for a period of five years within the Financial Control Unit of the former MRRA. Consequently, this amount was only written off in 2013.

### Amounts Estimated as Not Collectable

#### *Dues for Deposit of Waste and Rubble – Cleansing Services Department*

Balances of outstanding dues totalling €20,165, were considered as not collectable. These consisted of instances where a payment agreement was in place between MTI and the individual debtors (€8,442), as well as amounts which were in the process of being written off (€10,107). In the remaining cases (€947),

legal action is being taken to recoup the debts, whilst effort will be made to write off another four amounts at a total of €669, since it is deemed impracticable to institute legal action.

#### *Dues to Manufacturing Services Department*

The amount of €14,938, which was considered as not collectable from this Department, is made up of several small amounts. The main reasons for the uncollectable nature of these dues included problems relating to the work delivered, lack of adequate documentation, legal proceedings, as well as refusals by the respective debtors to settle the amounts due.

#### *Dues from Breach of Contracts, Damages, Maintenance and Others*

Out of the total amount considered as not collectable of €22,438 under this category, a balance of €19,003 (85%), related to claims for which a set-off agreement was being discussed but which had never been finalised. Since then, such claims had become time-barred and therefore not collectable. Before considering the write-off of these amounts, the cases were referred to the debtor's Legal Advisor.

#### Collectable Arrears

#### *Dues from Local Councils – Central Districts Department*

Out of total net collectable arrears of €87,732, €81,378 (93%) related to dues from a particular Local Council, which have been outstanding as from the years 1996 to 1999. A court case was instituted by the Local Council, which claimed that the said amounts were not payable. However, in a judgement delivered on 17 June 2014, the Court ruled that these amounts were in fact due to MTI. The Ministry has yet to take action to recover this balance, together with legal fees and interests of €623 and €71,613 respectively.

#### Collection Efforts

The Ministry stated that when invoices become due, registered Notices are sent to debtors on a monthly basis. In order to avoid claims becoming time-barred, when dues are not settled within a period of six months, such cases are referred to the Ministry's Legal Office for initiation of appropriate legal action.

#### *Transport Malta*

#### Vehicle and Driving Licences

The gross/net closing balance of arrears amounting to €19,143,662, as reported in the 2013 ARR submitted by Transport Malta (TM) consists of dues in respect of motor vehicle road and driving licences, as follows:

	€
a. Vehicle Licences	18,715,523
b. Driving Licences	<u>428,139</u>
<b>Total</b>	<b>19,143,662</b>

As in the previous year, none of the outstanding dues were written off during 2013, however, an estimated amount of €977,574 pertaining to Vehicle Licences was considered as not due as at year-end, and therefore included under the revisions column in ARR. TM confirmed that such balance pertained to licence fees and administration fees that were not due, in view of the fact that licensees regularised their position through the Road Licence Regularisation Scheme, which was still ongoing during 2013.



An ageing analysis of the amounts due in relation to Vehicle Licences is as follows:

	€
Amounts outstanding for less than one year (2013)	941,208
Amounts outstanding for over one but less than two years (2012)	833,562
Amounts outstanding for over two but less than five years (2009 – 2011)	3,017,731
Amounts outstanding for over five years (– 2008)	<u>14,853,856</u>
<b>Total</b>	<b>19,646,357</b>

From the outstanding balance of €14,853,856, an amount of €10,398,509 related to previous years up till 2004. Upon enquiry, the Directorate could not provide a complete ageing of this amount.

Moreover, it is pertinent to note that the above analysis still includes the amount of €977,574 pertaining to Vehicle Licences that were considered no longer due. On the other hand, the balance of €19,646,357 excludes the amount of €46,740, which was received during the year under review in relation to fines and Controlled Vehicular Access fees.

To this effect, TM confirmed that the ageing report provided by the Malta Information Technology Agency (MITA) is being issued for other purposes, such that the values in the ageing analysis provided do not tally with ARR, as noted above. TM also stated that as from January 2015, efforts will be made to issue an ageing analysis that conforms with the arrears template.

### Airport Tax

An amount of €334,443, pertaining to airport tax, was transferred from the Civil Aviation Directorate, and thus reported under the opening gross balance in the 2013 Return. Such balance, which is considered as not collectable, was originally due by two airlines, in terms of the Civil Aviation Regulations, applicable only with respect to Malta-originating passengers.

Court action was taken on the amount of €197,009, which claim was lost in both local and foreign Law Courts. The remaining amount of €137,434 is an estimate of the amount due from one airline for the year 2007, which is also considered as not collectable. Write-off of the full amount is being considered during 2014.

### Road Licence Regularisation Scheme

Registered owners with accumulated unpaid licences were given the possibility of regularising their position, thus benefiting from a reduction in licence and administrative fees, depending on whether the vehicle is scrapped, garaged or has its licence renewed.

During 2013, a total of 24,751 Notice Letters were sent to owners of unlicensed vehicles, of which 1,278 (*i.e.* 5%) regularised their position in line with the Scheme. To this effect, as reported in 2013 ARR, out of the total arrears collected of €355,309, the sum of €322,891, consisting of licence fees (€161,232) and administrative fees (€161,659), were collected.

### Ministry for Gozo

The Ministry's Arrears of Revenue consist solely of amounts payable to the Projects and Development Directorate, namely to the Works, Agriculture, and Public Cleansing Departments.

The opening balance in 2013 stood at €248,303, of which only €8,090 were collected by the Public Cleansing Department during the year under review, in respect of services rendered to Local Councils. Arrears newly accrued during the year amounted to €13,306, resulting in a closing balance of €253,519, out of which the amount of €28,183 is being estimated as not collectable.

A total of €149,030 of the outstanding amount is due to the Public Cleansing Department, in connection with waste disposal services. This amount, made up of €104,666 owed by individuals and private companies, and a balance of €44,364 due by Government Entities, has been constant at least for the past four years, and yet, although records in connection with the balance of amounts due were incomplete, the Department is still expecting to collect the entire sum.

Outstanding balances due to the Works and Agriculture Departments by Local Councils have still not been recovered.

The Ministry's performance and ageing of debtors can be analysed as follows:

Department	Opening Balance	Amount Collected	Percentage Collected	Gross Outstanding Balance	Amount considered as not collectable
	€	€	%	€	€
Public Cleansing – Local Councils	31,185	8,090	26	34,158	1,132
Public Cleansing – Waste Disposal	149,030	-	-	149,030	-
Works	39,880	-	-	39,880	-
Agriculture	28,208	-	-	30,450	27,051
<b>Totals</b>	<b>248,303</b>	<b>8,090</b>		<b>253,518</b>	<b>28,183</b>

Ageing of the net collectable arrears:

	€
Amounts outstanding for less than one year (2013)	14,464
Amounts outstanding for over one but less than two years (2012)	4,192
Amounts outstanding for over two but less than five years (2009 – 2011)	-
Amounts outstanding for over five but less than ten years (2004 – 2008)	25,385
Amounts outstanding for over ten but less than twenty years (1994 – 2003)	<u>181,295</u>
<b>Net Closing Balance</b>	<b>225,336</b>

### *Gozo Law Courts*

The opening balance as at 1 January 2013, reported in ARR submitted by the Gozo Law Courts, stood at €221,064 and €354,722 for Fines and Fees respectively.

#### *Court Fines*

As disclosed in ARR, out of the aforementioned balance, during the year under review, €41,562, *i.e.* 18%, were collected, while €1,205 constituted a downward revision in respect of amounts considered as not due, relating mainly to revoked fines. On the other hand, newly accrued amounts totalled €49,231, resulting in net collectable arrears of €227,528 as at 31 December 2013.

The opening balance reported in ARR does not tally with that of €221,435, shown in the Fines Report extracted from the Lecam system. The difference of €371 arises from variations in the amount of two fines, between the closing balance of 2012 and opening balance of the following year, and another fine included with 2013 opening balance but not in the closing balance of the prior year. Moreover, as highlighted in previous years, the said report still includes 16 fines disclosed with a negative balance, distorting the true picture. For example, a case which was encountered this year, relates to fines inflicted in 2006, where an actual opening balance of €908 was eventually reported as €743 due to two negative balances, in aggregate amounting to €165. Consequently, the amount collected was greater than the opening balance, thus again ending with a reported negative closing balance. Similar instances were also noted in fines relating to other periods.

Another shortcoming, also reported upon previously, relates to fines which have been settled but the respective amounts are still reported as outstanding. For example, two such fines of €466 each, identified in last year's write-up, are still shown as outstanding in the current year's Lecam report notwithstanding that one was paid in 1998, while a prison term was served in lieu of payment in the case of the other fine.

Once again, due to the limitations in the system, no distinction was made between amounts written-off and those considered as not due. As a result, separation of these amounts had to be done manually by NAO for audit purposes.

Since fines are deemed to be revenue attributable to the Courts of Justice Division in Malta, with the role of Gozo Courts limited to the monitoring of their collection process, outstanding amounts were not included in the Debtors' List submitted by the Gozo Courts, giving rise to a discrepancy of €227,528 between the latter and ARR.

### Court Fees

The opening balance for 2013, as reflected in the Fees Report extracted from the Cortex computerised system, stood at €354,690. This is understated by €32 when compared to the amount disclosed in ARR. This immaterial variation has been reported as not due and relates to the aggregate differences in two fees, between the 2013 opening balances and the closing balances of previous year.

During the year under review, the amount of €49,370 was collected in Court Fees, while €32,481 is revenue accrued during the same year. This gives a gross closing balance of €337,802, of which €45,112 are estimated as not collectable.

A discrepancy of €2,238 in Court Fees was also noted between ARR and the Debtors' List.

The ageing of the gross outstanding arrears<sup>2</sup> can be analysed as follows:

	€
Amounts outstanding for less than one year (2013)	81,712
Amounts outstanding for over one but less than two years (2012)	142,605
Amounts outstanding for over two but less than five years (2009 – 2011)	182,833
Amounts outstanding for over five but less than ten years (2004 – 2008)	75,105
Amounts outstanding for over ten but less than fifteen years (1999 – 2003)	41,927
Amounts outstanding for over fifteen but less than twenty years (1994 – 1998)	23,031
Amounts outstanding for over twenty years (1960 – 1993)	<u>18,117</u>
<b>Gross Closing Balance</b>	<b>565,330</b>

<sup>2</sup> Ageing is reported for all outstanding balances since information with respect to amounts estimated as not collectable could not be reliably determined.

## Ministry for Social Dialogue, Consumer Affairs and Civil Liberties

### *Industrial and Employment Relations*

The Department of Industrial and Employment Relations assumed responsibility to recoup arrears consisting of outstanding repayment of loans under the 'Self Employed Loan Incentive Scheme', which was introduced in the 1989 Budget and terminated at the end of 1992. The aim of this Scheme was to assist individuals to start up a business enterprise.

At the beginning of the year 2013, the gross outstanding balance amounted to €310,979, which was due to the Department by 75 individuals who benefitted from this Scheme. During the year under review, the amount of €2,498 was collected from past arrears, representing 0.8% of the opening balance.

The outstanding balance comprises a provision for bad debts amounting to €195,685, leaving a net collectable balance of €112,796, analysed as follows:

	€
Amounts outstanding for over fifteen but less than twenty years (1994 – 1998)	108,671
Amounts outstanding for over ten but less than fifteen years (1999 – 2003)	4,125
Amounts outstanding for less than ten years (2004 – 2013)	<u>-</u>
<b>Net Closing Balance</b>	<b>112,796</b>

The provision, which includes an amount of €22,821 pertaining to five deceased defaulters, is due by debtors who have not effected payments since May 2010. The Department has not yet planned the course of action to be taken with respect to the pending amounts. However, it was maintained that by sending Judicial Letters followed by Legal Letters, the repayment of loans is not time-barred.

During 2013, reminders were only sent to those defaulters who had committed themselves to start effecting periodic payments, following receipt of a Legal Letter previously sent by the Department.

## Ministry for the Economy, Investment and Small Business

### *Lotteries and Gaming Authority*

The Lotteries and Gaming Authority (LGA) reported a net outstanding arrears balance of €639,576 for the year ended 31 December 2013. This amount can be analysed as follows:

	€
a. Duties	198,576
b. Licence Fees	<u>441,000</u>
<b>Total</b>	<b>639,576</b>

### *Estimated as Not Collectable*

From the gross outstanding balance of €1,509,162 as at 31 December 2013, an amount of €869,586 was reported under the heading 'Estimated as not Collectable'. A significant increase of €513,499 was noted in this amount when compared to the 2012 Return, where a balance of €356,087 was reported.

Following NAO enquiry, LGA confirmed that out of this increase, an amount of €496,499 related to dues from a particular licensee and its subsidiaries, which were experiencing financial difficulties. As a result, during the year under review, their licence was suspended for not paying their outstanding dues. The

remaining balance of €17,000 related to a different operator, which was also suspended by LGA for not paying the licence fee due to financial problems.

LGA confirmed that both operators were reported to the police and legal proceedings have been initiated against them.

### Ageing Analysis

An ageing analysis of net outstanding arrears, which was also provided by LGA, confirmed that the majority of arrears were outstanding for less than one year, with only less than 10% being due for a longer period. Ageing of arrears is as follows:

	€
Amounts outstanding for less than one year (2013)	579,766
Amounts outstanding for over one but less than two years (2012)	<u>59,810</u>
<b>Net Closing Balance</b>	<b>639,576</b>

### Malta Communications Authority

The gross closing balance as at 31 December 2013 reported by the Malta Communications Authority (MCA) in relation to Radio Communication Licences, amounted to €155,281.

The outstanding balance at the end of 2013, can be analysed as follows:

	€
Amounts outstanding for less than one year (2013)	97,049
Amounts outstanding for over one but less than two years (2012)	23,184
Amounts outstanding for over two but less than five years (2009 – 2011)	34,513
Amounts outstanding for over five but less than ten years (2004 – 2008)	302
Amounts outstanding for over ten years ( – 2003)	<u>233</u>
<b>Net Closing Balance</b>	<b>155,281</b>

MCA confirmed that, as from end December 2011, the Authority took over arrears, which aged up to three years from the respective Ministry, with the exception of four licensees, which were due for more than three years. It was confirmed that in two of these cases, all dues have been paid and the licence has been cancelled, whilst in a separate case, discussions in relation to the collection of arrears are underway. In the remaining instance, legal action is being taken.

### Revisions

Revisions of €19,258 were reported in the 2013 ARR. Upon NAO enquiry, MCA confirmed that these revisions related to arrears due from Enemalta, which had to be cancelled by the issue of credit notes. These revisions related to licences to install and/or use 77 mobile radios, which Enemalta was no longer using.

Even though these radios had not been used for a number of years, Enemalta failed to initiate licence cancellation procedures. Once these procedures were started, MCA through its Legal Department, had to take all the necessary precautions to ensure that the equipment was dismantled and no longer in use.

## Collection Efforts

Back in 2012, shortly after MCA took over the management of individual radio communications equipment licensing, MCA had implemented an online payment gateway in an attempt to facilitate the collection of overdue licence fees.

During the last quarter of 2013, MCA was also working on the implementation of a new licensing system, which has been operational since January 2014. This system is providing more flexibility in the production of reports, which are also providing details regarding aged debtors.

MCA has also adopted a licensing enforcement process in order to address situations where licensees fail to pay their prescribed annual fee. This process involves the use of Legal Letters, which are sent to all defaulters. In those cases where the Legal Letter proves to be futile, and overdue fees are still unsettled within a defined period, MCA resorts to legal action.

Up to the date of writing of this report, MCA considers this process to be successful since it has managed to regularise the position of a number of defaulters without the need of initiating any legal action. In this regard, NAO has noted that the figure for net collectable arrears as at December 2013 stood at €155,281; a decrease of €172,589 (53%) over the same figure for 2012 (€327,870).

## Television Licensing Unit

Arrears due to Government falling under the responsibility of the Television Licensing Unit (TVLU) as at 31 December 2013, were reported as €10,408,726. This balance is made up of outstanding:

- a. television licences amounting to €10,173,850; and
- b. radio communication licences totalling €234,876.

## Amounts Estimated as Not Collectable

### Television Licences

A total of €4,069,513, calculated at 40% of the gross collectable arrears as stated by the Department, was reported as not collectable in ARR for 2013.

### Radio Communication Licences

An amount of €189,004, pertaining to 132 licences, was also reported as not collectable in the 2013 Return for a variety of reasons. These consisted of licensees being companies in dissolution, lack of data and the considerable fees involved to proceed legally.

## Ageing Analysis

NAO was informed that the extraction of an ageing analysis from the system in relation to net collectable balances of €6,104,337 and €45,872, pertaining to television and radio communication licences respectively, was very complicated. Therefore, the said information could not be reported upon in this year's write-up.

## Collection Efforts

### *Television Licences*

A meeting held by NAO with relevant officials revealed that TVLU is in the process of sending a number of Legal Letters in pursuit of those debtors with the highest balances due.

In a separate exercise, a number of write-offs are also being considered with respect to immaterial amounts, which have been due for a period longer than five years.

### *Radio Communication Licences*

During a separate meeting discussing licences transferred from MCA in 2011, it was confirmed that following their transfer to the Ministry, a final notice was sent to these defaulters, of which some were Government Departments, and others were companies without a registration number or in dissolution.

In 2012/2013, a number of Official Letters were sent to the remaining defaulters. In some instances, the dues were settled, whilst in 20 other instances, Court cases were initiated. Presently six legal cases remain unresolved. In these instances, appropriate action will be taken when Court proceedings are finalised.

Similar to the exercise involving television licences, write-offs are being considered in those cases where the amounts are relatively small or prescribed.

### *Trade Services (Commerce)*

The following is a sub-classification of the gross closing balance of arrears as reported by the Trade Services (Commerce) Department in the 2013 ARR:

	€
a. Trading Licences	3,784,524
b. Miscellaneous Receipts	4,000
c. Penalties paid by Students	<u>7,549</u>
<b>Total</b>	<b>3,796,073</b>

Out of the total gross outstanding arrears in relation to trading licences, the amount of €2,119,924 related to active licences. The remaining amount of €1,664,600 represents amounts considered as not collectable (€837,585), and licences which were already withdrawn, or in the process of being withdrawn and/or cancelled (€827,015).

### Revisions

Total revisions of €468,020 were reported in relation to trading licences in the 2013 ARR, which was considerably more than the amount of €147,354 reported under the same heading in 2012.

In line with the previous year's understanding, explanations from the Department revealed that these revisions either related to tariffs waived off following the legal amendments of 2007 (€135,759), or relate to licences that were no longer in use, but were not cancelled by the respective licensees (€332,261).

### Amounts considered as Not Collectable

A significant increase was also noted in the amounts considered as not collectable, which amounted to €54,371 in 2012, and increased to €837,585 in 2013. Clarifications from the Department showed that this increase was due to a change in the way the Department was calculating this amount, based on the premise that older debtors had a lesser probability of collection. In fact, arrears pertaining to the period 2001 – 2009 were assigned a 50% probability that such dues will not be collected. More recent arrears (2012 – 2013) attracted a 20% probability of uncollectability.

### Ageing Analysis

A detailed analysis of net collectable arrears was provided by the Trade Services Department as follows:

	€
Amounts outstanding for less than one year (2013)	147,381
Amounts outstanding for over one but less than two years (2012)	356,726
Amounts outstanding for over two but less than five years (2009 – 2011)	869,072
Amounts outstanding for over five but less than ten years (2004 – 2008)	1,161,701
Amounts outstanding for over ten but less than fifteen years (1999 – 2003)	417,421
Amounts outstanding for over fifteen but less than twenty years (1994 – 1998)	-
Amounts outstanding for over twenty years (– 1993)	<u>7,549</u>
<b>Net Closing Balance</b>	<b>2,959,850</b>

As reported last year, the amount of €7,549, consisting of penalties due by students who failed to honour their contracting obligations, pertains to the period 1986 till 1989, thus being outstanding for more than 20 years.

NAO further noted a difference of €1,362 between the net collectable arrears due in relation to trading licences, and the related ageing analysis, in respect of which no explanation was provided.

### Collectability of Trading Licences

Management stated that during 2013, the necessary staff redeployment, as well as changes to the Department's procedures were effected, in view of the amendments to the trade licensing legislation enacted in November 2012.

To this effect, during the year under review, the Department issued a number of Renewal Notices in relation to trading licences. A total of 16,028 reminders were issued in relation to licences which had been due for more than one year, 1,670 of which had been outstanding for over four years or more. An additional 3,967 reminders were issued to licence holders who had not paid their dues for 2013, whilst another 843 reminders were sent to the heirs of deceased licensees.

Furthermore, approximately 1,100 Legal Letters were also issued in 2013 and 2014, and around 15,000 Renewal Notices for 2014 were being issued at the time of the review.



## Ministry for the Family and Social Solidarity

### Social Security Benefits

DSP reported a figure of €18,594,832 as gross/net collectable arrears in ARR in relation to Social Security Benefits for 2013, an increase of 15% over the same figure reported last year. This amount represents various Social Security Benefits and Assurances, which have been overpaid to beneficiaries and are thus due to Government.

The Return groups all benefits and assurances together, and does not provide a breakdown of the amounts pertaining to each benefit/assurance type. However, such an analysis was included as part of the supporting documentation provided by DSP, and can be summarised as follows:

#### Benefit/Assurance Type

	€
a. Social/Unemployment Assistance, including Drug Addict <i>etc...</i>	10,069,507
b. Age/Old Age/Carers/Blind and Disability Pensions	1,612,907
c. Milk Grant, Sickness/Leprosy/Tuberculosis Assistance	937,964
d. Marriage Grant, Unemployment/Injury/Maternity/Sickness Benefit <i>etc...</i>	216,229
e. Six Month/Special Weekly/Cost of Living Allowance Bonuses	132,207
f. Children/Foster Child Allowance	1,579,490
g. Supplementary Allowance	120,527
h. Pensions (various)	3,816,668
i. Energy Benefit	106,448
j. Senior Citizen Grant	<u>2,885</u>
<b>Total</b>	<b>18,594,832</b>

From the above information, it transpires that more than half (54%) of the overpayments relate to social and/or unemployment assurances. This observation is exactly congruent to a similar analysis conducted during the 2012 review.

#### Revisions

Supporting documentation was not provided in relation to Revisions amounting to €189,844 reported in ARR. The latter specified that these amounts pertain to adjustments carried out by DSP which should have been included in the 2012 gross arrears. However, no further explanations in this regard were provided by DSP at the time of writing of this report.

#### Estimated Amounts considered as Not Collectable

Additionally, ARR did not include a figure in relation to amounts considered as not collectable. From information provided by the Department, the calculation of this information would prove to be difficult and subjective, however up to the date of NAO review, an exercise was being carried out to identify overpayments in relation to deceased beneficiaries. The results of this exercise would help the Department in determining which overpayments are most likely to be recouped, based on the respective dates of death and last repayment dates. The residual balances could then be reported as not collectable.

## Write-offs

For testing purposes, a sample of eight write-offs was selected at a total value of €28,472, which represents 40% of total write-offs. Of these, no Permanent Secretary approval was traced in relation to a write-off for €5,794 that related to an overpayment of two-thirds pension.

## Amounts Collected

Following testing in relation to amounts collected during 2013, it transpired that repayments in relation to two overpayments whose balances stood at €34,733 and €47,657 at the end of 2013, amounted to only €17 and €75 respectively. No evidence was traced in the respective files showing whether action is being taken by the Department to recoup the overdue amounts.

## Ageing Analysis

An ageing analysis of balances due at year-end reveals the following:

	€
Amounts outstanding for less than one year (2013)	5,122,567
Amounts outstanding for over one but less than two years (2012)	3,399,603
Amounts outstanding for over two but less than five years (2009 – 2011)	5,703,032
Amounts outstanding for over five but less than ten years (2004 – 2008)	2,796,931
Amounts outstanding for over ten years (1974 – 2003)	<u>1,572,699</u>
<b>Gross/Net Closing Balance</b>	<b>18,594,832</b>

Testing in relation to aged debtors revealed that although a number of overpayments have been pending for numerous years, and supporting documentation in their regard is lacking, they still featured in ARR.

Specifically, the departmental file in relation to an overpayment of €2,812, which has been due since 1984, is not available and no supporting documentation in its regard has been traced. Moreover, this amount does not feature in the Social Assistance and Benefits System (SABS).

Additionally, no supporting documentation was traced in relation to two overpayments of €3,816 and €6,640, which have been due since 1989 and 1995 respectively. The former overpayment was also not included in SABS. In both these cases, no evidence has been traced to show whether these amounts are being actively chased for collection.

Testing has also revealed that no repayments have ever been made against an overpayment of €6,642, which was created in 1991 in relation to Social Assistance. This case was referred for legal action in 2002, but no further action has been taken since. Furthermore, this overpayment could not be traced in SABS, and although the respective file gave details of the overpayment, the reason behind it was not stated.

## Collection Efforts

In an effort to recoup the amounts overdue, the Department either withholds part of any Benefits or Assurances that the beneficiary may still be receiving, or, whenever possible, enters into repayment agreements.

## *Elderly and Community Care*

The Elderly and Community Care Department reported a net collectable balance of €3,136,595, which represents an increase of 44% over the amount of €2,179,633 reported by same for the year ended 31 December 2012.

The Return submitted by the Department incorporates the following revenue categories:

	€
a. Staff Salaries Reimbursement	3,067,950
b. Revenue Account	61,055
c. Telephone	6,814
d. Training	<u>776</u>
<b>Total</b>	<b>3,136,595</b>

Whilst no amounts were reported as not collectable in the 2013 ARR, only a balance of €21,533 was recouped during the year, mostly pertaining to the Revenue Account.

### *Staff Salaries*

The amount of €3,067,950, which represents 98% of total arrears as at 31 December 2013, relates to staff salaries due from various Government Departments in relation to staff seconded by the Elderly Care Department. According to information provided, there were 36 seconded employees (mostly Geriatric Consultants), the majority of whom performing duties at Karin Grech and Mater Dei Hospitals (MDH).

Notwithstanding that the Department stated that reminders are sent throughout the year, no amount was collected during 2013 with respect to this category.

### *Revenue Account*

This Account receives to 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. DSP identifies any other income earned by the various residents within said homes, and through a shared software, the Elderly Care Department is able to calculate the total amount due in line with the provisions of Legal Notice 259 of 2004.

The total amount of €61,055 is due from 110 debtors, with the oldest balances being due since 2008.

### *Telephone and Training*

The amount of €6,814 relates to telephone expenses collectable from the three other Departments housed within the same building as the Elderly and Community Care Department. The full amount due relates to invoices issued during 2013. The amount, pertaining to training expenses, has been due since 2010.

### *Efforts for Collection*

In an effort to collect the balances due, the Accounts Section within the Elderly and Community Care Department sends monthly reminders, together with a copy of the respective invoice, to those with overdue amounts.

## Ageing Analysis

The outstanding balances can be analysed as follows:

	€
Amounts outstanding for less than one year (2013)	1,012,384
Amounts outstanding for over one but less than two years (2012)	705,665
Amounts outstanding for over two but less than five years (2009 – 2011)	1,417,855
Amounts outstanding for over five but less than ten years (2004 – 2008)	<u>1,152</u>
<b>Net Closing Balance</b>	<b>3,137,056</b>

An immaterial discrepancy of €461 was noted between the net collectable arrears in ARR and the ageing analysis.

## Ministry for Home Affairs and National Security

### *Armed Forces of Malta*

The gross closing balance as at 31 December 2013, disclosed by the Armed Forces of Malta (AFM) in its ARR, stood at €728,024 and can be analysed as indicated hereunder:

	€
a. Patrol Craft Conveyance/Hire of Vehicles and Machinery	373,908
b. Security Duties	269,014
c. Helicopter and other services rendered by AFM	80,953
d. Refund of Wages	<u>4,149</u>
<b>Gross Closing Balance</b>	<b>728,024</b>

The outstanding balance comprises a provision for bad debts amounting to €96,564 leaving a net collectable balance of €631,460. An amount of €451,973 is due from Government and Parastatal Entities, whilst the remaining balance of €179,487, is expected to be collected from individuals and/or private companies.

## Ageing Analysis

	€
Amounts outstanding for less than one year (2013)	631,213
Amounts outstanding for over one but less than two years (2012)	<u>247</u>
<b>Net Closing Balance</b>	<b>631,460</b>

The aggregate opening balance was revised downwards by a net amount of €21,690, comprising of an invoice of €21,816 being declared as not due and another invoice originally showing €380 which was corrected to €506. The amount of €21,816, was a claim for reimbursement of course expenses which, was to be recorded in the Below-the-Line Account that MFIN had granted approval for AFM to operate.

The amount of €96,564 considered as not collectable consists of arrears ranging between the years 1993 to 2009. The foregoing consists of a substantial amount of €75,244 (*i.e.* 78%), which is due by a Government department for patrol craft conveyance services, provided during 2008. On 3 July 2011, AFM requested authorisation from OPM to write off the claim however, upon enquiry it was confirmed that there were no developments as at testing date. With regard to the remaining balance of €21,320, AFM's Legal Branch, has to initiate an exercise to establish which claims are time-barred.

## Police

### Overview

The disclosed gross closing balance of arrears of revenue pertaining to the Police Department, as at 31 December 2013, amounted to €396,070, analysed as indicated hereunder:

	€
a. Weapons (Sporting) Licences	318,055
b. Miscellaneous Fines (issued to Airlines and Shipping Companies)	53,650
c. Services to Third Parties (Extra Duty)	13,984
d. Other Revenue (Miscellaneous, due from Third Parties)	<u>10,381</u>
<b>Gross Closing Balance</b>	<b>396,070</b>

### Weapons (Sporting) Licences

The opening balance of €319,478 was revised upwards by €1,776, mainly as a result of human errors when transferring ownership of licences from one district to another. An estimated amount of €13,995 has been considered as not collectable, mostly due to firearms being confiscated by the Courts, without the Police's Weapons Office being informed.

### Miscellaneous Fines

From an opening balance of €81,878, an amount of €43,443 was written off during the period under review. However, from audit testing it was revealed that only an approval from the Commissioner of Police was sought and subsequently granted for writing off two cases, amounting to €15,141 each, in which case, approval from MFIN should have been sought.

Furthermore, following a decision taken by the Immigration Appeals Board in October 2011, and consultation with the Attorney General's (AG) Office in August 2012, no action was taken by the Police Department to collect a fine of €27,370, initially in dispute with the individual. As a result, there is a risk that such amount becomes time-barred.

### Ageing Analysis

As reported in previous years, an ageing analysis of Weapons (Sporting) Licences cannot be carried out using the current Information Technology system in place, as this does not provide such information. However, the Police Department is working with MITA to develop a new system, which will enable the necessary reporting.

The Police Department also confirmed that the ageing of arrears due from Services to Third Parties (Extra Duty) is unavailable.

Meanwhile, an ageing analysis of the remaining debtors, (Miscellaneous Fines and Other Revenue) can be summarised as follows:

	€
Amounts outstanding for less than one year (2013)	2,666
Amounts outstanding for over one but less than two years (2012)	23,068
Amounts outstanding for over two but less than five years (2009 – 2011)	35,968
Amounts outstanding for over five but less than ten years (2004 – 2008)	<u>2,329</u>
<b>Total (Miscellaneous Fines and Other Revenue)</b>	<b>64,031</b>

## Limitation on Scope

An attempt to check the collection efforts on a sample of cases, with regard to Weapons (Sporting) Licences, proved futile since the Police Department did not submit the relevant information in time to be analysed by NAO.

## Land Registry

The Arrears of Revenue reported by the Land Registry relate to outstanding fees from official searches on individuals and entities, requested by notaries and other third parties, in connection with transfers, liabilities and testamentary searches.

The gross closing balance of arrears as at 31 December 2013 stood at €74,985, an ageing analysis of which is provided below:

	€
Amounts outstanding for less than one year (2013)	11,563
Amounts outstanding for over one but less than two years (2012)	1,635
Amounts outstanding for over two but less than five years (2009 – 2011)	27,764
Amounts outstanding for over five but less than ten years (2004 – 2008)	33,436
Amounts outstanding for over ten but less than fifteen years (1999 – 2003)	<u>587</u>
<b>Gross Closing Balance</b>	<b>74,985</b>

This outstanding balance comprises a provision for bad debts, amounting to €31,997, out of which write-off authorisation in respect of arrears, amounting to €20,190 was obtained from the Permanent Secretary during April 2014. This leaves a net collectable balance of €42,988 due from individuals and/or private companies.

## Past Arrears Collected

As reported in previous years, the 'Past Arrears Collected' could not be determined since it was not feasible for the Department to extract a list of claims paid during the year, from the system currently in place. Therefore, the amount in question, totalling €18,048, is a balancing figure and as such, the accuracy of the foregoing is doubtful. By way of example, during 2013 an amount of €3,000, was recovered in weekly instalments following a court judgment, yet the remaining balance due as at 31 December 2013, totalling €6,663 did not feature in the 'List of Searches' indicating outstanding claims. The Department envisages that such problems will be resolved when the Information Technology system is replaced, by the third quarter of 2015.

## Collection Efforts

The Department started sending Default Notices requesting payment, followed by a Judicial Letter after the third reminder. Thus, the occurrence of arrears becoming time-barred would be minimised as much as possible. Alternatively, a court case may be initiated. Moreover, a number of defaulters were notified that until arrears were settled, a deposit of €233 was required for every new search application submitted.

## Judicial

The Return of Arrears reports submitted by the Courts of Justice (COJ) Department, are extracted from the Lecam and Cortex computerised systems, respectively. Whilst the former system issues reports with respect to fines, the latter relates to court fees. As pointed out in prior years, accrued fees and fines extracted from these systems are not proving to be reliable. Several shortcomings prevailing from previous years have not yet been sorted out.

COJ has been in discussions with MITA, on a new computerised system, since 2009. This system is expected to improve the revenue reporting functions and allow for better collection of revenue in arrears. Up to the date of concluding this write-up this task was still in progress. According to MITA, the contracted date for completion is June 2015.

Similar to last year, COJ carried out another intensive exercise, whereby each fine and fee was reviewed and various discrepancies were noted. Where possible, amendments were made accordingly, resulting in a net downward revision of €217,948 to the closing balance of €12,416,067 as reported in previous year.

During the year, the amount of €1,522,931 was collected, whilst the newly accrued arrears totalled to €1,882,169.

Notwithstanding that during the year under review approvals were obtained to write off the total amount of €1,090,689, in their Return COJ reported the amount as €1,074,350, as per that issued from the computerised reports. In an email correspondence dated 17 October 2014, COJ confirmed that the latter figure was incorrect and that this was the result of the malfunctioning computerised systems. Action to correct these figures was taken during 2014.

The majority of the amount written off pertained to fees due from deceased defaulters, whilst the remaining balance related to a number of fees of immaterial amounts from untraceable individuals.

The gross closing balance as at 31 December 2013, disclosed by COJ has been analysed hereunder. These will be discussed further on in the report.

	€
a. Court Fines – Judges	4,789,299
b. Court Fines – Magistrates	4,384,329
c. Court Fees	2,255,809
d. Superior Registry – Civil Fines	26,961
e. Inferior Registry – Civil Fines	<u>26,609</u>
<b>Gross Closing Balance</b>	<b>11,483,007</b>

From the gross closing balance of €11,483,007, the amount of €144,611 relates to dues that are considered as difficult to be recouped, as explained further on in this write-up, leaving a net collectable balance of €11,338,396, out of which, by end of January 2014, the amount of €233,824 was already recouped.

The ageing of debtors as at year-end 2013 can be analysed as follows:

	€
Amounts outstanding for over twenty years (1969 – 1993)	180,686
Amounts outstanding for over fifteen but less than twenty years (1994 – 1998)	3,126,119
Amounts outstanding for over ten but less than fifteen years (1999 – 2003)	949,853
Amounts outstanding for over five but less than ten years (2004 – 2008)	2,391,521
Amounts outstanding for over two but less than five years (2009 – 2011)	1,811,635
Amounts outstanding for over one but less than two years (2012)	996,413
Amounts outstanding for less than one year (2013)	<u>1,882,169</u>
<b>Net Closing Balance</b>	<b>11,338,396</b>

## Court Fines

### *Judges' Court Fines*

The opening balance of €5,588,990 for 2013, was revised upwards by €80,892. According to COJ, this revision was mainly due to fines that in the past were converted into imprisonment, and therefore the amount was not due anymore. However, during the year under review, the respective individuals paid the fines that were inflicted on them and hence, they had to be reinstated in the system.

During 2013, the amount of €214,665, *i.e.* less than 4%, was collected, whilst the newly accrued arrears amounted to €333,297. An aggregate amount of €999,215, relating to 131 fines, dating between 1986 and 2011, was written off. The considerable amount written off included two fines, amounting to €939,740 and €21,000 respectively, which were due from two individuals who passed away.

Out of the €4,789,299 gross closing balance, the amount of €35,003 (*i.e.* 0.7%) relates to fines due from untraceable debtors and hence, they are being considered as not possible to recoup, leaving a net collectable balance of €4,754,296.

From the outstanding balance, the amount of €3,960,508, *i.e.* 83%, is due from only four individuals. Whilst the amount of €1,141,288 is due from one debtor and relates to a fine inflicted in 2004, the remaining balance represents three fines imposed in 1998 on three persons, each owing the sum of €939,740.

### *Magistrate Court Fines*

The Return for year 2012 indicated a closing balance of €4,617,811. For 2013, COJ reported a downward revision of €293,315 to this opening balance. Following a thorough exercise, COJ submitted to this Office a detailed report illustrating the reasons for every variance, the major difference being the revocation of the conversion into imprisonment, as that reported under the 'Judges' Court Fines'.

During the year under review, COJ collected the amount of €1,059,558, whilst the newly accrued debtors amounted to €1,168,926. Write-off approvals were obtained from respective level of authority for the amount of €49,535.

The 2013 ARR indicated a gross closing balance of €4,384,329, out of which the amount of €109,608 relates to fines that are considered as not possible to be recouped, since they are due from untraceable debtors, some of which are residing abroad, and deceased defaulters, leaving a net collectable balance of €4,274,721.



## Court Fees

The database reflecting the amendments to the figures, as issued from the Cortex system forwarded to this Office, indicated an opening balance of €2,157,570, out of which the amount of €241,842 was collected, and €24,325 was written off. Arrears newly accrued amounted to €364,406, giving a net collectable balance of €2,255,809 as at 31 December 2013.

## Civil Fines

### *Superior Registry*

Revoked fines by a Court's decree were the main reason why COJ revised downwards the opening balance of €32,810, by €5,325.

Out of the balance due at the beginning of the year, the amount of €6,214 was collected whilst €70 were written off. As at 31 December 2013, the outstanding net balance stood at €26,961, which includes €5,760 newly accrued arrears.

### *Inferior Registry*

The opening balance of €18,886 was revised downwards by €200. This amount represents a revoked fine by a Court decree, as well as a cancelled receipt which was incorrectly recorded in the system. During the year under review, the amount of €1,205 was written off, since it was considered difficult to recoup. The amount of €652 was collected whilst newly accrued arrears amounted to €9,780, leaving a net closing balance of €26,609.

### *Attorney General*

The opening balance of €6,348 reported in the original ARR by AG's Office was revised upwards to €17,473 after NAO's review, mainly due to omissions of various debtors in last year's return.

The newly accrued arrears totalling €16,560 are made up of 38 debtors, while the net collectable balance of €25,496, as at end December 2013, is due from 63 individuals with respect to court cases.

## Ageing Analysis

Amounts outstanding for over five but less than ten years (2004 – 2008)	€ 2,823
Amounts outstanding for over two but less than five years (2009 – 2011)	74
Amounts outstanding for over one but less than two years (2012)	6,039
Amounts outstanding for less than one year (2013)	<u>16,560</u>
<b>Net Closing Balance</b>	<b>25,496</b>

## Ministry for Finance

The gross/net closing balance as at 31 December 2013, as provided by MFIN, consists of:

	€
a. Quality Assurance Unit	8,463
b. Miscellaneous Reimbursement	13,359
c. Training	<u>3,600</u>
<b>Total</b>	<b>25,422</b>

It was confirmed that miscellaneous reimbursements of €8,160, which became due in 2012 by Gozo Ferries Ltd, in respect of a fee charged by the Government on a Letter of Guarantee issued in favour of the company, was settled in January 2014.

The Department has yet to recover a prepayment of €3,600, made towards training courses, which did not materialise during 2012.

An ageing analysis of the collectable arrears is as follows:

	€
Amounts outstanding for less than one year (2013)	8,882
Amounts outstanding for over one but less than two years (2012)	11,760
Amounts outstanding for over two but less than five years (2009 – 2011)	-
Amounts outstanding for over five but less than ten years (2004 – 2008)	-
Amounts outstanding for over ten but less than twenty years (1994 – 2003)	<u>967</u>
<b>Total</b>	<b>21,609</b>

An ageing of the remaining balance of €3,813 could not be provided by the Ministry.

### *Treasury Department, Salaries and Pensions Section*

The gross/net arrears closing balance as at 31 December 2013, as provided by the Treasury Department, Salaries and Pensions Section, consists of:

	€
a. Pension Claims from Public Entities	23,221,843
b. Refunds of Deceased Pensioners	17,254
c. Overpayments to Pensioners	11,932
d. Special Cases	<u>4,979</u>
<b>Total</b>	<b>23,256,008</b>

During the year, the sum of €19,549 was collected, representing 0.08% of the opening arrears balance as at 1 January 2013. This is considerably less than the equivalent amount collected during 2012, which amounted to €1,344,162 and represented 6% of the then opening balance.

Considering the materiality of the amounts still due, the Department forwarded a number of explanations in relation to each of the categories of arrears.

### *Pension Claims from Public Entities*

The amounts due from Public Entities include arrears from all Entities that employed officers, who on the date of retirement had the right for a Treasury Pension.

During 2013, there has been no movement in this category of arrears, with the respective opening and closing balances tallying at €23,221,843 in ARR. The Department confirmed that Notification Letters with respect to amounts due for 2013 were sent by the end of the first week of October 2014.

The Department also stated that the collection of these dues, especially from Entities such as Enemalta and Water Services Corporation may prove to be difficult, and would require intervention from outside the Department to ensure collection. Furthermore, two Entities are currently refusing to acknowledge their claims, and although the Department is assisted by AG, these matters remained pending.

In an effort to collect the outstanding amounts, Treasury Pensions Department aims to keep up-to-date records of the amounts due from each Entity, and has the intention to enter into agreements to ensure a timely and full repayment.

### Refunds of Pension issued to Deceased Pensioners

These dues consist of payments issued by the Department to individuals who passed away during the period to which the pension relates. As confirmed in the 2012 review, recoupment of overpaid amounts is then made either directly through the pensioner's bank account, or when the account has been closed, by sending a letter requesting collection from the registered heirs. The Department also confirmed that the agreement that was made with a local bank in 2012 allowing for payments to be processed through bank transfers, was still in place during 2013.

In a bid to reduce overpayments, the Department is linked to the Central Database, through which officials can ensure that whenever a beneficiary passes away, payments are stopped immediately without having to wait for the heirs to inform the Department of the demise.

During 2013, the Department was also in contact with the Corradino Correctional Facility to ensure that no payments were being made to Treasury pensioners who have been served with an effective imprisonment sentence.

### Overpayments to Pensioners

These overpayments arise when pensioners who decide to resume work, exceed the permitted earnings threshold. This would result in overpayments in pension that have to be refunded to the Department.

The Department has confirmed that in an effort to minimise this category of arrears, it liaises constantly with DSP, to ensure that pension payments being processed are correct before they are actually effected. Further discussions were also made with DSP during 2013 in relation to the possible use of SABS software by the Treasury Pensions Department, which would enable payments to be made only if the application is genuine.

### Special Cases

Different cases relating to overpayments fall under this category. In fact, part of the balance of €4,979 related to retired Police Officers who were reinstated within the Malta Police Force during 2013, after serving their 25-year term. Overpayments resulted since the Department was only informed about the reinstatement after the Treasury Pension had been paid.

In these cases, the established procedure states that if the overpayment is up to 60% of the pension rate, it can be deducted entirely from the following pension payment. Otherwise, repayment has to be made in three instalments. However, the Department confirmed that in those instances where the pensioner claims financial hardship, the repayment method may be reconsidered.

### Ageing Analysis

	€
Amounts outstanding for over five years ( – 2008)	22,897,458
Amounts outstanding for over two but less than five years (2009 – 2011)	2,195
Amounts outstanding for over one but less than two years (2012)	18,390
Amounts outstanding for less than one year (2013)	<u>13,572</u>
<b>Total</b>	<b>22,931,615</b>

The Department did not provide an ageing analysis of the €324,393 pertaining to Pension Claims from Entities.

### Inland Revenue Department

The Inland Revenue Department (IRD) reported a gross arrears balance of €849,743,003 in its ARR for the year ended 31 December 2013. This balance represents an increase of 20% over the gross arrears of €708,638,746 reported last year.

The following is a sub-classification of the gross closing balance of arrears as reported by the Department in its ARR:

	€
a. Pre' 99 System (Up to Year of Assessment 1998)	162,903,343
b. Self-Assessment System (Post Year of Assessment 1998)	415,537,343
c. Final Settlement System (Employers)	73,595,901
d. Social Security Contributions Class 1 (Employers)	135,675,050
e. Social Security Contributions Class 2 (Self-Employed/Occupied)	<u>62,031,366</u>
<b>Total</b>	<b>849,743,003</b>

Out of this balance, the amount of €615,211,393 was considered as not collectable, thus resulting in net collectable arrears of €234,531,610. Similar to previous years, an arbitrary flat rate was used to derive the estimated uncollectable amounts, which in the case of Pre' 99 and Self-Assessment balances amounted to 77.8%. With regards to the Final Settlement System and Social Security Contributions (Class 1), the non-collectability rate stood at 70% and 54.6% respectively. On the other hand, 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 (2013)	34,067,174
Amounts outstanding for over one but less than two years (2012)	31,400,921
Amounts outstanding for over two but less than five years (2009 – 2011)	58,883,834
Amounts outstanding for over five but less than ten years (2004 – 2008)	42,521,281
Amounts outstanding for over ten but less than twenty years (1994 – 2003)	49,347,455
Amounts outstanding for over twenty years ( – 1993)	<u>18,690,148</u>
<b>Total</b>	<b>234,910,813</b>

The total of the ageing analysis differs from the net collectable arrears in ARR by €379,203. The majority of this amount relates to payments collected by IRD in connection with the Pre' 99 system collection schemes. This amount could not be set off against the balance due in any particular year, therefore it was omitted from the ageing analysis.

### Collection Efforts

The Department commented that the efforts made to collect the amounts overdue are part of an ongoing process. In fact, collection efforts can take different forms including Enforcement Statements, Demand Notices, and Court action. Taxpayers may also call at IRD offices to regularise their position, often by opting for a repayment through instalments.

Additionally, IRD has made arrangements with other Government Departments and Entities, such as the Contracts Department and Malta Enterprise, to ensure that any applications for tenders, work permits and tax credits made with them, are supported by Tax Compliance Certificates. Defaulting taxpayers would have to settle their balances, or at least enter into an instalment arrangement with IRD, before their applications can be successfully processed by these Departments and/or Entities.

### Capital Transfer Duty Department

The gross closing balance as reported by the Capital Transfer Duty (CTD) Department in its ARR ending 31 December 2013 consists of:

	€
a. Duty on Documents	24,692,430
b. Death and Donation	<u>4,624,016</u>
<b>Total</b>	<b>29,316,446</b>

Out of the €29,316,446 gross closing balance, of which €13,484,443 were reported as being under contestation, the amount of €17,486,667 was considered as not collectable, thus resulting in net collectable arrears pertaining to Duty on Documents and Death and Donation of €9,963,895 and €1,865,884 respectively.

A difference of €42,188 was noted between the opening balance reported in ARR and the respective supporting documentation. The Department confirmed that this difference resulted from a number of adjustments that were required during an update in data carried out in 2014, for the preparation of the accrual accounting reports.

### Ageing Analysis

The outstanding balances in relation to Duty on Documents, being due from individuals and private companies, can be analysed as follows:

	€
Amounts outstanding for less than one year (2013)	5,369,152
Amounts outstanding for over one but less than two years (2012)	274,843
Amounts outstanding for over two but less than five years (2009 – 2011)	855,045
Amounts outstanding for over five but less than ten years (2004 – 2008)	1,524,556
Amounts outstanding for over ten years (– 2003)	<u>1,379,629</u>
<b>Total</b>	<b>9,403,225</b>

The ageing analysis relates solely to Duty on Documents, and does not incorporate figures related to Death and Donation. It was also noted that the total of €9,403,225 does not agree to the relative net collectable arrears presented in ARR by €560,670, because of backdated amounts that were entered into the system since 1 January 2014, which resulted in changes to the total of arrears due as at end 2013.

### Amounts Under Contestation

In addition to €17 million estimated as not collectable, a further €13.4 million are amounts relating to objections made by taxpayers.

### Collection Efforts

The Collection and Legal Sections within the Department are constantly monitoring the outstanding balances and taking action as necessary. During 2013, an exercise was also undertaken by CTD to highlight those claims that will soon become statute-barred.

### 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 2013:

	€
a. VAT (1998)	906,828,666
b. VAT (1995)	14,444,648
c. Customs and Excise Tax	6,372,468
d. Eco-Contribution	7,324,113
e. Refund to Government on stocks – 1997	<u>620,381</u>
<b>Total</b>	<b>935,590,276</b>

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.

Net collectable arrears amounted to €49,233,506 after deducting a balance of €886,356,770, which is estimated as not collectable by the Department.

Whereas write-offs during the year amounted to €3,030, a total balance of €98,844,674 was reported as not due in VAT Department's ARR, representing cancellations of assessments, levies and interest, following the submission of declarations by taxpayers.

Further to a meeting called by Treasury Department on 29 April 2014, to clarify calculations of amounts reported in ARR submitted by VAT Department, the large difference between the 2012 year-end net collectable arrears of VAT (1998) (€50,956,891) and the amount actually received in 2013 (€129,801,233), was discussed.

The Department explained that the discrepancy between both figures arose since receipts in the current year (in this case 2013) were first allocated against older balances owed, irrespective of whether a particular payment was made against a current balance due. Therefore, the amount of €129,801,233, does not only relate to the collection of past arrears, but also to current dues for those cases where a taxpayer had long outstanding arrears.

The Department also confirmed that in 2014, legislation was changed whereby payments received are no longer automatically allocated against old balances. Instead, payments intended to cover a VAT Return, will be allocated to the period pertaining to that Return and not against older balances. This will effectively cause both the past arrears collected and the newly accrued arrears reported balances to decline, and hence provide a more realistic account of the amounts being paid.

During this meeting, it was also mentioned that once the remittance scheme comes to an end, it would be opportune for VAT Department to address the issue of the original substantial balance generated by the system, as this balance is mainly made up of estimated assessments and interest accrued.

When further queried by NAO to provide a more detailed analysis of the total receipts of €129,801,233, the Department suggested that after 2014, a more accurate analysis could be presented. As reported in previous years, no ageing analysis of net collectable arrears could be provided by VAT Department.

An audit on collections from Eco-Contribution revealed several shortcomings which have been reported upon separately under the respective Ministry on page 256.

### *Customs Department*

The Customs Department submitted its ARR to Treasury, however said Return was never forwarded to NAO for further testing and analysis. Further enquiries with Treasury Department revealed that an exercise on the validity of the figures presented in the Customs' ARR was currently being conducted, and up to the date of the writing of this report, the final figures could not be provided by Customs.

### *Department of Contracts*

The outstanding gross closing balance of arrears of €322,987, as reported by the Department of Contracts as at 31 December 2013, consisted of outstanding penalties and damages due by eight contractors, which are still being pursued by AG.

Total dues of €18,994 were collected during the year from two contractors, one of whom, during 2011, was served with a Garnishee Order, as well as issued a Performance Guarantee in favour of the Department.

### *Estimated Amounts Considered as Not Collectable*

Besides the amount of €59,748 owed by a foreign company, which was considered as not collectable, an additional sum of €53,498, pertaining to three contractors, was also reported under this category. One of these contractors, a company owing a balance of €8,438, was struck off the Register of Companies, thus making it highly unlikely that outstanding dues will be collected.

Notwithstanding that another contractor, owing €11,236, was served with a Judicial Letter, the Department stated that since more than five years had elapsed from the date of the Court judgment, new proceedings would have to be filed in order to issue a Garnishee Order. Given the amount of Court and legal expenses involved, a request for write-off was submitted to the pertinent authority.

With regards to the remaining balance reported as estimated as not collectable of €33,823, the Department has filed a request to the liquidator of the company in question, by means of a Judicial Letter.

## Ageing Analysis

The resulting net collectable arrears of €209,741 is analysed as follows:

	€
Amounts outstanding for less than one year (2013)	-
Amounts outstanding for over one but less than two years (2012)	-
Amounts outstanding for over two but less than five years (2009 – 2011)	172,093
Amounts outstanding for over five but less than ten years (2004 – 2008)	-
Amounts outstanding for over ten but less than fifteen years (1999 – 2003)	<u>37,648</u>
<b>Net Closing Balance</b>	<b>209,741</b>

This includes amounts owed by two contractors, totaling €126,375, which were reported as under contestation in the Department's ARR. In one case, a contractor owing €105,865, appealed the decision by COJ taken in 2011. No hearing date has yet been set for this appeal.

## Ministry for Health

The gross closing balance of €5,060,660, as at 31 December 2013, is made up of the following:

	€
a. Licences	26,071
b. Ship Sanitation	5,507
c. Pharmacy Bills MDH	24,729
d. Hospital Tests Primary Health Care	2,897
e. Hospital Fees: St. Luke's Hospital	238,234
f. Hospital Fees: MDH	1,854,959
g. Hospital Fees: Sir Paul Boffa Hospital (SPBH)	105,556
h. Sundry Bills: MDH	123,493
i. Resignations and Overpayments: MDH	211,476
j. Breach of Contract	2,278
k. European Union Countries E125	1,167,544
l. European Union Countries E127	<u>1,297,916</u>
<b>Gross Closing Balance</b>	<b>5,060,660</b>

From the gross receivable at year-end of SPBH, a total amount of €68,840 is being estimated as not collectable, leaving a net closing balance of €4,991,820, as analysed below:

	€
Amounts outstanding for less than one year (2013)	1,315,580
Amounts outstanding for over one but less than two years (2012)	784,363
Amounts outstanding for over two but less than five years (2009 – 2011)	1,882,918
Amounts outstanding for over five but less than ten years (2004 – 2008)	805,560
Amounts outstanding for over ten but less than fifteen years (1999 – 2003)	154,484
Amounts outstanding for over fifteen years (– 1998)	<u>48,915</u>
<b>Net Closing Balance</b>	<b>4,991,820</b>



### *Mater Dei Hospital*

Following a detailed review of the Return, the debtors' list and the respective supporting documentation submitted by MDH, various shortcomings and variances were noted, mainly that the foregoing documents could not be corroborated due to insufficient supporting documentation.

Although the discrepancies were communicated to the Financial Controller, amended versions were not submitted. It was stated that since the current systems are rudimentary, it will take time to provide the requested information. According to the Financial Controller, the present accounting system in the Billing and Revenue Section at MDH is being phased out. It is being envisaged that by January 2015, the new system should be running, and hopefully such discrepancies will be minimised.

### Entitlement Unit

Additionally, NAO could not corroborate the amounts of E125 and E127 claims recorded as arrears of revenue in the Return pertaining to the Entitlement Unit, with the supporting documentation provided. Subsequent to an intensive exercise carried out by the new officer in charge, assisted by an NAO official, amended versions of both the Return and debtors' list were submitted in November 2014.

According to the Director at the Entitlement Unit, in an attempt to address the shortcomings in question, it was stated that:

- a. the Entitlement Unit was restructured in the last quarter of 2013 and the current staff at the Payment Section is newly recruited. Since then, the staffing situation was stable and strengthened by the allocation of a qualified Accountant;
- b. in the absence of properly documented reconciliations, an exercise was carried out, in order to be able to provide an accurate year-end Return as much as possible; and
- c. in 2014, the new Management reassessed the situation of the system and is currently taking a number of initiatives.

### Licences

The outstanding amount of €26,071 mainly related to licences for dental clinics, covering previous years, up to the year 2000. It is understood that such fees emanate from the legislation regulating this profession. However, several dentists are refusing to pay, arguing that other professions do not have similar licences. The Financial Controller stated that collection efforts are made through reminders sent by the Superintendent of Public Health. However, this claim could not be substantiated.

*Gozo General Hospital*

In 2013, the opening balance of amounts due to the Gozo General Hospital (GGH) stood at €108,804, of which only €3,410 were collected during the year under review. On the other hand, €11,658 were registered as newly accrued amounts, resulting in a gross closing balance of €117,052. However, €53,118, i.e. 45% of this amount, is estimated as not collectable, leaving a net collectable total of €63,934 as at 31 December 2013.

Ageing of debtors can be analysed as follows:

	€
Amounts outstanding for over two but less than five years (2009 – 2011)	38,357
Amounts outstanding for over one but less than two years (2012)	13,919
Amounts outstanding for less than one year (2013)	<u>11,658</u>
<b>Net Closing Balance</b>	<b>63,934</b>

Measures were taken during the year under review to address shortcomings highlighted in previous reports, aiming at improving collection of amounts due in a timely manner. Among these are the following:

- a. Electronic Point of Sale machines were installed at GGH, and one of them is fully functional.
- b. New clerks working on a 24-hour, seven day week, were posted at the Accident and Emergency Department, to ensure that someone is available to collect payments at all times. Clerks will also be posted at the Outpatients Section and Health Centre in the very near future.

GGH will also be implementing a system whereby a patient who does not provide the European Health Card (E21) will have to pay a deposit of €100, which deposit will be forfeited if the said card is not presented within a 36-hour timeframe. GGH is also working on the installation of a program that will link the Accident and Emergency Department, Outpatients Section, the Health Centre, and the wards, to the Almoners Office. This would enable the applicable forms to be filled online, and the invoices and receipts also generated online accordingly. Controls have been included in this program to ensure that all fields are duly filled in, with proper audit trail of the respective users.

## Arrears of Revenue 2013

Ministry/Department		Gross outstanding on 31/12/2012	Collected during 2013	Written off 2013	Revisions 2013	Arrears 2013
Office of the Prime Minister	€	11,958	5,746	0	0	815
Department of Information	€	62,056	54,955	0	-50	70,851
Government Printing Press	€	521,796	117,927	0	0	258,490
Government Property Department <sup>a</sup>	€	28,253,080	6,555,470	17,116	3,841,162	7,163,994
Ministry for Tourism <sup>f</sup>	€	1,624,364	335,824	181,735	-32,169	605,042
Institute of Tourism Studies <sup>g</sup>	€	361,503	180,641	0	-1,915	44,831
Department of Local Government <sup>h</sup>	€	1,611	1,611	0	0	2,575
Ministry for Education and Employment <sup>a, g</sup>	€	506,129	69,847	0	53,293	146,906
Ministry for Sustainable Development, the Environment and Climate Change <sup>l</sup>	€	1,126,790	434,921	8,421	-2,868	879,428
Ministry for Transport and Infrastructure <sup>j</sup>	€	658,050	100,245	190,236	876	246,262
Transport Malta <sup>a, k</sup>	€	18,184,747	355,309	0	-977,574	2,626,241
Ministry for Gozo	€	248,303	8,090	0	0	13,306
Gozo Judicial Courts <sup>l</sup>	€	575,786	90,932	0	-1,236	81,712
Ministry for Social Dialogue, Consumer Affairs and Civil Liberties Industrial and Employment Relations <sup>h</sup>	€	310,979	2,498	0	0	0
Ministry for the Economy, Investment and Small Business Lotteries and Gaming Authority <sup>e</sup>	€	858,263	305,204	0	0	956,103
Malta Communications Authority <sup>j</sup>	€	327,870	248,925	0	-19,258	95,594
Television Licensing Unit <sup>e, j</sup>	€	10,430,454	26,653	935	706	5,154
Trade Services (Commerce) <sup>e</sup>	€	4,750,213	651,012	0	-468,020	164,892
Ministry for the Family and Social Solidarity Social Security Benefits <sup>g</sup>	€	16,130,271	2,408,496	70,541	-189,844	5,133,442
Elderly and Community Care (including Welfare Committee) <sup>m</sup>	€	2,179,633	21,533	0	0	978,495
Ministry for Home Affairs and National Security Armed Forces of Malta <sup>h</sup>	€	322,428	203,927	0	-21,690	631,213
Police <sup>l</sup>	€	426,667	66,039	43,443	1,775	77,110
Civil Protection <sup>l</sup>	€	20,207	13,637	0	0	12,554
Land Registry <sup>j</sup>	€	81,470	18,048	0	0	11,563
Judicial (Malta) <sup>l</sup>	€	12,416,067	1,522,931	1,074,350	-217,948	1,882,169
Attorney General <sup>l</sup>	€	6,348	7,968	0	11,125	16,560
Notary to Government <sup>e</sup>	€	72	72	0	0	1,511
Ministry for Finance <sup>e</sup>	€	50,090	33,550	0	0	8,882
Treasury (Pensions Section) <sup>e</sup>	€	23,248,632	19,549	0	0	26,925
Inland Revenue (including Tax Compliance Unit): <sup>e</sup>	€	527,738,578	172,951,997	444	-164,016,991	387,671,540
Income Tax						
Social Security Contributions: Class 1 and Class 2	€	140,494,924	55,397,821	0	-1,452,793	114,062,106
Final Settlement System	€	40,405,244	41,085,787	0	-1,040,077	75,316,521
Capital Transfer Duty: <sup>e</sup>	€	25,867,164	1,589,910	0	-6,935,068	7,350,244
Duty on Documents						
Death and Donation Duty (including Penalties)	€	4,632,912	8,922	0	0	26
V.A.T. <sup>e</sup>	€	698,502,284	133,315,598	3,030	-98,844,674	469,251,294
Customs	€	n	n	n	n	n
Contracts <sup>e</sup>	€	341,981	18,994	0	0	0
Ministry for Health Consolidated <sup>a, m</sup>	€	3,498,441	1,024,129	0	-8,487	2,594,835
Gozo General Hospital <sup>o</sup>	€	108,804	3,410	0	0	11,658
<b>TOTAL<sup>d</sup></b>	<b>€</b>	<b>1,565,286,169</b>	<b>419,258,128</b>	<b>1,590,251</b>	<b>-270,321,725</b>	<b>1,078,400,844</b>

Gross Outstanding on 31/12/2013	Gross Variation	Amounts Est. as not Collectable	Net collectable arrears as at 31/12/2013	Net collectable arrears as at 31/12/2012	Net Variation	Due from Govt. Dept. & Para. Bodies	Individual & Private Companies	Amounts collected January 2014	Balance as at 31/1/2014
7,027	-4,931	0	7,027	11,957	-4,930	0	7,027	0	7,027
77,902	15,846	0	77,902	62,056	15,846	77,902	0	26,480	51,422
662,359	140,563	0	662,359	521,797	140,562	662,290	69	0	662,359
32,685,650	4,432,570	9,458,542	23,227,108	18,794,538	4,432,570	5,997,637	17,229,471	512,664	20,714,444
1,679,678	55,314	54,365	1,625,313	1,388,264	237,049	0	1,625,313	0	1,625,313
223,778	-137,725	12,921	210,857	344,898	-134,041	199,886	10,971	12,622	198,235
2,575	964	0	2,575	1,611	964	2,575	0	710	1,865
636,481	130,352	56,389	580,092	791,936	-211,844	63,293	516,798	4,878	575,214
1,560,008	433,218	26,391	1,533,617	b	b	0	1,533,617	0	1,533,617
614,707	-43,343	58,546	556,161	b	b	273,956	282,205	4,296	551,865
19,478,105	1,293,358	334,443	19,143,662	17,850,304	1,293,358	0	19,143,662	208,545	18,935,117
253,519	5,216	28,183	225,336	220,120	5,216	76,306	149,030	0	225,336
565,330	-10,456	45,112	520,218	499,702	20,516	0	520,218	0	520,218
308,481	-2,498	195,685	112,796	115,294	-2,498	0	112,796	240	112,556
1,509,162	650,899	869,586	639,576	502,176	137,400	0	639,576	0	639,576
155,281	-172,589	0	155,281	327,870	-172,589	74,747	80,534	16,606	138,675
10,408,726	-21,728	4,258,517	6,150,209	6,199,915	-49,706	140,000	6,010,141	100	6,150,109
3,796,073	-954,140	837,585	2,958,488	4,695,842	-1,737,354	0	2,958,488	189,121	2,769,367
18,594,832	2,464,561	0	18,594,832	16,130,271	2,464,561	0	18,594,832	510,369	18,084,463
3,136,595	956,962	0	3,136,595	2,179,633	956,962	3,074,764	61,831	27,974	3,108,621
728,024	405,596	96,564	631,460	229,730	401,730	451,973	179,487	201,946	429,514
396,070	-30,597	13,995	382,075	426,667	-44,592	7,888	374,187	3,113	378,962
19,124	-1,083	6,570	12,554	13,505	-951	1,105	11,449	0	12,554
74,985	-6,485	31,997	42,988	52,940	-9,952	0	42,988	9,828	33,160
11,483,007	-933,060	144,611	11,338,396	7,359,142	3,979,254	0	11,338,396	233,824	11,104,572
26,065	19,717	569	25,496	5,779	19,717	0	25,496	2,064	23,432
1,511	1,439	0	1,511	72	1,439	1,485	26	1,242	269
25,422	-24,668	0	25,422	50,090	-24,668	12,392	13,030	12,374	13,048
23,256,008	7,376	0	23,256,008	23,248,632	7,376	23,221,843	34,165	0	23,256,008
578,440,686	50,702,108	449,987,846	128,452,840	111,987,680	16,465,160	0	128,452,840	4,845,598	123,607,242
197,706,416	57,211,492	113,706,470	83,999,946	49,129,921	34,870,025	0	83,999,946	2,339,396	81,660,550
73,595,901	33,190,657	51,517,077	22,078,824	12,121,573	9,957,251	0	22,078,824	433,996	21,644,828
24,692,430	-1,174,734	14,728,535	9,963,895	7,909,364	2,054,531	0	9,963,895	146,831	9,817,064
4,624,016	-8,896	2,758,132	1,865,884	2,718,423	-852,539	0	1,865,884	0	1,865,884
935,590,276	237,087,992	886,356,770	49,233,506	55,305,414	-6,071,908	0	49,233,506	0	49,233,506
n	n	n	n	65,586,944	n	n	n	n	n
322,987	-18,994	113,246	209,741	282,233	-72,492	0	209,741	1,729	208,012
5,060,660	1,562,219	68,840	4,991,820	3,488,295	1,503,525	2,468,240	2,523,580	2,680	4,989,140
117,052	8,248	53,118	63,934	65,852	-1,918	0	63,934	133	63,801
<b>1,952,516,909</b>	<b>387,230,740</b>	<b>1,535,820,605</b>	<b>416,696,304</b>	<b>410,620,440</b>	<b>69,573,030</b>	<b>36,808,282</b>	<b>379,887,953</b>	<b>9,749,359</b>	<b>404,946,945</b>

- a) Opening Balance 2013 does not tally with Closing Balance 2012 (*vide* comments).
- b) Net Collectable Arrears 2012 could not be determined since during 2013 this balance was split between the Ministry for Sustainable Development and Climate Change and the Ministry for Transport and Infrastructure.
- c) A difference of €68 was noted between amounts due from Government Departments and Parastatal Bodies and Individual and Private Companies, and Net Collectable Arrears. The immaterial difference arose from the Department's accounting system.
- d) Totals are incomplete in view of a) to c) above.
- e) Featured in 2012 under the Ministry of Finance, the Economy and Investment.
- f) Featured in 2012 under the Tourism and Culture Department within the Office of the Prime Minister.
- g) Featured in 2012 under the Ministry for Education, Employment and the Family.
- h) Featured in 2012 under the Office of the Prime Minister.
- i) Featured in 2012 under the Ministry for Resources and Rural Affairs.
- j) Featured in 2012 the Ministry for Infrastructure, Transport and Communications.
- k) Featured in 2012 under the Lands and Transport Directorate within the Ministry for Infrastructure, Transport and Communications.
- l) Featured in 2012 under the Ministry for Justice and Home Affairs.
- m) Featured in 2012 under the Ministry for Health, the Elderly and Community Care.
- n) 2013 ARR not submitted to NAO.
- o) Featured in 2012 under the Ministry for Gozo.



Office of the Prime Minister

# Electoral Office

## Background

The administration of the Electoral Office (EO) is the sole responsibility of the Electoral Commission (EC) as established by Article 60 of the Constitution. EC is an autonomous body and the members of the Commission are appointed by the President, acting in accordance with the advice of the Prime Minister, after consultation with the Leader of the Opposition. The Chief Electoral Commissioner (CEC), who is also the Chairman of the Commission, is the Head of EO, and is responsible for the day-to-day running of the same Office, and for the implementation of the decisions of the Commission.

A total amount of €5,825,000 was allocated to EO for the year 2013, through the Office of the Prime Minister Recurrent Vote. Out of this amount, the Commission was assigned €4,000,000 for its activities under Programmes and Initiatives, and another €450,000 for its running costs under Contributions to Government Entities.

## Audit Scope and Methodology

The main scope of the audit was to evaluate the level of existing internal controls over the procurement and payments of expenditure incurred by EO during the year 2013, in accordance with existing laws and regulations.

The audit also aimed to ascertain a prudent and judicious use of Government resources, including

an efficient administration of public funds. Particular consideration was given to payments in connection with duties carried out during the election period.

A sample of 30 transactions, amounting to €2,506,922, was selected based on materiality and frequency of expenditure. These were chosen from a number of accounts falling under Materials and Supplies, Office Services, Repair and Upkeep, Transport, Contractual and Professional Services, as well as Hospitality. The extent of controls on overtime and other allowances paid to electoral and non-electoral employees was also examined.

## Limitations on Scope of Audit

According to the Secretary to the Commission, years back EC had decided that since its meeting minutes and other documents contained sensitive information, they were deemed to be of a confidential nature, and therefore should not be open to scrutiny. The former also stated that this decision was re-confirmed in December 2000, when the Commission sought the advice of its legal advisor, who endorsed the previous decision, which decision is also supported by Article 5(4) of the Freedom of Information Act (Chapter 496), stating that the Act shall not apply to documents held by EC.

Consequently, the National Audit Office (NAO) was not given access to substantiate decisions taken by EC, to compensate various electoral and non-electoral individuals for performing election-

related duties, either by means of ‘lump sums’ or on an hourly basis. Details of such payments can be found in this write-up.

## Audit Disclaimer

Whilst analysing the remuneration paid to officers ‘on loan’ from other Government Departments, who assisted during the election process, NAO did not verify whether such individuals availed of vacation leave from their respective employments, when such service was provided during normal office hours.

## Key Issues

### *Payments approved by the Electoral Commission Board in relation to ‘Laminating, Cutting and Checking’ Exercise*

#### Background

According to the Commission, the election process “... involves many persons from the Public Service in different grades and from different entities, and certain specific requirements are usually needed for each particular election.” EC appoints those individuals who are deemed capable of performing election duties, following consultation with Political Parties, Government Departments, Police, Armed Forces of Malta and other stakeholders.

Those who are in regular employment and work after office hours were paid at overtime rates, whilst retired individuals were paid at an agreed hourly rate, which was either based on their last salary prior to retirement, or as decided and approved by EC. After the elections are concluded, EC reviews the responsibilities and duties performed by all appointed officers, and decides on an additional ‘lump sum of money’ to be paid to the latter accordingly, at times over and above overtime payment.

During the course of the audit, CEC maintained that “... the EC is not subject neither to the Public Administration Act, ... nor to the Public Contracts Regulations, under the Financial Administration & Audit Act, ... This notwithstanding, ... imposes additional responsibility on the Electoral

*Commission to act all the time with discretion and discernment, aware that public funds are involved”*. Despite this statement, NAO noted that various recommendations put forward following an audit on Personal Emoluments, published in the Report by the Auditor General for the year 2006, were not implemented, and certain observations highlighted in the said Report still prevail. These will be outlined in more detail further on in this write-up.

In preparation for the General and Local Council Elections, electoral and other ‘on loan’ staff performed a ‘Laminating, Cutting and Checking’ exercise of the voting documents. This was spread over six days, *i.e.* between 17 and 22 January 2013.

In order to complete this task, two shifts were required, which consisted of a morning shift and an afternoon/evening shift of six hours and a half each. EC decided to grant a fixed amount of €900 to each officer who participated in this exercise, consisting of an average of €129 for a six and a half-hour shift, and double this amount, *i.e.* €258, for duties performed on Sunday shifts. The total amount paid by EC for this task totalled €65,700.

#### Extra Payments paid to Officials for performing Election Duties during Office Hours

Similar to that reported in the 2006 Annual Audit Report, a total of 31 electoral and seven non-electoral employees who worked the morning shift referred to above, irrespective of their grade, were remunerated an aggregate amount of €32,914 in addition to their normal salary, even though work was carried out during their normal office hours. This constitutes an excessive use of public funds. It also transpired that nine of the Electoral Officers who worked during the said morning shift, were also on duty for the afternoon/evening shift, and were thus each compensated double the fixed sum.

#### Hourly Rate paid exceeding Overtime Rate

The above also meant that officers who worked outside office hours, *i.e.* during the afternoon/evening shift, were paid an average hourly rate of €19.78, when the lump sum of €900 was calculated on an hourly basis, which rate is well above the maximum overtime pay of Salary Scale 10, as stipulated in Section 3.2.1.3 of the Public



Service Management Code (PSMC). According to the Collective Agreement for Employees in the Public Service, the equivalent of this maximum overtime rate payable during 2013, was capped at €13.78 per hour. This situation further contributes to overspending of Government funds.

### Minor Staff remunerated at *par* with Other Officers

The list of personnel taking part in the laminating exercise, as compiled by the Director Operations, showed that nine<sup>1</sup> individuals did not perform duties directly related to the exercise itself, but carried out reception, technical and cleaning duties. These individuals, including Minor Staff, were remunerated with the same amount paid to the other officers, *i.e.* €900 for each shift over the six-day period.

Moreover, NAO observed that on three separate occasions when Casual Elections were held, an aggregate amount of €860 was approved as payment to Minor Staff whose duties in connection with the elections were not specified.

### Inconsistencies in the use of Officers acting as Reserves

Three individuals acted as Reserves throughout the morning shift of the laminating exercise and were paid the full amount. However, in contrast, only one employee was engaged as a reserve for the afternoon/evening shift. Without prejudice as to the necessity for the Reserves, a total of three for the first shift is considered excessive. The aggregate amount paid to these four officers totalled €3,600.

### Minimum Rest Period not respected

In the case of employees who worked both shifts, an adequate minimum rest period of 11 hours, as stipulated by the Organisation of Working Time Regulations, was not respected. This states that *“Every worker shall be entitled to a minimum daily rest period of eleven consecutive hours per 24-hour period during which the worker performs work for his employer”*. In fact, when taking into consideration the hours worked by the officers in question, theoretically this resulted in consecutive

rest of 10.5 hours. Non-compliance with standing regulations may put the Government at risk in the case of a dispute.

### *Other ‘Lump Sums’ paid during Normal Office Hours*

In addition to the ‘lump sums’ paid for the ‘Laminating, Cutting and Checking’ exercise, this Office also traced additional amounts, totalling €16,708, approved by EC and again paid to electoral staff, for participating in election-related duties, also performed during normal office hours. Such instances lead to excessive expenditure paid out of the public funds.

### *Personal Payments to Cleaning Contractor Employees not covered by existing Letter of Acceptance*

By means of an Acceptance Letter, EO engaged a private company to provide cleaning services for a period of one year, up to June 2013. This correspondence stipulated that the latter was to make available two cleaners on week days, and another cleaner on Saturdays, excluding public holidays. The Acceptance Letter did not specify any chargeable rates in connection to extra hours performed.

Timesheets revealed that the two employees assigned by the service provider to this effect were also involved in the previously mentioned laminating exercise. These two employees were privately compensated by EC, an additional amount totalling €1,543, for providing cleaning services during the period in question. At the same time, EC also effected the normal payment to the company, covering the existing agreed services during the said exercise.

### *Inadequate Working Schedules maintained to substantiate Extra Payments*

In support of various ‘lump sums’, totalling €33,670, approved by the Commission for work performed by electoral officers, no proper timing schedules were documented. As a result, for nine days during which election-related activities were carried out, NAO could not verify the number of hours worked by each individual, since attendance

<sup>1</sup> Six of these individuals worked both shifts during the ‘Laminating, Cutting and Checking’ exercise.

sheets were also not kept to substantiate the amounts paid. Furthermore, in another two instances, CEC approved payments at an aggregate of €14,352, for which not even the dates or duration were recorded, thus hindering audit trail.

The only attendance sheets provided for duties carried out by the electoral staff, in connection with the General and Local Council Elections, as well as the Casual Elections, were those pertaining to the laminating exercise. However, although officers signed-in daily for the duration of the exercise, it was noted that the time of arrival and departure in respect of both morning and afternoon shifts, were not registered. Nonetheless, these attendance sheets were endorsed by the Director Operations to proceed for payment.

### *No evidence substantiating Payment for Disturbance Allowance*

On 18 March 2013, CEC approved the total payment of €5,295 as disturbance allowance to individuals who were involved in the distribution of voting documents of the General and Local Council Elections, between 4 and 7 March 2013. Subsequently, through correspondence dated 29 April 2013, CEC and the Director Operations re-considered to grant “... a reduced distribution allowance ...” of €100 each to another 12 employees, also deciding that, “... in cases where the employee did not work after normal office hours, or did so to a small extent, the allowance is further reduced.” It later transpired that three of these officers received an amount of €80, €78 and €50 respectively to this effect, in aggregate disbursing an additional amount of €1,108.

In the circumstances, NAO could not justify the “... reduced disturbance allowance ...” compensated to these employees from public funds, nearly two months after the event, since their actual involvement in the distribution of votes is unclear.

### *Overtime carried out at the Valletta Electoral Office, Naxxar Counting Hall and Qormi Stores*

#### *Considerable Amount of Overtime performed by Electoral Staff*

Whilst reviewing a sample of salaries paid to 14 electoral employees, it transpired that total overtime earned by the latter averaged approximately 53% of their basic pay, in aggregate totalling €118,050. The highest amounts paid for overtime performed, were those during the period when the public service work the winter schedule, *i.e.* January to May, as well as between October and December 2013. From the sample selected, five of these employees performed overtime every month throughout the year, earning a collective amount of €61,089. Two of the said officers in the grade of Principal and Assistant Principal collectively earned a total of €35,438 in nearly equal amounts, representing an average of 90% of their basic pay. Of this total, an amount of €18,658 was paid in connection with shredding and maintenance work carried out at the Qormi Stores, covering a total average of 39 hours per week being worked in overtime by both officers. The substantial amount of overtime approved and paid to electoral officers may be resulting from a poor control environment due to lack of scrutiny by Management in this area.

#### *Non-compliance with Attendance Verification Systems’ Policy and Guidelines*

NAO acknowledges that at the Valletta Office, clocking devices have been implemented and used to record attendances during normal office hours. However, testing revealed that during 2013, employees did not make use of such devices to record actual overtime performed on location, with the risk that officers intentionally record incorrect clocking to overstate their claim for overtime. In

the absence of similar devices, manual attendance sheets were also used at the Naxxar Counting Hall and Qormi Stores, by both electoral and non-electoral staff.

### Disturbance Allowance over and above Overtime Payments

As already mentioned, a disturbance allowance was paid to employees who were involved in the distribution of the voting documents. This involved 40 officials who collectively received the amount of €4,435, and who also received payment for overtime performed during the same period. Another two officials were not financially compensated for overtime, but were collectively granted 48 hours time-off *in lieu*.

### Inconsistencies in Overtime

The Report by the Auditor General for the financial year 2006 highlighted the issue of an inconsistent internal policy with regards to overtime payments. This still prevails. Whilst in some cases, overtime claimed was foregone and instead substituted by ‘lump sums’, in other instances, EC decided to pay an extra allowance over and above overtime claimed, as in the case of the disturbance allowance already mentioned under the previous observation. This may result in unnecessary costs.

### Amounts paid to Senior Officer

A senior officer with EO, who actively participated in the elections, received various payments at an aggregate of €4,640. These payments covered work performed during, as well as after, normal office hours. This practice is considered to contradict what is specified in the relative section of PSMC, which states that “*Overtime pay is not allowed to officers above salary scale 7*”.

### Source of Hourly Rate paid to Other Personnel engaged at Naxxar Counting Hall not validated

The EC Board appoints other individuals to perform duties at the Naxxar Counting Hall which, during 2013, reached a group of at least 37 officers, consisting of public service officials and retirees.

It transpired that the global sum paid to these individuals working at the Counting Hall during the election period amounted to €222,026. Three of these individuals who acted as group leaders, were paid €16 per hour, while the remaining officers were paid a rate of €10. No evidence of EC decisions substantiating these rates was provided, since related decisions, as noted under ‘Limitations on Scope of Audit’, are not available for scrutiny.

The audit revealed that the three group leaders received payments for services rendered, totalling €52,246, which also included three extra payments of €2,330 each, in addition to the hourly rate.

Moreover, it transpired that during the year under review, one of the group leaders, held the position of a Director within the Public Service, which position also falls under Salary Scale 4. Officers in this grade are not normally entitled to overtime payments. However, as explained under ‘Audit Disclaimer’, NAO did not verify whether vacation leave was availed of by the officer in question while rendering services to EC. The lack of transparency in remunerating individuals who assist during the election process, is of concern. NAO reiterates that such remuneration to officers above Scale 7 contradicts PSMC regulations.

## Control Issues

### Procurement by Direct Order

Although EC verbally communicated that it strives for best practice in procuring goods and services, it was noted that no quotations were obtained for purchases amounting to €314,673, which consisted of 10 sampled Payment Vouchers (PVs) out of a total of 30 examined, pertaining to nine different suppliers.

It also transpired that during the year under review, seven of the above suppliers provided other goods and services to EC, at an additional aggregate value of €233,106. CEC maintained that procurement is effected from suppliers of trust and accepted by political parties. This is still considered as unfair competition and unequal opportunities to all

interested parties willing to provide the required goods and services, with the possibility of losing more advantageous offers.

### ***Imprudent Expenditure on Dinners***

- a. A one-time payment of €4,251 was made to a company for various dinners at a local restaurant, during the General and Local Council elections. This transaction was made up of nine bills, consisting of €3,451 for food and drinks, including €60 for tips, and an additional charge of €800. This latter amount pertained to ‘stand-by time’ on 8 and 9 March 2013, when although booked, no one showed up for dinner. In response to audit enquiries, it was stated that *“Regretfully, the pressure of work did not allow the meals to be taken up”*. To this effect, NAO also noted that six bills out of the nine dinners attended, were less than the €400 charged for each of the evenings when the booking was not availed of.
- b. It was observed that the total of the said bill comprised at least an amount of €527<sup>2</sup> which was paid for liquors and wine consumed during these meals. NAO opines that this type of expenditure constitutes an imprudent use of the taxpayers’ money.
- c. The copies of chits provided lacked several details, such as the number of persons and dates attended, which hindered the verification process of the payments in question. Notwithstanding, these bills were still authorised for payment by the Commission.

### ***Lack of substantiating evidence for Meals provided***

An amount of €34,187 was paid to the Police Department by means of a Transfer Schedule of Payment on 17 April 2013, in relation to meals served to police personnel while performing duties during the General and Local Council Elections in Malta and Gozo. Two suppliers provided these meals; one is situated at the Police General

Headquarters in Floriana, whose bill totalled €33,564, and another is located in Gozo at a cost of €623.

Testing revealed that a detailed breakdown to support the amount of €33,564, invoiced by the canteen of the Police General Headquarters, was not available. Upon enquiry, a scanned copy of the fiscal receipts was obtained by EO from the Police Department. However, details of the meals provided by the canteen, including the number of police officers availing themselves of this service, were not provided.

Moreover, since no formal arrangements with the Police Department were traced, NAO requested any information leading to the decision that meals were to be borne out of EC Vote. In this regard, it was commented that EC *“... directly procures such items in order that charges made by Police do not escalate”*. However, cost effectiveness could not be verified since the cost per person for each meal could not be identified, and no quotations from other food suppliers were traced for comparison purposes. The lack of supporting documentation further indicates that no controls are in place to ensure that EC was only charged for meals consumed. This also implies that no checking was carried out prior to effecting payment.

### ***Non-compliance with Fiscal Regulations***

A Multi-Payment, amounting to €44,678, was issued in favour of an individual in connection with the production of braille templates for General and Local Council Elections, which service was procured by direct order. It transpired that the invoice presented by the service provider did not disclose any Value Added Tax (VAT) number, and no fiscal receipt was issued by same. Since the supply exceeded the threshold of €7,000 established through Legal Notice (LN) 524 of 2010 (Value Added Tax (Exemption from Registration) Regulations), the service provider was obliged to register for VAT. To this effect, the latter ought to have been processed as a Vendor, and not through the Multi-Payment function, thus weakening certain controls over creditors.

<sup>2</sup> This amount is not exhaustive, since details on the photocopied chits provided were not always clear.

### ***No Proper Record Keeping of Inventory Items purchased***

Control over inventory items is weak, especially where such items are handed over to other parties for usage and/or storage purposes. Unless proper records are regularly updated, one may easily lose control over Government-owned property. The following shortcomings refer:

- a. NAO verified two PVs to different suppliers, amounting to €17,429 and €98,570 respectively. The former amount related to the ‘Electoral office setup’ at Malta College of Arts, Science and Technology, Saint Vincent De Paul Residence and Mater Dei Hospital, whilst the latter expenditure of €98,570 pertained to the refurbishing of the Naxxar Counting Hall.

Auditors enquired about the record keeping of these items, as well as their respective location after the election process is concluded. In the case of items procured for the refurbishing of the Naxxar Counting Hall, CEC commented that such items are fixed on the premises and are being surveyed by Police personnel. On the other hand, regarding the items procured for the electoral set-up in the three different locations, CEC stated that certain property items are stored at one of the supplier’s premises on Commission’s request, for use in subsequent similar occasions. However, none of these items were traced to the Inventory Ledger.

Furthermore, it was noted that the setting up of the Naxxar Counting Hall included works carried out on the premises of the Armed Forces of Malta and Police Quarters, including labour and material for horse stables, which in total amounted to €13,401. Due to the fact that no other details were available, NAO could not ascertain if these works were related to inventory or otherwise.

- b. During the verification of the sampled PVs, an invoice was traced for the acquisition of a canopy heater. The Commission stated that, *“Although the heater is still the Commission’s property, it has been handed*

*over to the Police Department for use since, otherwise, there would be no real value-for-money”*. However, it was neither traced in the Inventory Ledger, nor was a Transfer Note raised to this effect.

- c. Testing of another three PVs in the audit sample, amounting to €14,822, and pertaining to inventory items located at EO, revealed that at the time of audit, Inventory Room Lists were not updated to include such additions. The officer in charge of inventory verbally upheld this observation, stating that following the shift of offices from another location, Inventory Room Lists were still in the process of being updated.

### ***Lack of Segregation of Duties***

An officer at the Procurement Section has a fundamental role in the setting-up of various locations during the elections, including necessary arrangements with related suppliers, up to the Local Purchase Order phase of the procurement process. In fact, being an authorised signatory, this Officer is also responsible for the control of departmental expenditure, and is the sole officer in charge of inventory at EO. Moreover, the latter performs various duties at Qormi Stores throughout the year.

Due to lack of segregation of duties, effective internal controls are very limited. The fact that the majority of the procurement process is under the responsibility of one person, may be a contributory factor to a previous finding highlighted in this report, where quotations for a considerable amount of purchases were not sought.

### ***Misallocation of Expenditure***

Testing showed that ‘lump sum’ payments approved by EC, with an aggregate value of €99,475, which were paid to electoral staff for performing election duties, both during and after normal office hours, were erroneously charged as overtime under Permanent Staff – Overtime in the Departmental Accounting System. Similarly, payments to other personnel engaged at the Naxxar Counting Hall, amounting to €222,026, were also charged as overtime under Temporary Staff - Overtime.

## Recommendations

### Key Issues

#### Payments approved by the Electoral Commission Board in relation to ‘Laminating, Cutting and Checking’ Exercise

NAO is of the opinion that Management should be concerned about the considerable amounts paid to the respective individuals, who performed election duties during their normal office hours. As civil servants, electoral staff are expected to be remunerated for extra hours performed at the applicable overtime rate, according to their respective pay point and scale. In addition, EC is to ensure compliance with Organisation of Working Time Regulations.

EC is encouraged to draw up a strategic work plan prior to such large-scale exercises, clearly indicating the duties for each employee and the necessity of any reserves. These plans will facilitate the identification of any anomalies at planning stage and minimise related expenses from public funds.

#### Other ‘Lump Sums’ paid during Normal Office Hours

NAO reiterates that Management ought to be more apprehensive about the substantial amounts paid extra, to employees who performed election duties during their normal office hours.

#### Personal Payments to Cleaning Contractor Employees not covered by existing Letter of Acceptance

If EO requires cleaning services during election preparations, terms and conditions in this regard should be clearly communicated with the service provider, and eventually stipulated in a contract agreement. The required services are to be procured in a transparent manner to avoid unnecessary costs at the taxpayers’ expense.

#### Inadequate Working Schedules maintained to substantiate Extra Payments

Management is to ensure that all necessary details, such as timing schedules, as well as a brief description of duties performed, are clearly provided in order to enable a proper audit trail, and to substantiate the payments that are forwarded for approval.

#### No evidence substantiating Payment for Disturbance Allowance

Besides the recommendations highlighted under previous observations, NAO reiterates that EO employees are expected to be invariably remunerated according to the prevailing Collective Agreement for Employees in the Public Service.

#### Overtime carried out at the Valletta Electoral Office, Naxxar Counting Hall and Qormi Stores

Management is to consider other more cost-effective ways in carrying out duties related to the elections, bearing in mind that, as required by PSMC, overtime work should be resorted to only in exceptional circumstances. In particular, this Office questions the value added obtained from the considerable amount of regular overtime performed on ‘shredding and maintenance’ at Qormi Stores. To this effect, periodic reviews of overtime work should be made with the aim of changing or adapting work patterns, so as to economise on overtime and increase productivity by other means.

Full use of the automated system should be made to enable maintenance of efficient records for overtime, eliminate manual record keeping on attendancesheets,andsimplifypayrollcalculations, besides dealing with the risk of abuse. This also applies for overtime performed outside the office premises, whereby Management is encouraged to immediately introduce appropriate devices for such workers, as stipulated in the Attendance Verification Systems Policy and Guidelines issued by the HR Systems and Data Management Department in 2009. These specify that “When

*attendances of every person whose name appears on the department's manual Attendance Sheets are captured electronically, the function of the signed forms is no longer valid".* Portable devices can be utilised, and be fully integrated into the central system.

Whilst emphasising that work performed outside office hours is expected to be remunerated according to PSMC, Management is to ensure that overtime claims are accurate, by implementing a common policy that is applied consistently and without exceptions.

### Amounts paid to Senior Officer

It is acknowledged that Senior Management plays a key role during elections. However, EC is to ensure that remuneration for higher grades is in accordance to Section 15 of the Collective Agreement for Employees in the Public Service.

### Source of Hourly Rate paid to Other Personnel engaged at Naxxar Counting Hall not validated

Notwithstanding the autonomous structure of EC, best practice necessitates that engagements are formalised by means of a contract for service, with clearly defined job responsibilities. The Commission is also to ascertain that PSMC regulations are followed when remunerating officers holding senior positions within the Public Service. Furthermore, public officers are expected to avail themselves of vacation leave to perform duties in other Government entities in respect of which they receive additional remuneration.

### Control Issues

#### Procurement by Direct Order

Although EC is not listed as a Contracting Authority for the purposes of the Public Procurement Regulations, it is recommended that, as much as possible, in order to ensure transparency over procurement, it adheres to standing regulations.

### Imprudent Expenditure on Dinners

EC is to strive to avoid any unnecessary costs and extravagance in the use of public resources.

### Lack of substantiating evidence for Meals provided

As already suggested by this Office in the 2006 audit, appropriate measures have to be taken to enable more transparency in the service being provided. Any decisions taken, including the possibility of issuing an expression of interest, are to be made during the planning phase of the elections, with the main aim of utilising public funds in the most efficient way, whilst providing equal opportunity to all interested parties.

### Non-compliance with Fiscal Regulations

Management should make every effort to ensure compliance by suppliers, to abide by their fiscal obligations, through the issue of the relative fiscal receipt.

### No Proper Record Keeping of Inventory Items purchased

Given that the lease contract for the Naxxar Counting Hall is only valid up to November 2014, the Commission is expected to compile detailed records of its inventory items located there, to exercise proper control on such items, especially since the premises in Naxxar may no longer be available after the contract expires.

Furthermore, considering the substantial amounts involved in the setting up of voting locations, proper control on items purchased can only be exercised through an adequate inventory database, to minimise the possibility of theft, and safeguard the Commission's interests. It is therefore being emphasised that, since the responsibility of best practice during the procurement process lies ultimately with EC, the latter is to ensure transparency throughout the whole procurement process.

As per MF Circular No. 14/99, a list of all inventory items is to be maintained by the Officer in charge of inventory, in respect of each room, section, stores, or any other outstation. Likewise, Room Lists are to be kept and updated accordingly.

### Lack of Segregation of Duties

While appreciating the complex process of the elections, EO is encouraged to step up internal controls and address the issue of lack of segregation of duties. This will ensure a more transparent procurement process especially with regards to the preparation of off-site locations prior to elections.

### Misallocation of Expenditure

Since it is clear that payments decided upon and approved by EC to electoral and non-electoral staff are not related to actual overtime, such payments are expected to be charged under allowances.

## Management Comments

An exit meeting was held at NAO on 24 June 2014, during which Management's written comments were submitted. Apart from the final observation concerning 'Misallocation of Expenditure', EO contested the highlighted weaknesses in this report, on the basis that the tasks referred to were mostly performed on behalf of EC, and are considered to be of an extraordinary nature, *i.e.* not forming part of the routine administrative, financial and operational duties of EO. To this effect, Management stated that an agreement was reached with the Inland Revenue Department, establishing a 15% withholding tax treatment on non-overtime payments for work specifically related to election processes. Such functions should be of an extraordinary nature, consisting of one-off and non-routine work.

A summary of other comments provided are listed hereafter:

### *'Laminating, Cutting and Checking' Exercise*

- a. Management reiterated that payment was given for a service which was unrelated to the normal duties of the staff involved.

- b. The EO contested the fact that the hourly rate paid during this exercise exceeded the overtime rate, on the basis that since the work involved did not constitute overtime, no such comparison ought to be made with the Collective Agreement for Employees in the Public Service. However, EO expressed its concern on the considerable expense in holding elections with voting documents, and looks forward to the day when these documents are rendered obsolete. To this effect, Management is also considering whether in the future, preparation of voting documents could be outsourced, or substituted with the use of 'e-ID' cards. Until all stakeholders agree to this drastic change in the voting process, the conventional voting document will continue to be used.

- c. The EO insisted that the contribution of minor staff during the laminating exercise was as vital as other work, and therefore the latter received the same remuneration without distinction.

- d. With regards to the inconsistent use of officers acting as Reserves, Management maintained that although listed as such, these persons worked as hard in the operations as others.

- e. As to the Working Time Regulations that were not respected, it was stated that the laminating exercise had to be done within a specified time-frame, or else the election process could have been negatively affected.

### *Payments to Cleaning Contractor Employees*

The EO insisted that the work involved during elections time is outside the scope of the contract between the contractor and the former, such that the two cleaners engaged were remunerated proportionately for the hours carried out, in addition to their normal cleaning functions which were also carried out. It was again remarked that during the laminating exercise, no officer is paid according to one's grade, scale or normal working rate per hour, but at a fixed sum determined by EC.



### *Inadequate Working Schedules*

Management commented that remuneration for election-related tasks, in most cases, is linked to work performed within specified deadlines, rather than the actual time taken to perform such duties. It was claimed that all remunerated staff worked their quote fully and diligently.

### *Disturbance Allowance*

Regarding the compensation of the ‘reduced disturbance allowance’ to a number of employees, EO reiterated that the allowance covered the “... *inordinate amount of work* ...” that still needed to be carried out within the Office, while the rest of the employees were distributing the voting documents.

### *Considerable Amount of Overtime*

Management commented that apart from the publication of the Electoral Registers, the Office experienced “... *several drastic variations in the collection of data regarding ID cards and electoral registers* ...”, besides the relocation of its offices. This necessitated extra overtime due to backlogs, whilst also considering that a General Election was held during the year. With regards to shredding and maintenance works at Qormi Stores, MaltaPost p.l.c. has been commissioned to destroy and dispose of large masses of sensitive documents at one go, *in lieu* of the ongoing overtime performed by EO personnel.

### *Non-compliance with Attendance Verification Systems’ Policy and Guidelines*

EO claimed that the current palm reader, which was installed back in 2006, requires manual printing and checking, and is unsuitable to register overtime. Requests to change the system have been repeatedly refused by the Office of the Prime Minister (OPM). Management is again communicating with OPM, in a bid to procure an enhanced palm reader for proper logging and reporting of attendance, both during normal office hours and overtime work.

### *Inconsistencies in Overtime*

Management stated that EC has been consistent over the years in deciding which major exercises

merit the granting of remuneration. Work is remunerated according to PSMC whenever tasks consist of normal duties. However, several electoral processes do not fall under this category, and hence the remuneration of ‘lump sums’.

### *Amounts paid to Senior Officer*

EC remunerated this officer for performing considerable extra hours after normal office hours, in relation to extraordinary tasks within specified time limits, which are not considered as overtime.

### *Source of Hourly Rate paid to Other Personnel*

Management confirmed that steps are being taken to engage these individuals on a part-time basis with EC, for a specific number of weeks. With regards to other Government staff, additional compensation is paid for tasks which are completely unrelated to the officers’ job description.

### *Control Issues*

- a. Under tense election circumstances, EO cannot risk for the sake of transparency, non-delivery or bad services by newcomers; thus opt for procurement by direct order.
- b. Concerning the imprudent costs on dinners, Management stated that the outlet concerned is the only one in the vicinity of the Naxxar Counting Hall, and various EC officials require such dining facilities, even though at times, dinners booked were missed, since they were precluded from leaving the Hall.
- c. In respect of meals provided to the Police Force, EC confirmed that it has no other means for verifying payments requested by the former. Thus, it accepts the Commissioner of Police certification.
- d. As to the improper record of inventory items purchased, EO stated that the amounts indicated for work carried out at various locations do not refer solely to inventory items, but also the services in connection with these items. The ‘fixed’ installations within the Counting Hall, quarters dedicated to EC, the media and political parties, as well as to the Armed Forces and the Police, have been retained in place.

- e. Management emphasised that with respect to the mentioned lack of segregation of duties, ultimately CEC approved all procured items.

## Conclusion

Following the exit meeting, further correspondence was received, stating that internal evaluations will be conducted to introduce cost-cutting measures in accordance with Financial Regulations. It was agreed that past work practices need to be revised in order to create new work processes that are more efficient and cost-effective. Another initiative which was recently introduced, consisted of the commissioning of an operations review of the EO by the Management Efficiency Unit, which will also include the counting process in its remit.

EO is also planning to issue a formal letter of appointment, accompanied by an adjoining detailed agreement, for every individual recruit. Each assignment will be for a specific period and task, and will apply to both Counting Hall staff, as well as to EO employees performing duties during the elections period. This procedure will eliminate the need to engage staff on overtime, for one-off election-related duties. Such appointments will be target-oriented and not strictly remunerated against the actual hours worked.

Another planned development is the creation of a post of Elections Manager, to replace the existing part-time managerial structure that has been in place for several years. A capacity building exercise will be undertaken in order to improve efficiency within the EO.





Ministry of Foreign Affairs

# Head Office

## Operational and Maintenance Expenses

### Background

The budget allocation to cover Operational and Maintenance Expenses at the Ministry for Foreign Affairs (MFA) for financial year 2013 was €8,556,000. Of this amount, a total of €4,486,700 was allocated to the Head Office (HO). The actual expenditure incurred by the latter during the year under review stood at €4,387,879.

The main costs under this category consist primarily of contributions payable for affiliation with international organisations (44.6%) and travelling abroad on official duty (25%). Local visits by foreign dignitaries also absorb a considerable amount spread over various line items, such as hospitality and transport. Funds could also be utilised for expenses incurred by Missions abroad on extraordinary items.

### Audit Scope and Methodology

The principal aim of the audit was to ascertain the validity of Operational and Maintenance expenses incurred. It was also established whether procedures adopted for procurement of goods and services, as well as the management of contract agreements, was adequate and in compliance with the Public Procurement Regulations (PPR) S.L. 174.04, and any other relevant legislations, policies and procedures.

Based on information gathered, an outline systems overview was prepared, summarising areas of

concern and other potential risks within the current system. A sample of 29 transactions, based mainly on materiality, but also taking into consideration the nature of the expense, was selected for testing. The sampled transactions, with a value of €717,315 amounted to approximately 16% of the total expenditure incurred by HO during the period reviewed.

### Audit Disclaimer

In view of limitations encountered during the audit, testing was neither comprehensive nor exhaustive on internal statistical data provided by MFA, concerning total periodic amounts disbursed for the procurement of various items under review. This data was not tested and, where applicable, was quoted as given. In view of the technical nature of the sampled project and the rudimentary receipts provided, it was not possible to reconcile the amount paid to the organisation financed by MFA, to receipts submitted in respect of the Official Development Assistance project grant.

### Limitation on Scope of Audit

The file indicated by MFA, concerning the procurement of security paper for use by the Department of Citizenship and Expatriate Affairs (DCEA), could not be traced.

Consequently, detailed review of required specifications and criteria, documentation relevant

to the selection process, respective approvals, related correspondence, Letter of Acceptance (LA) and contractual agreement, if any, could not be performed by the National Audit Office (NAO). Only the relevant Local Purchase Order, invoice, Payment Voucher and the Value Added Tax receipt were traced and subject for examination.

According to MFA, in line with Article 17 of PPR, these regulations are not applicable for the purchase of security paper; thus procurement was made by direct order. A total of €14,000 was paid to the supplier to this effect during 2013.

## Key Issues

### Clerical Services

#### Services not procured by a Departmental Call for Tenders

- a. Total expenditure eventually disbursed by MFA on clerical services since 2012, up to time of audit (August 2014), amounted to €51,054, of which €36,508 were incurred during 2013. The amount involved required a departmental call for tenders, or a call for quotations published in the Government Gazette, but this service was procured from the open market, from two distinct service providers, charging different rates. The first one started rendering its services to DCEA on 27 August 2012 at €10.50 per hour, and the second one, likewise to DCEA, as from 20 November 2012 at €9.44 per hour.
- b. In spite of the lower rates available to it, MFA chose to extend the agreement with the original contractor, through a direct order approved by the Ministry for Finance (MFIN) on 29 April 2013.
- c. MFA did not provide evidence that the Office of the Prime Minister endorsed such engagement in line with standing regulations.
- d. The second agreement was still being utilised as at time of audit (June 2014), despite the fact that it had expired for over

six months, with clerical services now being utilised by the Ministry itself, rather than DCEA.

#### No Contract of Service in place

A contract of service was never drawn up between MFA and the second service provider rendering services for a period of six months, or up to the budget limit of €6,000, whichever was the earliest. Only a notification email and an official LA were issued by MFA.

Furthermore, with the exception of the applicable rate per hour, various details pertinent to such agreement were excluded from the LA. These omissions included the starting date, the duration of the agreement, the overtime rate payable, the maximum budget limit allowed for this contract, and the number of clerks being engaged.

#### Shortcomings in Timesheet Records

Manually filled-in timesheets that were evaluated, pertained to nine temporary officers hired from one contractor. These covered services for the months of February and March 2013 at DCEA. It transpired that all the 20 timesheets examined were not endorsed by an MFA officer, certifying the correctness of the hours logged by the respective employees.

## Control Issues

### Hire of Chauffeur Driven Cars

#### Variation on Contract – Hire of Additional Type of Vehicle excluded from the Agreement

An ‘Ambassadorial’ type car, at the rate of €41.22 per hour, was included in the contractor’s bid for tender, but on the recommendation of the Evaluation Board, was excluded from both LA and the agreement. The latter had concluded that another ‘Ambassadorial’ type car, which was also quoted in the bid but at the cheaper rate of €17.85 per hour “... falls under the requisites”, and was thus selected instead.

However, a request by the Director Protocol and Consular Services to cover the hire of chauffeur driven ‘Ministerial’ type car, addressed to the then Acting Permanent Secretary, incorrectly claimed that this had been left out “... *inadvertently* ...”, and that the need for such car was only felt during implementation.

Given this misleading statement, the respective approval was granted. Total expenditure incurred on this type of vehicle up to date of audit (June 2014) was €3,214.

#### Renewal of Performance Guarantee not available

The contractor, as required by Article 6 of the contract for chauffeur driven cars, submitted a bank guarantee with a value of €12,000, covering the first year of service.

However, a renewal of this guarantee, to cover the second year of the contract from 24 July 2013 onwards, was not available.

#### Limitations in Records covering Trips performed

Examination of manual records provided by MFA, supporting the transfers by hired chauffeur driven cars, revealed various shortcomings. Vouchers evaluated covered 391 hours accumulated over 78 instances, during the two sampled months of June and November 2013.

The main shortcomings identified are summarised as follows:

- Voucher numbers were not pre-printed but manually filled-in along with all the remaining details, making it difficult to verify the presence and completeness of an audit trail.
- Details of the type of vehicle being used were not recorded, even though these are relevant for the verification of invoices due to the different rate payable for the service provided. Moreover, the documents in use did not even include a space where this important detail can be filled-in.
- The name and position of the officer confirming and approving the hire and the

respective date was not recorded; only the signature was logged.

#### Official Development Assistance

##### Voluntary Organisation receiving Financial Assistance when not meeting all the required conditions

According to the Office of the Commissioner for Voluntary Organisations, as at audit date (June 2014), one of the organisations had not yet submitted the annual returns for year ending 2012, as required by Legal Notice 379 of 2012 – ‘Voluntary Organisations (Annual Returns and Annual Accounts) Regulations’. The last related accounts received by the Commissioner covered year ending 2011.

To this effect, the Commissioner was of the opinion that the organisation in question “... *is not entitled at this stage for the Government funds and it should be withheld* ...”.

As MFA does not confirm with the Commissioner whether the Voluntary Organisation was in line with the requirements, the entity in question was still advanced the amount of €15,000.

#### Awarding of Overseas Scholarships

##### Uncertain Job Opportunities after completion of funded Scholarships

Notwithstanding the expenditure of €70,176 incurred and the conditions of the respective undertaking, no evidence was traced in file to show that, prior to the granting of the scholarships, any enquiries or verifications were made by MFA, on whether relevant job vacancies or opportunities were available internally, or within Government, to engage the students upon successfully completing their sponsored studies.

The Director Protocol and Consular Services maintained that it is not the Directorate’s “... *remit to say whether any vacancies exist* ...” or “... *whether successful students have been offered employment* ...”.

## Limitations of the Endorsed Form of Undertaking

The form of undertaking, endorsed by the students prior to commencing the scholarship, does not clearly specify that all course fees and related expenses have to be refunded by the individual, if the scholarship is not completed or is abandoned, or if any offers for employment with Government within the stipulated period are refused.

By way of example, two sampled forms of undertakings reviewed, only bind the scholarship holders to pay a penalty of €4,659 each, if they fail to comply fully with their obligations as per undertaking. This means that in the event of default, MFA can only recuperate a maximum of €9,318, *i.e.* approximately 13% of the original €70,176 outlay on the two scholarships in question.

## Compliance Issues

### *Ministry's Vehicle Fleet*

#### Lack of Control on Government-owned Vehicles and Fuel Consumption

MFA's vehicle fleet comprises a total of 19 cars, of which 14 vehicles are attached to authorised high level officers, whilst the remaining five are for general-use purposes.

- a. Logbooks are not kept for any of the five vehicles used by MFA for official duties, as is required by the Public Service Management Code (PSMC), section 8.2.4.1. Thus no control can be exercised on the use of vehicles and expenditure on fuel consumption.
- b. A total of 41 fuel requisitions and issue notes from the Fleet Management System were examined. These covered 1,245 litres of fuel costing €1,809, and supplied to 10 vehicles during the months of July and August 2013. The following shortcomings relate:
  - In six instances, the receiving officer signing for fuel was the same officer raising and endorsing the respective

requisition forms, rather than this being issued and endorsed by an independent person.

- Three requisitions for the purchase of fuel were noted, where two dissimilar signatures were used by the same officer, implying that in certain cases, these are being endorsed by forged signatures.

## Recommendations

### *Key Issues*

#### Clerical Services

Rigorous compliance with PPR and other relevant legislations is expected, taking into consideration the established thresholds, as well as the necessary approvals required from the pertinent authorities.

In the circumstances, MFA was also at least expected to utilise that agreement where lower hourly rates were being charged, to reduce costs accordingly. Furthermore, Management is to ensure that the timeframe imposed by MFIN is observed.

Procurement of a substantial value, or covering a considerable duration of time, is to be invariably covered by a written agreement, clearly specifying the terms and conditions binding both parties. Amongst others, these are expected to include the starting date and the duration of the agreement, the type and quantity of the item or service, the applicable rates payable, and the maximum budget limit allowed.

In addition, invoices are to be reconciled to actual hours worked, and certified as well as endorsed by a responsible officer prior to any payments made without exception or fail.

### *Control Issues*

#### Hire of Chauffeur Driven Cars

NAO considers that the decisions taken by the Adjudicating Board should have been adhered to throughout the duration of the contract.



MFA is to ensure that valid and adequate performance guarantees are made available by the contractor, in accordance with contractual requirements, to cover the whole duration of the respective agreement.

It is in Management's interest to ascertain that proper control mechanisms are in place prior to effecting any payments. MFA is encouraged to replace the current records used for chauffeur driven transfers, with pre-printed and consecutively pre-numbered vouchers, to be duly filled-in for each trip.

### Official Development Assistance

MFA is expected to confirm eligibility with the Commissioner for Voluntary Organisations prior to advancing financial assistance out of public funds to voluntary organisations.

### Awarding of Overseas Scholarships

Even though the concept of locally trained and qualified individuals is encouraged, MFA is to ascertain that Government is in a position to offer a suitable job for prospective students at the end of the relevant courses. Considering the cost involved in such initiatives, it is felt that priority should be given to make available those training programmes that address competency gaps within Government.

Management is also to ascertain that the form of undertaking, endorsed when awarding scholarships, clearly specifies all the conditions and obligations to which students are bound, including clauses relating to the refund of course fees and expenses.

Meanwhile, MFA is encouraged to assess the basis of the current penalties and ensure that the respective amounts are related to the applicable course fees and ancillary expenses incurred from public funds.

### Compliance Issues

#### Ministry's Vehicle Fleet

Management is expected to introduce logbooks for general use cars, in compliance with PSMC section 8.2.4.1, to better monitor and control the use of these vehicles on official duties and the expenditure on fuel.

It is essential that fuel requisition forms are duly approved and endorsed by an officer independent from the one receiving the fuel, for better control on the related costs.

### Management Comments

Management noted the findings and also stated that action will be taken accordingly to address the shortcomings.

It was further claimed that the decision to retain clerical services from the original contractor, even though at a higher rate, was taken in view of the fact that changing the latter would have entailed additional training by MFA, and hence disruption of services which were required urgently.

MFA also remarked that since a 'Ministerial' type car is a protocol requirement, if overlooked, this could have led to negative diplomatic relations. This shall be taken into consideration when re-issuing the forthcoming tender.



Ministry of Tourism

# Heritage Malta

## Revenue Audit

### Background

Heritage Malta (HM), also referred to as the Agency, was set up in 2002 under the provisions of the Cultural Heritage Act, Chapter 445 of the Laws of Malta, and is the national agency for museums, conservation practice and cultural heritage.

HM is governed by a Board of Directors consisting of a Chairman, Deputy Chairman and six members, appointed by the Minister responsible for cultural heritage.

The organisation structure at HM comprises four main units, through which the Agency is responsible for ensuring that those elements of cultural heritage entrusted to it are protected and made accessible to the public. It is also in charge of conserving and restoring cultural property within its portfolio, in the best possible manner, as well as to provide the respective training, research and practice. In addition, it strives to create public awareness through displays, exhibitions, thematic events, public relations and other initiatives, and acquire sites, buildings, and collections of objects for the museums.

The subsidiary of HM, namely Heritage Malta Services Ltd (HMSL), serves as its commercial arm for activities and events of a commercial nature. Amongst others, these include the hiring out of venues for corporate entertainment, photography or filming, and monitoring the museum shop activities. Any revenue derived from such activities is recognised in the books

of HMSL, with the latter paying the Agency a management fee to make up for ancillary expenses which are borne by HM.

### *Performance, Financial Resources and Statistics*

The Agency finances its operations mainly through revenues generated from admission fees to museums and sites, which fees are set out in several Legal Notices. Two Government Subventions, which in 2013 amounted to €3,340,000 and €479,719, were granted to fund recurrent and capital expenditure respectively. Gross income generated by HM during the same year reached €5,676,976, of which €4,922,793 related to entrance fees. This represented an increase of 6% over 2012 figures.

### Audit Scope and Methodology

The main objectives of the audit were to determine whether an adequate system of internal controls on revenue collection was in place, to assess the operating effectiveness of the said controls over the various revenue streams, and to provide recommendations to enhance governance, the efficacy of control practices, and also to reduce risks associated with revenue management.

The focus and extent of audit work was based on an assessment of materiality and related risk. This was achieved mainly through a walk-through of the system in place, as well as reviews of the reports generated, statistics and bank statements.

## Audit Disclaimer

Although a comprehensive Information Technology (IT) audit was carried out by the National Audit Office (NAO) in 2011, the ticketing system in use at the time was replaced with a new system while the foregoing audit was still in progress. Checks on this new system were performed by the service provider and HM's IT staff. Thus, no independent opinion was available on the system's adequacy and effectiveness of embedded controls as at time of audit.

## Limitation on Scope of Audit

### *Cancelled Tickets*

NAO was informed that any cancelled tickets are submitted to Head Office (HO), together with an email indicating the reason for cancellation. However, in a good number of instances, such tickets were not traced. In view of this, the exact number of invalidated tickets could not be reconciled to the actual physical tickets.

### *Recovery Tickets*

Between 2009 and 2011, weekly confirmations of recovery (manual) tickets in hand were submitted to HO by each site, with the former verifying this information against previous week's balances. However, Management claimed that such procedure was not carried out during 2013, due to lack of staff. Moreover, no adequate stock records were kept at the respective locations. The related documentation provided by HO indicated only the number of tickets distributed to the various sites with effect from April 2014.

### *Reconciliation of Membership Income*

Albeit membership subscriptions are issued through the ticketing software, and the respective application forms kept on file, various discrepancies were noted between the latter and the report generated from the system. Moreover, this record did not indicate whether a membership was complimentary or otherwise, making it very difficult to reconcile with actual income received.

## Key Issues

### *Weak Internal Control System*

Although checks are carried out by HO, as well as by site executives, these are still considered as ineffective in a number of areas, leaving ample room for abuse and other undetected shortcomings. The following are the main matters noted during the audit, which will also be outlined separately under Control Issues:

- a. no independent ticket scanning;
- b. high level of dependence on the integrity of front office staff;
- c. lack of centralised internal policies;
- d. significant number of cancellations not supported by the actual physical ticket and respective justification; and
- e. discrepancies between figures in Management Accounts when compared to other source records.

## Control Issues

### *Ticketing System*

#### Background

Tour operators and language schools are given access to the ticketing system. Each entity is provided with a separate account, enabling the generation, printing, amendment and cancellation of tickets directly from the respective offices.

#### Ticketing Controls

While the system in place offers tour operators and language schools the flexibility to print tickets at their own leisure, ticketing controls are limited to those exercised by front office staff, the success of which depends very much on the integrity of the same employees. In the circumstances, any collusion between the operators or language schools, and HM staff, is very difficult to detect.

The following shortcomings were identified:

- a. As at time of audit, neither turnstiles nor any other scanning devices were in place at the various locations except for *Haġar Qim* Park and *Mnajdra* Temples, the Palace Armoury and Palace State Rooms, as well as *Skorba* and *Ta' Haġrat*. By default, the system provides an embedded feature referred to as 'marked as entered', indicating that the ticket has been used. However, a ticket seller has the possibility to untick this option, intended to be used mostly in instances where the ticket is not availed of immediately upon purchase. This could easily lead to manipulation, thus allowing the visitor to enter more than once in any particular site.
- b. Reliance is also placed on front office staff, in cases involving groups. Given that the system allows one ticket to be issued for a whole group, due to the lack of means of verification, groups have to be physically counted with the actual number manually inputted into the system. Any unutilised 'entrance passes' may be used on a different occasion, or voided (cancelled) and refunded. In instances where there is no segregation of duties in the process, this could lead to both genuine errors as well as intentional abuse.
- c. Clients may also opt to purchase 'Multi-site' tickets for multiple persons. In such a case, a single ticket will include various admissions, indicating the number of visitors covered. Once a particular location is visited, the ticket will be 'marked as entered' for that site, with front office staff inputting the number of visitors present. Once again, accuracy of these records depends on the integrity of the respective employees.

### Voided Tickets

A report provided by HM, referred to as 'Voided Tickets Report', revealed that in 2013, there were 5,143 instances involving cancellation of tickets. Through testing performed by NAO, the following issues were noted:

- a. A total of 4,035, *i.e.* 78% of the said voiding instances, related to tickets purchased by travel agents and language schools. While in such cases no justification is required, since cancellation is effected by the same purchaser, in all other instances, the respective site officers were to provide HO with the reason *via* email, and forward to the latter the physical tickets. Notwithstanding this, out of a sample of 109 voiding occurrences selected for review, only in 50 instances was the email with the justification traced, and just 37 of them where the actual cancelled ticket was located.

Auditors were eventually informed that no such records are maintained in the case of tickets issued and voided by HO staff. However, supporting documentation was also not provided for the remaining instances of cancellation by other HM employees. As a result, no physical inspections of the cancelled tickets could be carried out by NAO, as these were either not available and/or not located by HO.

- b. While tour operators and language schools may only cancel tickets which have not been 'marked as entered', Executives on site, as well as other HO staff, amounting to a total of 18 individuals, together with an Administrator using a generic account, are allowed to void 'marked as entered' tickets. In such case, there is no way to ensure that this facility is not abused.
- c. Without prejudice as to the validity of the majority of cancelled tickets, certain reasons indicated are highly questionable. At least 21 instances were noted where the ticket was annulled because the client 'changed his mind', or 'tickets were forgotten at home'. This raises serious doubts on whether the invalidation of such tickets is justified. Furthermore, some of the reasons imply that tickets are being issued before they are paid for, eventually resulting in a significant number of voided tickets.
- d. In addition to the aforementioned voided tickets report, listing all cancelled tickets, NAO was also presented with an audit log showing the number of times users tried to

void a ticket. However, various instances were identified where tickets included in one record were omitted from the other, thus rendering them inconsistent and unreliable.

### **Reconciliation of End-of-Day Reports**

#### **Background**

The End-of-Day Report (EODR) constitutes a check performed by each cashier at the end of the respective shift, wherein the cash and credit card sales are added and the total is inputted into the system. This is then reconciled, or otherwise, by the same system and a report is generated accordingly.

#### **Control Measure by-passed**

The fact that cashiers have access to the 'Ticket History' screen against which they can verify the amount of cash in their respective tills, impinges on the effectiveness of the above-mentioned control since any favourable discrepancies may not be reported.

#### **Physical Inspections**

A total of 127 physical inspections, comprising reconciliations between EODRs and cash held in the respective cash registers, were carried out during 2013 by Site Executives within HM. Auditors were informed that these were requested by the Manager Visitor Services, on an *ad hoc* basis. However, it was noted that they were not proportionally distributed across the sites. By way of example, while during 2013, one site, namely, St. Paul's Catacombs in Rabat with an annual turnover of €138,181, was subject to 28 inspections, not even one verification was carried out at the Palace Staterooms in Valletta, with a registered turnover of €619,816 during the same year. A further nine out of the 24 (42%) museums and sites, were also not subject to such inspections during the period under review.

Further to the above, it also transpired that whilst one employee underwent 11 inspections at three different sites, 30 out of a total of 61 front office staff members were not subject to any checking during the same year. Moreover, seven of the individuals who experienced an inspection in

2013 did not feature in the front office employee list provided by HM for the said year. This implies that the relevant records are not updated.

#### **Access to Safes**

Both the number of staff, as well as grades having access to safes, varied from one site to another, in most cases exceeding three staff members in each location. In one instance, access was also granted to a student employed temporarily with HM. In view of the additional risks involved, the need to allow so many officers to use the safe is highly questionable, since the retrieval of daily float and deposit of moneybags could be carried out by the Site Executive or any other senior officer on site.

#### **Recovery Tickets**

Recovery tickets consist of manual tickets provided to sites, intended to be used in cases of system failure. Through verifications performed by NAO, the following matters were noted:

- a. During 2013, no adequate stock records of recovery tickets were maintained by both HO and the individual sites. Consequently, correctness of the outstanding tickets in hand could not be confirmed. Moreover, while stock in hand was duly reported to HO by Site Executives on a weekly basis in the year under review, no independent inspections were carried out by the former to ensure correctness of reported balances.
- b. No prices are printed on recovery tickets, but these are manually recorded on the ticket itself, together with the number and type of visitors. Once access to the system is restored, the ticket barcode is scanned and ticket details are manually recorded therein. Thus, once again, accuracy of the inputted data depends on the integrity of front office staff.
- c. Although the counterfoil of used tickets is to be submitted to HO upon use, verifications carried out revealed that this was not always the case.

## Membership Fees

Membership fees receivable, disclosed in the 2013 Management Accounts, stood at €17,706. However, on trying to confirm this figure with supporting documentation, the following issues, which fail to provide the comfort of completeness of revenue, transpired:

- a. According to a report from the ticketing system, membership sales during 2013 totalled €23,398, *i.e.* €5,692 more than that disclosed in the financial records. Management provided a reconciliation between the two records, wherein it transpired that complementary memberships were reflected in the report with their respective price rather than a nil value, resulting in a discrepancy of €7,412. The difference was attributed to other reconciling items, including voided memberships, test entries inputted in the system, and occasional sales not included therein.
- b. The aforementioned report did not indicate any transaction number, time and date, thus again hindering verifications. Moreover, on several instances, different individuals were allocated the same membership number. *Vice versa*, on a number of occasions, the same individuals were included twice, at times with different membership numbers and different fees. This implies that the said report is not reliable and system controls, if any, are very limited.
- c. Significant discrepancies were noted, between the Membership fees received in 2013 as per the ticketing system report, when compared to the manual spreadsheet reflecting the respective members. It also transpired that a number of entries, included in the report generated from the system, were not covered by an application form.
- d. In a number of instances, the nature of membership applied for in the application form did not tally with that reflected in the respective spreadsheet.
- e. In the year under review, HM organised several open days, during which individuals

applying for memberships were eligible for a 10% discount. However, since in many instances the date in the application forms was not filled in, it could not be ascertained that the discount granted was duly entitled.

## Gift Shops' Stock

With effect from 2013, souvenir shops situated at the various museums are manned in-house by HM staff rather than leased to third parties.

While discrepancies identified in a stock count carried out at the National Museum of Archaeology were immaterial, those identified at *Ġgantija* Temples were considered as significant compared to the actual stock on site. Thus, albeit the shop had been open for public, as at time of audit, stock was not covered by updated and reliable stock records.

## Recommendations

### Key Issues

#### Weak Internal Control System

Internal controls are fundamental to the successful operation and day-to-day running of the Agency. It is thus recommended that Management develops its own internal control 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, the identified weaknesses and significant control failings.

Notwithstanding the above, sound internal controls still cannot eliminate the possibility of processes being deliberately circumvented by the collusion of employees. Thus, staff and operations should be supervised by competent officers who understand the processes and procedures that are in place, and who are ready to query such procedures and decisions, if and when necessary, and take appropriate action to address any shortcomings in a timely manner.

## Control Issues

### Ticketing System

All the advantages and disadvantages of the current ticketing system are to be duly analysed to determine whether the benefits justify the additional risks.

### Ticketing Controls

While acknowledging that HM is currently considering the option of integrating the ticketing system with the eventual use of turnstiles for all sites, the matter should be given its due importance. In the meantime, as far as possible, segregation of duties is to be implemented as this reduces the risk of inappropriate actions by the persons involved in the process.

### Voided Tickets

The facility to cancel tickets already 'marked as entered' is to be limited to the least possible staff members, ideally located at HO. In addition, all requests for cancellation of tickets are to be covered by an email, including a valid justification, and kept for future reference. Moreover, measures are also expected to be taken by HO to deter possible abuse by third parties. Furthermore, tickets are not to be issued unless payment is actually effected.

### Reconciliation of End-of-Day Reports

#### *Control Measure by-passed*

Segregation of duties is one of the fundamental internal controls. Thus, only Site Executives are to be given access to the 'Ticket History' screen for control purposes.

### Physical Inspections

A formal audit trail schedule is to be prepared, taking into consideration the turnover of each location and all front office staff employed therein, thus ensuring that resources, as well as checks, are targeted towards those sites with higher turnover and cover different staff members as much as possible. Moreover, the scope of such reconciliations may be widened to incorporate

more verifications, which could be governed by a Standard Operating Procedure, explaining what is to be performed during the inspections. This will help achieve consistency and ensure that audit trails are carried out in a more comprehensive manner.

### Access to Safes

A policy stipulating the number and grades of officers allowed right to use the safe can be drawn up by HO and adopted by all sites. Such access is to be provided to the least number of persons possible.

### Recovery Tickets

A proper stock control system, as laid down in Treasury Circular No. 6/2004 – 'Stock Control Procedures', is to be adopted. Audit trails performed by Site Executives are to include a physical count, indicating the number of recovery tickets in hand, which is then to be verified by HO with that declared in emails submitted. Moreover, justifications are to be provided to the latter whenever manual tickets are used.

Further to the above, in order to reduce the manual intervention in the use of recovery tickets, HM may consider printing different sets of coloured tickets, with each colour corresponding to a particular category of visitor. This would enable more control to be exercised, thus reducing the possibility of abuse.

### Membership Fees

The IT system is to be reviewed in order to ensure that data inputted therein is reliable and reflects the actual income received. Memberships issued as complimentary should be included in the ticketing system report with a nil value. In addition, regular reconciliation with other available records is to be carried out, to identify any discrepancies that may arise in a timely manner. Furthermore, application forms are to be properly filled in and dated.

### Gift Shops' Stock

Stock-takes and update of records are to be carried out on the delivery of goods, in order to ensure adequate control over such items at all times.



## Management Comments

Management concurred with a number of recommendations put forward by NAO, aimed primarily at enhancing internal controls, and started to take action to address certain areas as follows:

- a. *Ticketing Controls* – Turnstiles at *Haġar Qim* Park are currently in test phase with 100% positive results. The remaining high volume sites will have turnstiles implemented by the end of 2015, whilst sites with low turnover will be equipped with a ‘people counter’. It was further indicated that HM utilises Mystery Shopping services, which proved to be a very effective tool.
- b. *Voided Tickets* – HM will make sure that an email is always sent to accompany such tickets. It will also reduce and keep the number of staff with voiding permission to a bare minimum.
- c. *Physical Inspections* – Management will strive to implement the recommendations as soon as possible, and evaluate any possible consequences over a period of time. However, it was remarked that audit trails in high volume sites may lead to poor customer service.
- d. *Access to Safes* – Proposed action to ensure uniformity amongst sites has been accepted and will be taken on board.
- e. *Recovery Tickets* – The ticketing system has been amended to include a log of the recovery ticket serial numbers allocated to each site. Management also agreed with NAO’s suggestion of having pre-printed coloured recovery tickets and believes that this will further close the loophole. The Agency shall be investigating the requirements to implement this solution.
- f. *Membership Fees* – It was indicated that the system caters for complimentary memberships thus showing the cost as nil. However, the respective users failed

to record them at 100% discount, thereby leading to discrepancies.

- g. *Gift Shops’ Stock* – Management asked the responsible Department to execute stock-takes as suggested by NAO.

The following comments and reservations were also expressed by HM:

### *Ticketing System*

It was maintained that the system was created with the users and/or stakeholders in mind, together with the business objectives. All stakeholders were consulted to make sure that the operation of the ticketing system meets HM’s requirements. It was also stated that with over 10 years experience in ticketing procedures, the Agency can safely say that the present *modus operandi* with tour operators and other stakeholders has drastically increased the revenue generated from tickets and eliminated the risk of having unpaid tickets and debtors.

### *Voided Tickets*

Management remarked that the very first voiding control check embedded within the ticketing system is the electronically recorded ‘reason for voiding’. Without such a reason, the ticket will not be voided. The email sent by whoever voids the tickets is an important secondary control check which is not always required, and not always possible to send right away, but which the Finance Section had established with HM Manager Visitor Services as an additional security measure.

The officers who have the facility to void tickets are in senior grades, and thus there must be an element of trust.

In reply to observation (c)<sup>1</sup> concerning the reasons provided for cancelled tickets, it was remarked that visitors often change their mind after purchasing a ticket, especially after noting better priced options. Instances where a front officer issues the ticket before the money is tendered, such as in cases of heavy demand, can also lead to the eventuality that a number of such pre-printed

<sup>1</sup> Observation under title ‘Voided Tickets’ on page 124.

tickets are cancelled. According to HM these are acceptable normal occurrences, but the Agency shall still endeavour to make sure that voiding tickets 'marked as entered' is minimised.

Although Management also considers that the recommendation to set a policy for front office staff is plausible in theory, in practice its implementation might also weaken the customer service. The voiding of tickets functionality for tour operator and language schools is actually also a business requirement, intrinsic to the operation, aimed to make sure they have as much flexibility as possible to purchase HM tickets, eventually leading to more sales.

### *Reconciliation of End-of-Day Reports*

#### *Control Measure by-passed*

In reply to the observation under this caption, management commented that, while it is true that the 'Ticket History' screen can lead to potential abuse, it cannot be removed since it is a feature related to a normal Point-of-Sale reading, after end of shift. However, other possible solutions shall be investigated in this regard.

#### *Access to Safes*

NAO's recommendation, aimed at achieving uniformity between the different locations will be taken on board. It was agreed that it is not

acceptable for a student to be given access to safes, but it was also stated that the remaining staff at the sites cannot be denied such permission, since Site Executives are not present at a particular site all day long. Moreover, employees using the safes record the reason for access, together with the date and time, in a logbook. Management also maintained that, in practice, segregation of duties within HM can never be implemented because the amount of people required in one site would need to be doubled.

### *Recovery Tickets*

HM acknowledged the fact that there is a high risk associated with the use of recovery tickets. In view of this, the Agency has already invested in additional Point-of-Sale computers as a backup, in almost all sites, in case of computer failures. Internet keys have also been provided to mitigate internet connection problems. Thus, the need for recovery tickets has been minimised.

While management agreed with the recommendation relating to the lack of verification of recovery ticket balances, it was highlighted that it could not be implemented due to the restricted current staff complement at HO.





Ministry for Education and  
Employment

## Kunsill Malti għall-iSport

### Background

*Kunsill Malti għall-iSport* (KMS) is the official body appointed to implement Government policy on sport, and is regulated by the Sports Act. One of the Council's functions is to provide financial and other assistance to sports organisations and is also responsible for the administration of four main sports facilities in Malta, namely Cottonera, Marsa, Kirkop and *Tal-Qroqq* Sports Complexes, as well as a number of facilities in certain schools.

The main funding in 2013 was received from Government Contributions, totalling €4,130,000, and the income generated from its own operations, which amounted to €4,626,760<sup>1</sup>. Aggregate expenditure incurred by KMS during the same year totalled €10,142,404 exclusive of Value Added Tax (VAT), out of which €5,247,517 were granted as assistance to sports organisations. The entity registered a loss of €1,379,825 for the year under review. According to Management this was mainly due to:

- a. new workers (a total of seven workers) assigned with KMS after March 2013, plus the two months' salary of the Chairman's Personal Assistant and one government employee;
- b. increase in salaries as a result of the new collective agreement signed in 2013, effective from the beginning of the year;

- c. heating of two swimming pools throughout the whole year; and
- d. increase in assistance to entities committed before March 2013.

### Audit Objectives and Methodology

The main scope of the audit was to determine the level of internal controls over expenditure, and to ensure efficient administration of public funds, in line with standing laws, regulations, policies and procedures, also making recommendations where warranted. Furthermore, the entire process, with regard to the monetary assistance provided to sports organisations, was verified.

The audited Financial Statements for the year ended 31 December 2013 were analysed to determine KMS's overall financial position, and minutes of Board meetings and other information of relevance to the audit were gathered.

A sample, consisting of a total of 36 transactions, was chosen. Five transactions, amounting to €496,922 (VAT excl.) from a total of €1,810,472 (VAT excl.), were selected from the accounts relating to assistance to sports organisations. Another 31 transactions, amounting to €112,137 (VAT excl.), were selected from 10 accounts out of the remaining expenditure, in aggregate amounting to €1,076,345 (VAT excl.).

<sup>1</sup> This figure included an amount of €3,143,199 being notional income mainly related to rent subsidy to sports organisations.

## Audit Disclaimer

In view of time constraints, testing was neither comprehensive nor exhaustive. The observations and respective recommendations in this Report are based on the shortcomings encountered during audit testing and the outcome following enquiries made by National Audit Office (NAO).

## Limitations on Scope of Audit

The objectives and the completeness of the audit examination were hindered as KMS did not present adequate information as indicated hereafter:

### a. Strategic Plan

The Sports Act Cap. 455 stipulates that the Council is to present to the Minister for his approval, a three-year strategic plan outlining objectives and targets for that period and to prepare, on an annual basis, an operational plan in line with what was proposed in the former. However, a copy of the strategic plan, covering 2013, was not available. NAO was informed by Management that the strategic plan for the period 2012-2015 was delayed in view that the National Sports Policy had not yet been finalised. A Sports Operational Strategy Document was prepared in the beginning of 2014.

### b. Minister's Approval

According to KMS, following his appointment in 2008 till March 2013, the then Chairman was delegated the responsibility for the approval of direct orders up to a maximum of €6,000 (VAT excl.). Yet, no document was provided evidencing the Minister's authorisation in terms of Article 20(1)(b) of the Public Procurement Regulations (PPR).

Similarly, correspondence sent by the Ministry for Education and Employment, informed NAO that the Permanent Secretary, who held office during the period 1 January to 15 October 2013, was also responsible for the approval of direct orders up to a maximum of €6,000 (VAT excl.). However, the actual delegation by the Minister, was not provided by the said Ministry for audit purposes.

### c. Financial Assistance to Sports Organisations

The sampled transactions, covering financial assistance to sports organisations, included €200,000 paid to an Association, to develop a new sports hall and/or training facilities through the Facility Improvement Scheme, €86,000 provided for works carried out at a *Boċċi Club*, also allocated through the foregoing Scheme, and an amount of €70,000 which was reimbursed to a Local Council for the provision and installation of gymnasium equipment.

The original application and/or claim for assistance submitted by the respective sports organisation or club, as well as any relevant initial correspondence, such as budget forecasts of the entity concerned, were not provided for audit purposes in the above instances.

Moreover, though an agreement was eventually drawn up between both parties and the amount of €70,000 was advanced to the Local Council in question, an official letter of commitment addressed to the latter, and invoices relating to works carried out, were not available at KMS for NAO's review.

## Key Issues

### Contractual Services

In October 2012, KMS issued two departmental call for tenders, one for security services and the other for cleaning services in KMS's sporting facilities. Both tenders were issued for a period of one year, extendable by another year at the discretion of KMS, and up to established thresholds of €120,000 (VAT excl.) each. Weaknesses indicated hereafter relate:

#### Terms and Conditions not formally agreed upon

A letter of appointment referring to the tender conditions was issued by KMS to both service providers. However, no form of acceptance from the contractors to bind the contract was made available.

### Thresholds and Time Limit exceeded

- a. The total invoices charged to KMS in respect of the security services tender, from December 2012 up to May 2014, amounted to *circa* €443,390, of which €337,401 pertained to services rendered in 2013. This is by far over and above the set threshold, especially given that total cost is set to increase since this agreement was still in place as at audit date (September 2014).

Likewise, the total invoices received by KMS with regard to the cleaning services tender, from February 2013 until May 2014, amounted to *circa* €270,680. Of this amount €227,687 related to services rendered in 2013.

This implies that both tenders should have been issued through the Department of Contracts (DC) rather than Departmental.

- b. The agreement with the contractor, for the provision of cleaning services, continued to be undertaken by KMS, at least up to May 2014, regardless of conditions imposed by the Departmental Contracts Committee within the Ministry for Education and Employment upon approval, that it was to be terminated strictly after a period of one year, *i.e.* by mid-January 2014.

Moreover, pursuant to enquiries by this Office, no information was provided, as to whether such an extension was formally approved by DC, and communicated to the contractor accordingly.

### Valid and Adequate Performance Guarantee not available

- a. Even though, as per conditions of the tender document and Letter of Acceptance for security services, a performance guarantee, set at 10% of the contract value, was to be presented by the winning bidder, and released within 30 days of the final bill, such document was not available to cover the security services.

However, testing revealed that only the bid bond covering up to €1,000 was extended, whereas, the bank guarantee should have covered up to €12,000.

Moreover, no evidence was provided that any form of guarantee was extended beyond 10 April 2014, in spite of the agreement still being utilised as at audit date (September 2014).

- b. The bank guarantee, submitted by the contractor for cleaning services, only covered the first year of the agreement. In addition, the amount guaranteed during the first year of the agreement was €11,000, which lies below the 10% of the maximum contract amount, requiring a guarantee of €12,000.

### Payments for Services rendered not supported by proper Attendance Records

#### *Security Services*

Notwithstanding that security guard services are paid on an hourly basis, neither rosters of work, nor attendance records are held at any of KMS's sites to support invoices submitted by the service provider, which as already indicated totalled €337,401 in 2013.

#### *Cleaning Services*

- a. Rosters of work for cleaning services at KMS's facilities were also inexistent. This makes it rather difficult to establish actual working hours in order to validate respective payments, which in aggregate amounted to €227,687 in the year under review. Moreover, an analysis of the cleaning timesheets provided showed that cleaners work dissimilar shifts, with differing break periods, if any, which were not recorded consistently in all timesheets. KMS Accounts Department confirmed that "... *arrangement is done verbally*".
- b. Examination of available attendance sheets, provided by KMS for cleaning services, revealed various deficiencies in these

manual records. The timesheets evaluated pertained to eight cleaners, covering the Cottonera and Kirkop Sports Complexes, during the month of July 2013.

The following shortcomings were identified:

- No attendance sheets were available for one of the four cleaners working at the Cottonera Sports Complex. Only a breakdown of the total number of hours per day, provided through the contractor's invoice, was included. In response to enquiries by NAO, KMS replied that "... *the invoice is the timesheet itself ...*" and that a KMS officer "... *signed to certify her attendance at Head Office ... .. deemed to be relevant effective check for KMS ...*".
- One cleaner was observed to have worked all the month of July 2013 with the exception of just one day off, at an average of approximately 62 hours per week<sup>2</sup>, at the Cottonera Sports Complex. Meanwhile, other cleaners in Kirkop were mostly working 14 hour shifts<sup>3</sup>, including one hour break during weekdays, with instances being observed of cleaners working these abnormal shifts at a stretch of up to four days in a row.
- Rather than verifying timesheets on a daily basis, it is understood that KMS officer at the Kirkop Sports Complex was endorsing such documents once on a weekly basis, while that at the Cottonera Sports Complex even on a monthly basis.

#### *Clerical and Accountancy Services*

During 2013, KMS subcontracted temporary personnel from four different service providers, for an aggregate amount of €24,269, to complement the existing staff within the Accounts Department. An invoice from each supplier, in aggregate amounting to €8,298, was selected to confirm that the hours claimed were supported by adequate

documentation. Upon enquiry, KMS confirmed that records substantiating the hours worked were not available, but alleged that these were checked by the Accounts Manager against a log kept on the email calendar.

#### *Financial Assistance to Sports Organisations*

Eligibility for financial assistance is either mentioned specifically in the Act, as in the case of the Malta Olympic Committee (MOC), or may be granted following the submission of an application by any registered sports association or federation, through any one of the various incentive schemes operated by KMS.

Further to the three payments already mentioned within the limitation of scope, related to a *Boċċi Club*, an Association and a Local Council, the sampled transactions included another payment of €176,616 to MOC. The amount of €120,000 covered the participation in the Games of the Small States of Europe, and the remaining €56,616 was to be relocated to national associations or federations and for the technical preparation of athletes. Another payment of €20,000 was made to a Foundation as assistance for the hosting of an activity.

The following shortcomings relate:

##### *a. Budget Forecasts not requested*

The claim by the Foundation, for financial assistance to host the activity, was not backed up by a detailed forecast of all the planned expenditure to evaluate whether the event is viable.

##### *b. No Formal Agreement signed*

No formal agreement stipulating the relevant terms and conditions was in place between KMS and the Foundation, in connection with the financial assistance granted. Only a letter of approval, covering the amount involved, and endorsed by a KMS senior official, was issued.

<sup>2</sup> Working 12-hour shifts, including one and a half hour break on weekdays (totalling 22 days), and six hour shifts including half an hour break during weekends (totalling eight days).

<sup>3</sup> Shift is from 08:00 to 22:00 with one hour break.



c. **No Conditions issued on Procurement Procedures**

Adherence to PPR was not included as a condition upon signing of letters of commitment or agreements in the case of the five organisations reviewed.

**Non-adherence to Agreement Conditions**

a. **Non-compliance with Conditions tied to Financial Assistance**

A contract, covering the assistance to be given for 2013, was signed between KMS and MOC on 13 May 2013.

The contract required that MOC notifies the Council with the actual amounts being allocated from its end as financial assistance to other eligible sports entities. A breakdown of such funds was also to be indicated within 30 days of the signing of the contract. However, following enquiries made by NAO, it transpired that the only available information related to the allocation of amounts was dated 8 October 2012, *i.e.* prior to the contract date.

b. **Reimbursement of Payment without presentation of Invoice**

An amount of €19,183, being part of a reimbursement of €85,797 to the *Boċċi Club*, in respect of the renovation works carried out at the same club, was not covered by a tax invoice for VAT purposes, but was only supported by a certified bill of quantity.

c. **Invoices not covered by a Certified Bill of Quantity**

Two invoices submitted in respect of major works projects, namely the new multipurpose sports hall and/or training facilities, and renovation at the *Boċċi Club*, were not covered by a certified bill of quantity to justify and validate the substantial expenditure presented for reimbursement. The relevant invoices had a global value of €144,209 and €66,614<sup>4</sup> respectively.

**Director's Remuneration approved retrospectively**

An amount of €18,000, paid on 4 March 2013, represented a single disbursement made to a Board Director, for services rendered as acting facility manager at *Tal-Qroqq Sports Complex*, for the 18-month period from September 2011 to February 2013. This was only approved at the end of his tenure, by a letter dated 18 February 2013, signed by the then Parliamentary Secretary for Youth and Sport.

**Continual use of Direct Orders**

a. **Accounting Services**

A private firm was originally awarded the tender for the provision of accounting services, to assist in the day-to-day running of KMS Accounts Department, for one calendar year up to 15 January 2013.

Following an agreement entered into on 10 July 2012 by KMS, for additional professional services from the same contractor, chargeable at the original tender rate, a 'Variation of Letter of Engagement' notification, dated 16 January 2013, extended the original one-year period indefinitely, until either party terminated. The total cost of professional and accounting services, which was not factored in at tendering stage in line with PPR, in aggregate amounted to €40,573. This is considered to be a direct order for an indefinite period.

b. **Research and Consultancy Services**

The tender, awarded for the provision of the European Union related research and consultancy services with respect to sports, had a maximum budget of €20,000, to cover a one-year retainer period. The foregoing allowed the option of extending the retainer for further periods, following expiration of its validity.

KMS eventually paid a retainer fee for a total of 31 months, covering the period from June 2011 up to December 2013, together with additional charges of €660 for overseas

<sup>4</sup> Excludes the amount of €19,183, for which no invoice was presented, but a reimbursement was made.

hours, in aggregate amounting to €31,036, thus exceeding the budgeted amount by €11,036.

#### c. Spare Parts for Treadmills

Spare parts for treadmills were procured by direct order from the original supplier for a total cost of €7,470, including the engineering services provided. However, the necessary Ministry for Finance approval for this direct order was not sought.

## Control Issues

### *Agreement not in line with Direct Order Approval*

The audit sample included an invoice dated 4 February 2013, amounting to €9,482. This referred to maintenance works to the domed roof of the Cottonera Sports Complex, for the period between June 2011 and June 2012.

Testing revealed that on 25 September 2009, approval was granted by the then Ministry of Finance, the Economy and Investment (MFEI), to KMS, to enter into an agreement by direct order in respect of such maintenance, covering a period of one year, at a cost of €8,036 (VAT excl.).

However, the agreement signed with the contractor on 1 June 2010 was actually effective for the duration of 24 months from the date of signing, or until terminated by one or both parties. This also implies that the payment in question was not covered by MFEI approval.

### *Other General Shortcomings*

#### Substantial increase in Telephone Costs

During 2013, there was a significant increase in telephone costs of 55%, as expenditure incurred by KMS increased from €39,930 in 2012, to €62,003 in the following year. Total staff as at end December 2012, working at the Cottonera Sports Complex, amounted to 24. Due to additional staff on site, the subsequent year ended with a total of 38 employees. According to Management, this may have partially contributed to the increase in telephone costs.

A sample of two telephone bills, covering a period of two months (May and October 2013) in respect of the Cottonera Sports Complex, revealed high telephone bills to cover mobile phone calls. By way of example, 89% (€3,952) of the aggregate sampled invoiced amount (€4,448) related to 6,662 mobile calls made from the fixed lines. It also transpired that all staff had access to these unbarred telephone lines. According to the adviser to the Minister, action has been taken to curb costs.

#### Lack of Control over General-use Vehicles

The logbooks, in respect of the three government-owned and two leased vehicles used by KMS during 2013, which were requested for audit purposes, were not provided since this Office was verbally informed that none are kept. As a result, testing to ascertain whether proper control was exercised over the use of cars and the issue of fuel, could not be performed.

## Compliance Issues

### *Attendance Verification Systems and/or Devices not in use*

During the audit, it was confirmed that two punch clocks were installed at two separate KMS sites, out of the four main sports locations.

Minutes of Board meeting held on 1 August 2013 revealed that the then Chief Executive Officer confirmed that all employees, including Head of Departments and contractual employees, would be instructed to punch in and out of work. However, on 10 September 2014, NAO was informed that higher authority was still required to proceed.

## Recommendations

### *Key Issues*

#### Contractual Services

Procurement of a substantial value, or covering a considerable duration of time, is to be invariably covered by a formal agreement in line with the tender document, clearly specifying the terms and conditions binding both parties. Rigorous

compliance with PPR and other relevant legislation is expected without any exception, so as to ascertain transparency and fairness, as well as ensuring that the most competitive market prices are obtained.

KMS is to ensure that adequate performance guarantees are made available by service providers in accordance with tender requirements, and remain valid throughout the whole duration of the respective agreement.

Adequate and reliable controls are to be introduced concerning services rendered. A proper roster and uniform template for an attendance sheet system, clearly recording the actual hours worked, is to be implemented. These are expected to be certified and endorsed by the responsible officer, on a daily basis, on behalf of KMS, prior to any payments being made. The system can eventually be upgraded to a biometric-electronic attendance system.

#### Financial Assistance to Sports Organisations

Management is to ensure that all the necessary information is available prior to committing any public funds to sports organisations. KMS is also encouraged to include the rationale of public procurement as a requirement when approving financial assistance, to ensure better transparency in using public funds. Agreements are to be invariably signed; moreover, the importance of post evaluation of the funded projects is not to be overlooked. All contract conditions are to be invariably enforced. Payments should never be made unless the necessary documents and certifications are presented.

#### Director's Remuneration approved retrospectively

Commitments are not to be entered into unless the appropriate authorisation has been obtained. Adherence to PPR is paramount in ensuring that accountability and transparency prevail.

#### Continual use of Direct Orders

Procurement is to be invariably made in accordance with standing regulations. In line with PPR, Article 20(4), in exceptional cases, direct contracts in excess of €6,000 (VAT excl.) may be

placed after obtaining the prior written approval of the Minister. Reference to MFIN Circular No. 3/2013 – 'Public Procurement Regulations – Direct Orders', can also be made for further guidance *vis-à-vis* direct orders.

#### Control Issues

##### Agreement not in line with Direct Order Approval

KMS is to adhere to prevailing regulations to ensure procurement proceedings are carried out fairly and in a transparent manner.

##### Other General Shortcomings

Management is encouraged to take adequate measures to effect telephone cost savings, amongst which, reassessing access to mobile phone calls from landlines. Personnel requiring such access are to be identified and the respective authority duly documented.

KMS is expected to maintain proper logbooks for all general-use vehicles in accordance with standing regulations outlined in the Public Service Management Code (PSMC) sections 8.2.4 and 8.2.5.

#### Compliance Issues

##### Attendance Verification Systems and/or Devices not in use

As outlined in PSMC section 3.1.5, attendance verification devices are an effective tool to capture employee attendances by means of electronic reading devices. These devices, such as the punch clock, although they will not eliminate all risks, will reduce errors which are more prone to arise from a manual attendance system.

#### Management Comments

##### Limitations on Scope of Audit

As the delegation of responsibility for direct orders requested was not all traced, KMS agreed that in future, it will keep a copy of applicable delegations.

### *Contractual Services*

Management has agreed that procurement of a substantial value or covering a duration of time is to be further covered by a formal agreement and will be implementing such proposal for procurements exceeding the amount of €30,000 as from 2015. KMS has noted the reservations raised by NAO with regard to security and cleaning services and, although there are justifications for the occurrence, it cannot but agree with these conclusions. Steps will be taken to ensure that the situation will not be repeated. It further agreed that there was a weak system in place to monitor performance guarantees. Measures are now being taken to rectify this shortcoming.

Though Management maintained that controls on the hours worked by contracted staff were being done unofficially and without a standard procedure by the facilities Managers, as from December 2013, rosters of work and attendance records were introduced for both services in order to have an official process and documentation to support invoices submitted by such service provider. An Accounts Officer is also presently checking the hours declared on invoices submitted for clerical and accountancy services, with attendance sheets prior to proceeding for payment.

### *Financial Assistance to Sports Organisations*

Requests for financial assistance have now been capped up to a maximum of €10,000. A declaration of funding and a detailed report of how the project is going to be finalised is now also required. KMS is not of the opinion that it should act as a Financial Controller of these projects as once the project is approved, Management should

only monitor the delivery not the detail, especially since part of the funds are also provided by the respective Association itself. Measures will be taken to ensure that no payment is reimbursed unless an invoice and a certified bill of quantity are presented.

### *Other General Shortcomings*

Since May 2014, KMS has moved to a fibre-optic telephone system resulting in better rates. Furthermore, it has removed telephone lines that were non-operational in all its complexes and limited access to mobile phones only to the Facility Managers. Since October 2014, detailed monthly reports of all telephone calls to and from its Head Office are also being requested by Management.

### *Attendance Verification Systems and/or Devices not in use*

The use of punch clocks will be used by sub-contracted employees, to ensure better monitoring of their services. Eventually, these will also be used by KMS employees.

### *Issues not addressed*

No reply was received with respect to the following audit issues:

- Director's Remuneration approved retrospectively
- Continual use of Direct Orders
- Agreement not in line with Direct Order Approval

# University of Malta and Junior College

## Capital Expenditure

### Background

The University of Malta (UoM) is a corporate body having a distinct legal personality, with the capability of entering into contracts for acquiring, holding and disposing of any kind of property, as well as entering into all transactions which are incidental or conducive to the exercise or performance of its functions under the Education Act, Cap. 327 (Part VII), and subsidiary legislation.

Besides the main Msida campus, there are two other campuses; one is housed in the Old University Building in Valletta, and serves as a prestigious setting for the hosting of international conferences, seminars, short courses and summer schools, whilst the other is the Gozo Campus, where part-time evening degree and diploma courses in various areas of study are offered.

Revenue is generated by UoM, however, expenditure is also funded from the consolidated fund through the Vote of the Ministry for Education and Employment (MEDE). The Financial Estimates Capital Vote V, Item 7021 for 'Construction/adaptation/refurbishment works and equipment', show that the budget allocation with respect to UoM and Junior College for financial year 2013 stood at €4,500,000. However, actual total capital expenditure amounted to €5,775,271.

### Audit Scope and Methodology

The objectives of the audit were to verify that during the financial year 2013, capital expenditure incurred was duly authorised, properly accounted for, and in adherence to the Public Procurement Regulations (PPR) S.L. 174.04, as well as other relevant circulars. Management issues, such as the applicable procedures, delays in project execution, quality of work performed, internal controls, and any cost variations from the original amount budgeted, were to be determined.

Testing focused on procurement related to the capital expenditure of a range of projects. An introductory meeting was held with UoM Finance and Procurement Directors, as well as the Accountant (Finance Operations), in order to gain knowledge about internal controls and adopted procedures. Other meetings were held with Management and Administrative Officers during the course of the audit, as necessary. Another meeting was also held with top officials within MEDE, in order to determine the role of the Ministry, *vis-à-vis* the capital budget pertaining to UoM.

A sample of 10 contracts, whose procurement process entailed calls for tender, was selected for testing. Seven of these tenders were issued directly by UoM, whilst the remaining three were issued through the Department of Contracts (DC). Two direct orders approved by the Ministry for Finance (MFIN) were also examined. In addition, a sample of 34 payments made to 11 different suppliers,

amounting in total to €80,395, was selected from a list of capital expenditure transactions below €6,000 exclusive of Value Added Tax (VAT).

### *Limitations on Scope of Audit*

The objectives and the completeness of the audit examination were hindered as the following information was not presented for audit purposes:

#### a. Minister's Approval

Correspondence sent by the then Head of Secretariat, Ministry of Education, Employment and the Family, notified that the Minister authorised the Rector and the Director of Finance to approve direct orders up to a maximum of €6,000 (VAT excl.). However, notwithstanding a request and subsequent reminder, the actual delegation by the Minister in terms of Article 20(1)(b) of the PPR was not made available.

#### b. Financial Plans

Although the National Audit Office (NAO) was informed that UoM submitted the proposed projects in line with MFEI Circular No. 6/2012 – '2013 Financial Plans', the relative documentation was not made available for audit review.

#### c. Role of the Ministry

MEDE's role with respect to UoM capital expenditure could not be confirmed by NAO, as the relevant queries remained unanswered.

## **Key Issues**

### *Actual Expenditure in excess of the Amount Budgeted*

An overview of the capital expenditure incurred during the year 2013 revealed material variances between the approved estimates and actual capital expenditure. In particular, the acquisition

of property<sup>1</sup> for the new UoM residence, which was not budgeted for, involved an expenditure of €1,320,091<sup>2</sup>. Furthermore, communication from MEDE, dated 15 November 2013, informed UoM that the allocation was reduced from €4,500,000 to €3,700,000, in line with the revised budgetary projections for 2013. However, by then, most of the expenditure had already been incurred. As a result, despite the overall Government's effort to curb expenditure, UoM still exceeded both the revised budget and the original annual allocation by €2,075,271 and €1,275,271 respectively.

### *Delays in submitting Social Security Contributions and Taxes to mitigate Cash Flow Problems*

'Indirect taxes', listed as payables in UoM Annual Report and Consolidated Financial Statements, increased from €3,520,182 as at end September 2012, to €9,117,011 as at end September of the following year. According to UoM, these consisted of amounts payable in respect of income tax arising from the Final Settlement System (FSS) and Social Security Contributions (SSC) which fell in arrears "... due to timing of cash flow".

This implies that UoM could be partly funding budgetary shortfalls by delaying the submission of FSS and SSC, which amounts were already collected from its employees' salaries. Furthermore, besides the possibility of incurring undue penalties emanating from the relative legislation, this also impinges on the cash flow management of the national budgetary plans.

### *Breach of Procurement Legislations*

#### a. Provision of Building and Engineering Consultancy Services

A departmental tender for the provision of building and engineering consultancy services was awarded in February 2011, for a period of one calendar year or up to a maximum of €120,000, whichever came earlier. In March 2012, the contract was extended for a further year, or up to a maximum of another €120,000, on the

<sup>1</sup> Acquired property comprised a farmhouse, maisonette, garage and a field.

<sup>2</sup> This does not include the construction of the Computing Services Building, for which an additional €46,801 was incurred during 2013, without being budgeted for.

same terms and conditions. This was an option incorporated in the original tender document.

Since the total estimated value amounted to €240,000, factoring in the extension already envisaged at tendering stage, this required a tender through DC in line with PPR. However, such procedure was by-passed. European Union (EU) regulations were also not complied with, since purchases above the threshold of €125,000<sup>3</sup> (VAT excl.) required a public tender notice in the EU Official Journal, which was not published.

b. **Supply, Delivery and Installation of Mobile Offices**

A total of 32 mobile offices were procured by fragmented purchases, namely a departmental tender, a variation to tender and a direct order, over a span of 12 weeks, for an aggregate expenditure of €170,613, as depicted in *Table 1*.

This procurement exceeded the applicable threshold of €120,000 (VAT excl.), thus UoM was obliged to issue a tender through DC in accordance with standing regulations. The advertising of a public tender notice in the EU Official Journal in line with EU PPR was also necessary. However, both these requirements were again not complied with.

## Control Issues

### *Significant Variations*

Whilst appreciating the difficulties in drawing up meaningful cost estimates, NAO opines that variations between a tender estimated cost and the actual contract value in excess of, or less than, 10% are significant. Such discrepancies were noted in eight of the 10 sampled tenders. In six instances, overestimation of costs ranged between 12% and 31%, whilst two cases were underestimated by 27% and 70% respectively.

### *Full Audit Trail of the Process for Acquisition of Property not in place*

During 2013, €1,320,091 was disbursed for an unplanned acquisition of property after its owners approached UoM with an offer of sale. Initially, the land was to be utilised as a car park and eventually, when funds are available, it was intended to be developed into new residence facilities.

From UoM meeting minutes, it was established that the Council had authorised a negotiating team to coordinate this acquisition. The contents of the subsequent meeting minutes disclosed that the purchase of property had been finalised. NAO was informed that the procedure that was followed after the appointment of the negotiating team until finalisation of the deal was not documented.

**Table 1: Fragmented Purchases of Mobile Offices**

<b>Procurement Method</b>	<b>No. of Units</b>	<b>Invoice Date</b>	<b>Invoice Amount</b>
			<b>€</b>
Departmental Tender	24	10-Sep-12 25-Sep-12	127,960
Variation to Tender	2	27-Nov-12	10,663
Direct Order	6	27-Nov-12	31,990
<b>Totals</b>	<b>32</b>		<b>170,613</b>

<sup>3</sup> With effect from 1 January 2012, the threshold in respect of 'Supplies and Services Contract Notice' increased to €130,000.

However, UoM alleged that the cost was based on the price of an adjacent property previously purchased by UoM.

### ***Tender for Resurfacing of Roads***

The departmental tender for resurfacing of roads at UoM premises was awarded in August 2013, for a total cost of €126,443<sup>4</sup>.

#### **a. Quality Control**

The tender for resurfacing of roads did not contain provisions for penalties to be imposed on the contractors in the event of poor quality control results. The respective Director within UoM maintained that if the works are unsatisfactory, the contractor would be requested to redo the work and any payments withheld until the works are rectified. As an additional safeguard, the retention of 5% is not paid before the expiry of the liability period. This is to ensure that, in the event of defaults emerging within this period, the contractor rectifies any defects accordingly.

However, monitoring and supervision claimed as performed by the respective department was not evidenced, and thus could not be corroborated. The only related document provided was the architect's certification *vis-à-vis* the amounts paid, which document was signed by the same Director.

#### **b. Changes to the Scope of Tender**

The value of works carried out on the tender for resurfacing of roads amounted to €116,896, *i.e.* 7.6% less than the total cost for which it was awarded. An analysis of the supporting documents revealed that road resurfacing, which was charged according to the rate stipulated in the financial bid, was only performed on 2,193 out of the 3,000 square metres originally planned. However, an aggregate charge of €29,559 for 'Variations' and 'Extra Works (Trenching Works)' included in the total amount

invoiced, could not be reconciled to any of the rates included in the bill of quantities.

According to UoM these unforeseen extra works mainly entailed excavating and reinstating trenching, to pass an underground fibre optic cable and an electrical cable before the start of the academic year, to avoid disruption and inconvenience to UoM operations. However, no further approvals were sought to cover these additional tasks.

### ***Inadequate Cover for Potential Liabilities***

#### **a. Bank Guarantee**

All the 10 sampled tenders required UoM to be furnished with a bank guarantee amounting to 10% of the value of the contract. However, a copy of such bank guarantee in respect of two departmental tenders, awarded in July and August 2013 respectively, was not available. As a result, there is no evidence that this was in force.

#### **b. Insurance Policy**

A requirement, included in the tender document of the 10 sampled cases, was the contractor's obligation to be insured against the risks stipulated therein. However, copies of the insurance policies were not retained in the respective files. As a result, UoM's interests could be jeopardised.

## **Compliance Issues**

### ***Fragmented Purchases to by-pass Procurement Regulations***

Besides the shortcomings indicated earlier on, the sample selected, from the list of items of a capital nature of up to €6,000 (VAT excl.), revealed various instances where procurement by-passed standing regulations, particularly by dividing the value into more than one purchase order, thus giving the impression that the expenditure is of a less material amount.

<sup>4</sup> The financial bid consisted of three distinct parts, namely Road Resurfacing Works, Pedestrian Footway Works and Provisional Dayworks, which amounted to €111,850, €8,593 and €6,000 respectively.



This approach could have also been used to bypass the Ministry's scrutiny, since expenditure over €6,000 (VAT excl.) required separate disclosure when presenting capital claims, in line with the applicable standing agreement between both parties.

The particular circumstances surrounding fragmented procurement that were encountered are outlined below:

### Computer Hardware

#### a. *Expired Agreement*

In June 2014, UoM confirmed that the same approved suppliers<sup>5</sup> were still being requested to submit their quotes quarterly, and procurement made accordingly, even though the standing arrangement for the purchase of computer hardware expired three years before. This implies that these purchases were being effected by fragmented direct orders. To this effect, according to information made available, UoM spent a total of €93,424 during 2013.

#### b. *Documentation to substantiate Procurement Selection not available*

Except for the ones selected, record of the other quotes applicable for the same period has not been kept in order to support the decision taken.

#### c. *Procurement split on Two Orders*

Six laptops, together with related accessories, were purchased on 26 June 2013 for the Registrar's Office from one of the approved suppliers. The total expenditure, which amounted collectively to €8,093, was divided between two purchase orders bearing the same date, clearly to by-pass the procurement regulations. Since the amount in question exceeded the established threshold for direct orders, this required a departmental call for tenders or a call for quotations published in the Government Gazette as per Section 20(d) of PPR.

### Network Material

Material, amounting collectively to €7,688, was purchased on 11 September 2013, to install the network at the Digital Games and Mobile Offices, and to refurbish the network at the Centre for Entrepreneurship and Business Incubation. The Memorandum attached to the invoices indicated that this material was needed urgently to start works.

This procurement, which was again split in two orders from the same supplier, was made on the basis of quotations obtained directly from a number of suppliers, even though the collective amount disbursed on network material required a public call advertised in the Government Gazette. However, the Director (Procurement) still maintained that no higher authorisation was necessary, as the works were required for two different faculties on two different and distinct projects.

### Laboratory Taps

Laboratory taps, costing €14,733, were purchased from the open market through the same supplier on 9 May 2013. Three purchase orders were raised in this respect, two of which were dated just a day apart, whilst the third one, which corrected the first two, was dated a month later.

Director (Procurement) claimed that UoM was only made aware that the taps needed replacement, as they were no longer serviceable, when the refurbishment of the Chemistry Laboratories was underway. Thus, this purchase was considered urgent in order to restore the function of the same laboratories and procured following quotations obtained directly from UoM selected suppliers. Moreover, it was noted that such quotations were for individual models only, regardless of the quantity required.

However, the above claim by Director (Procurement) was immediately dismissed by the Auditors, as the earliest correspondence traced with respect to such requirements was dated 30 May 2012, *i.e.* a year earlier. In another

<sup>5</sup> An agreement was reached with eight approved suppliers for computer hardware following a Request for Participation. This was valid for three years, until 30 June 2011.

correspondence dated 9 November 2012, the Technical Officer (Estate and Works) stated that the project had been postponed after the quotes were obtained, but he was instructed “... *to go ahead to plan and purchase the materials needed so that the works will commence in May of next year*”.

Thus, in the circumstances, procurement was expected to be made following a departmental call for tenders or after publishing a call for quotations in the Government Gazette.

### Aluminium Partitions

Aluminium partitions were required to create offices for the Gaming Department. This purchase amounting to €8,498, was made on the basis of quotes obtained directly from UoM selected suppliers, notwithstanding that the respective threshold was exceeded.

This procurement was also split on two purchase orders which were raised three working days apart. Thus, procurement regulations were again by-passed.

Director (Procurement) assumed full responsibility for this decision, stating that if the procurement was made through a call for tender, the works would have been delayed by up to six months.

### Office Furniture

A supplier was paid an aggregate amount of €83,032, covering 29 invoices dated from October 2012 to October 2013, for office furniture. NAO was informed that this procurement was effected through piece meal purchases based on three quotations and not through a call for tender, mainly because they were for distinct cost centres within UoM, bought at different times, and to match existing furniture.

The sampled aggregate expenditure of €11,622 with respect to two purchase orders raised in the same month, with invoices both dated 20 September 2013, related to office furniture for the Faculty of Wellbeing Offices. Whilst the purchase made through one of the invoices was based on the cheapest of three quotes, the internal memorandum

raised for the other invoice stated that the furniture needed to match existing furniture for aesthetic and comparability purposes.

In a number of instances, purchases were made on the same date, or on dates which were in close proximity.

## Recommendations

### Key Issues

#### Actual Expenditure in excess of the Amount Budgeted

Actual expenditure is to be contained within the budgetary provisions and any commitments are only to be entered into within the parameters of these allocations. Care is to be taken to ensure that funds are available before entering into a commitment, to avoid situations where payments are postponed indefinitely, leading to cash flow problems and even possible interest payments.

In the event of unavoidable and unforeseen expenditure, UoM should preferably make all possible efforts in order to prepare a solid financial contingency plan, by securing the necessary funds prior to commitment, through direction from the Ministry for Finance (MFIN).

#### Delays in submitting Social Security Contributions and Taxes to mitigate Cash Flow Problems

UoM is to adhere to the pertinent legislation and ensure that the relative taxes arising from FSS, as well as SSC, are submitted on time to the Inland Revenue Department. Under no circumstances are payments to be temporarily postponed in order to fund shortfalls in budgetary allocation.

#### Breach of Procurement Legislation

Procurement is to be invariably made in accordance with the prevailing regulations, to ensure transparency and fair competition. Therefore, any tenders, with an estimated value in excess of €120,000 (VAT excl.) are processed through DC. Moreover, UoM is to keep abreast with EU procurement directives, amongst which,

the applicable revised bi-annual thresholds, that render the publishing of calls for tender in EU Official Journal obligatory.

### **Control Issues**

#### **Significant Variations**

A certain level of variation in project cost estimates is acceptable. However, in order to provide Management with the best information available for UoM's overall budget, these are to be as realistic and as reasonably accurate as possible, thus contributing towards the compilation of more precise estimates.

#### **Full Audit Trail of the Process for Acquisition of Property not in place**

The gist of any discussions and/or negotiations, held throughout the process involving the acquisition of property, is expected to be documented and filed. This will ensure transparency of the proceedings.

#### **Tender for Resurfacing of Roads**

Management is to ensure that there is evidence that capital projects are adequately monitored, in particular where quality is concerned. Such evidence is to be filed appropriately for ease of reference, continuity, as well as for audit purposes. Additionally, for the sake of quality assurance, UoM is encouraged to introduce provisions in similar tender documents, stating that works should be duly certified by an independent architect at the contractor's expense, in order to safeguard its position. Such certification, which may be used to impose the necessary penalties, is to be kept for future reference.

Although NAO acknowledges the fact that planning the tasks that need to be carried out for a particular project, such as road resurfacing, may be challenging, this initial stage is of fundamental importance and needs to be carried out diligently. In this respect, from past experience in similar projects, due consideration should be given to the possibility of additional works which may be required, such that they are also included in the tender document and the respective charges agreed upon accordingly. In the event that direct orders are absolutely necessary, it is to be ensured

that prior approval from the Permanent Secretary is obtained.

#### **Inadequate Cover for Potential Liabilities**

##### **Bank Guarantee**

UoM procurement officers are to draw the attention of any contractor/s who fail to comply with the provisions of the agreement. Furthermore, it is to be ensured that a copy of the bank guarantee is adequately filed, thus providing sufficient audit trail.

##### **Insurance Policy**

A copy of the insurance policy is to be invariably requested and filed for ease of reference and audit purposes. It is also to be ensured that UoM is adequately covered.

### **Compliance Issues**

#### **Fragmented Purchases to by-pass Procurement Regulations**

UoM is to ensure a fair and transparent selection process, in line with the basic principles of public procurement. Expenditure on items of a similar nature is to be considered as a single purchase so as to benefit from quantity discounts, thus optimising value for money. Additionally, effective management requires that action is to be taken well in advance, to ensure that supplies are available on time.

Although procurement by direct order is not the preferred procedure, MFIN Circular No. 3/2013 – 'Public Procurement Regulations - Direct Orders', provides five circumstances under which requests for direct orders are justified. One of these refers to situations when PPR cannot be followed due to extreme urgency arising from unforeseen events, which are not attributable to the contracting authority.

When the value of the direct order is below EU thresholds, the request for approval is to be directed to the Direct Orders Section at MFIN, following the prior endorsement by the responsible Ministry's Permanent Secretary. Public officials,

condoning direct orders without seeking prior approval from the proper authorities, will have to assume responsibility for their actions in line with the mentioned circular.

UoM is encouraged to seek DC's advice and proceed accordingly in particular instances, such as the purchase of computer hardware, where there may be alternative options. As an example, in the case of procurement through a Request for Participation, NAO was advised that the correct way to utilise this procedure is to follow closely Article 26 regulating Framework Agreements. Although this Article falls under Part IV of PPR<sup>6</sup>, and thus its use for lower thresholds are not regulated by the law, its principles are still valid. UoM's attention is also drawn to the fact that the maximum duration of such an agreement should be four years in line with the same regulations.

Documents evidencing the basis of selection are to be filed for ease of reference and to ensure an adequate audit trail.

## Management Comments

UoM agreed with the fact that an entity must not spend more than its allocation, but maintained that Management acted in good faith as, in December 2012 and April 2013, it had been served with 'Letters of Comfort' from MFIN in this respect. After April 2013, a list of projects, whose cost amounted to about €8,900,000, was submitted to both MEDE and MFIN, but only €5,800,000 of this amount was spent as a result of delays experienced in the processing of tenders through DC. MFIN subsequently honoured the commitment through additional allocation.

Although legislation is to be abided with, every four weeks, UoM faces dire cash flow problems as capital expenditure has to be paid from its funds before being claimed from the Ministry, besides the

fact that Government allocations are received late. As a result, the cash flow resources are strained to the extent that UoM is risking being unable to pay its employees every four weeks. This situation, together with a possible solution, was brought to the attention of MFIN but no reply had been received until the management comments were compiled.

UoM was not aware of the breach of procurement legislation in the case of the tender for the Provision of Building and Engineering Consultancy Services. NAO's recommendations will thus be followed for future projects. However, it still maintained that the purchase of mobile offices was in line with PPR.

UoM stated that it was in the final stages of selecting the list of preferred suppliers for computer hardware through an expression of interest. In the meantime, the previous arrangement continued being used. However, NAO's recommendation to keep evidence of the basis of selection was considered valid, and will be taken on board.

The purchase of six laptops for the Registrar's Office, which were urgently required with particular specifications, was an isolated case. It was stated that quotes were requested from eight different suppliers, thus almost exhausting the list of all the reliable suppliers on the market.

No reply was received with respect to the following audit issues:

- Significant Variations
- Full Audit Trail of the Process for Acquisition of Property not in place
- Tender for Resurfacing of Roads
- Inadequate Cover for Potential Liabilities
- Fragmented Purchases to by-pass Procurement Regulations – Laboratory Taps

<sup>6</sup> PPR Part IV 'Rules common to public contracts whose value exceeds one hundred and twenty thousand euro (€120,000)'.



**Ministry for Sustainable Development,  
the Environment and Climate Change**

# Ministry for Sustainable Development, the Environment and Climate Change

## Expenditure Audit

### Background

The Ministry for Sustainable Development, the Environment and Climate Change (MSDEC) was set up to assume a number of functions previously exercised by the then Ministry for Resources and Rural Affairs (MRRA). The portfolio of MSDEC varies from Waste Management Strategy to Fisheries, Agriculture and Animal Welfare.

The Financial Estimates for Vote 17 show that the approved budget for 2013 consisted of €61,323,000 for Capital Expenditure, whilst €50,599,000 was allocated under the Recurrent Vote. Out of the latter, a projected outlay of €25,932,000 was assigned for Programmes and Initiatives.

### Audit Scope and Methodology

The main scope of the audit was to determine the level of existing internal controls over the procurement and payment of expenditure incurred by MSDEC during the year under review. 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.

The audit was conducted in accordance with generally accepted auditing standards. An introductory meeting was held with MSDEC officials, to discuss relevant issues pertaining to the procurement procedures in place. Further queries were subsequently raised and discussed

with officers in charge, during the course of the audit. Detailed substantive testing was carried out to confirm the existence and the correct application of procedures and controls.

Targeted accounts consisted mainly of Materials and Supplies, Contractual and Professional Services, Travel and Rent. Individual transactions included in the audit sample were selected on the basis of their nature and materiality. A total sample of 85 transactions was selected, collectively amounting to €1,804,757 and representing 67% of the amounts expensed from the sampled accounts.

Audit testing was performed to ensure compliance with the Public Procurement Regulations (PPR) through Legal Notice (LN) 296 of 2010 and the Public Service Management Code (PSMC) of 2011, together with all amendments (where applicable) issued thereafter. Selected payments were traced to Letters of Acceptance (LA), invoices, Payment Vouchers (PVs) and fiscal receipts or tax invoices, in order to determine whether authorisation was obtained prior to the date of the transaction, and that related invoices were certified correctly for payments to be effected.

The selected sample was verified against the applicable Contract agreements and documentation supporting the procurement procedures being followed. Transactions relating to travel abroad were also checked to verify that the subsistence allowance entitlement was in accordance with duty rates issued by the Ministry for Finance (MFIN), as well as in compliance with PSMC.

During the audit it was also ensured that payments for the year, to both local and foreign suppliers, were not in excess of the amounts actually due, but as specified in the Tender documents and Contract agreements.

## Limitations on Scope of Audit

A number of limitations were encountered during the audit, hindering the objectives and completeness of the audit examination. Such instances are explained below:

### *Untraceable Documents supporting Payments*

During the course of the audit, MSDEC failed to provide relevant documentation, comprising Local Purchase Orders, LA, PVs, suppliers' invoices and other information justifying the purchase made, to substantiate eight transfer payments in the audit sample, amounting to €484,039 and representing 27% of the sample selected. Such transfer payments, which included expenditure for the period January to March 2013, were effected during May of the same year when MRRA accounts were closed-off, and the relevant MSDEC and Ministry for Transport and Infrastructure (MTI) accounts were created.

A number of attempts were made by the National Audit Office (NAO) to obtain the necessary documents but these proved futile. The issue was escalated further to both MSDEC Permanent Secretary and the then MRRA Director for Strategy and Support Services. However, NAO was informed that the required documentation could not be traced and therefore such transactions, which were material in value, could not be verified.

### *VAT Status*

In 64 instances, the invoices traced in file were quoting a Value Added Tax (VAT) Registration Number, presumably pertaining to ex-MRRA.

Upon requests for clarifications, MSDEC only provided a copy of the VAT Registration Certificate relating to the then Ministry for Food, Agriculture and Fisheries, which was with effect from 1 January 1995. It was verbally stated that the VAT Registration Number in question was currently being used. However, since the scope

for this registration could not be established, NAO was hindered from validating whether encountered invoices were valid as tax invoices for the scope of the audit. Notwithstanding a number of attempts made by this Office to obtain the required information, none was provided. As a result, it could not be ascertained whether invoices should be supported by fiscal receipts, or whether a tax invoice was sufficient.

Further shortcomings in relation to the submission of fiscal receipts or tax invoices, can be found under 'Control Issues' in this write-up.

## Key Issues

### *Lack of Sufficient Audit Trail and Documentation*

This audit revealed that in a number of Ministry files under review, the lack of audit trail was a common factor that precluded this Office from obtaining a good understanding of the facts that took place, in relation to the transactions tested. Moreover, NAO noted that minutes in a number of files were not followed-up or even substantiated with adequate documentation. In such cases, auditors could not verify whether public tendering procedures were adhered to, which could result in lack of control on public spending.

The following are a number of instances encountered that portray this lack of audit trail:

### *Vessel Monitoring System*

From correspondence dated 18 October 2011 between MRRA and the then Ministry of Finance, the Economy and Investment (MFEI), it transpired that on 13 August 2010, the Fisheries Control Directorate issued a tender for the 'Fisheries Information System', which also included a 'Vessel Monitoring System' (VMS), as required by the European Union Fisheries Regulations. This same correspondence stated that the tender was adjudicated in favour of a particular service provider on the basis of the cheapest offer. The following shortcomings relate.

- a. Unfortunately, NAO could not validate this statement since the relative Tender document, Evaluation Report, and Contract



agreement could not be traced, casting doubts on the procurement process.

- b. It was noted that on 17 April 2013, the General Contracts Committee within MFIN, granted approval to further extend the services of the supplier for the year 2013, “... for the estimated cost of €400,000 (VAT excl.) or until the new VMS system is awarded and is operational”. Such approval was over and above previous extensions granted by MFIN before February 2012.
- c. Total payments made to the supplier in question during the year under review, amounted to €177,763. However, in the absence of a contract, NAO could not ascertain that the rates charged on selected invoices are correct, and whether all amounts featuring on these invoices pertained to VMS.

### Consultancy Services

- a. The Department of Contracts issued a Tender on behalf of MSDEC, for consultancy services in relation to an Outline Development Application for a wind farm at *Wied Rini*, limits of Rabat, Malta. The Tender was awarded to a company at a contract value of €188,800. However, from the relevant file, NAO could not trace the tender submissions and Evaluation Report.

It also transpired that a letter from MRRA, dated 15 September 2010, was issued to the service provider, confirming an ‘order to start work’ commencing 23 August 2010, which date was prior to the date when the Contract agreement was signed, this being 9 September 2010.

- b. A Letter of Acceptance issued on 28 January 2010 indicated that consultancy services by another company, for €14,053, should be executed within eight weeks from the official date of order to commence works. However, since the formal order was not traceable in file, NAO was not able to determine whether the eight-week timeframe was respected.

### Retrospective Approval for Variation Order

A Tender was issued by MRRA in August 2009 for consultancy services to draft tender documents, as well as to supervise and co-ordinate the installation of equipment for the new fish market facility. The Tender was awarded to a service provider for the value of €14,053, and a LA in this respect was issued to the successful bidder on 28 January 2010.

It transpired that the contract value was revised upwards to €42,258, due to extensive revisions of mechanical and electrical works of the project itself, which led to increases in the drafting of specifications, design layouts and related supervisory works. This revision was approved by the then MRRA Permanent Secretary on 11 December 2012.

Such approval, representing more than three times the original amount, came after two invoices, amounting to €31,019, had already been issued to MRRA on 27 September 2011. Therefore, this not only indicates that the total amount invoiced was substantially in excess of the original tender amount, but that the variation was approved almost 15 months after the issue of the relative invoices, which were settled in the second half of 2013.

No evidence was provided as to whether notice of this variation was published in the Government Gazette in accordance with Article 20(2) of PPR.

### Control Issues

#### *Payments for Veterinary Services not substantiated*

##### Background

In 2009, MRRA issued an Expression of Interest for the running of an Animal After-care Centre at *Ta’ Qali*, to provide free emergency medical treatment to stray dogs and cats, as well as other veterinary services to pets against payment. The Ministry received four submissions, including that of the successful Clinic, which offer was eventually selected. During the year under review, total payments of €63,800 were made to this service provider.

### Evaluation Report not available

- a. This Office could not verify the Evaluation Report justifying the selection of the successful bidder, since only the signed Agreement could be traced in file. This is indicative of a lack of transparency that could lead to inefficient spending of public funds.
- b. The offer submitted by the selected bidder was “... to conform to current market prices ...”, with no actual rates being quoted. Consequently, no comfort could be drawn from the fact that, at least, the most economical offer was selected. Moreover, in the circumstances, the rates charged by the Clinic in the relative invoices could not be verified.

### Lack of Consistency between Signed Documents

As indicated above, according to the expression of interest submitted by the service provider and the Agreement signed on 28 September 2010, the Clinic was bound to provide treatment to animals at the current market prices. Clause 21 of the same Agreement between MRRA and the successful bidder also states that “*The Beneficiary binds himself to medicate and rehabilitate strays at his own cost, only when the animal has been brought in by the Animal Welfare Directorate and has been found to have no owner. Should a Welfare Officer pick up a pet needing treatment but belonging to a private owner, then it will be the responsibility of the Animal Welfare Directorate to pay the bill at the Centre<sup>1</sup> ...*”.

However, the Clinic’s obligation to provide free treatment to stray animals was partly waived with a contradicting Memorandum of Understanding, signed between the parties on the same date, which states that “*With regard to animals brought in by the Animal Welfare Directorate, a bill is to be issued by the Beneficiary to the Animal Welfare Directorate for services rendered. The doctor’s fees will not be included in this bill and the Ministry will only be liable for the payment of medicines and consumable materials ...*”.

Since the Evaluation Report confirming the selection of the successful bidder could not be traced, as already noted, it could not be established whether the cost of medicines and consumable materials had been taken into consideration during the evaluation process.

### Medicines and Consumables not verifiable

There was no mechanism in place to verify whether all medicines and consumables listed on the individual invoices have actually been utilised during the medication process. Invoices issued include details of the treatment required per animal; however, no proof of any verification of such treatment was made available by the Animal Welfare Directorate. Thus, it could not be established whether payment of invoices to the Clinic were fair and correct. Upon enquiry, NAO managed to retrieve a copy of an undated price list, however the prices charged for some medicines quoted on the sampled invoices could not be tallied with the list provided. In the absence of internal controls that validate the treatment, medicines, and other consumables used for the respective animals, there is no guarantee that any overcharging is not occurring.

### Non-adherence to Procurement Regulations

#### Services in relation to Project Inaugurations procured directly from the Open Market

Testing revealed that in two instances relating to the inauguration of projects under MRRA administration, PPR were not adequately followed, which is conducive of lack of transparency that could lead to unnecessary costs. The following cases relate:

- a. MRRA was responsible for the inauguration of the *Sant’Antnin* Family Park at Marsascala, held in February 2012.

NAO tested three payments in relation to this event, two to one company totaling €10,044 and another of €3,982 to a different service provider. Since only the invoice, LA and PV were traced in file, this indicates

<sup>1</sup> In the case of privately-owned animals, costs are recovered by the Animal Welfare Directorate upon collection of the animal by its owner.

that items were procured directly from the open market, without at least obtaining any quotations. Moreover, in one of these instances, LA was not even endorsed by the then Permanent Secretary.

Furthermore, it emerged that in actual fact all services procured were effectively rendered by the same supplier, given that one of the companies has 60% shareholding in the other, with both sharing the same registered office. However, to acquire the services totalling €14,026, MRRA failed to issue a call for tender or quotations in terms of PPR.

- b. In December 2012, MRRA organised a Christmas Village at *Ta' Qali*. During the review of the relative file, NAO noted that the Ministry had utilised the services of a number of different service providers, whose invoices were processed and eventually settled during the year under review.

Correspondence by MSDEC Permanent Secretary, dated 24 July 2013, gave the green light for payment to avoid legal proceedings, but also recognised the fact that *“This is not an ex-post approval of a direct order, nor an approval of what happened, but simply a recognition of the fact that if a service was requested by Government officials and rendered, then it has to be paid (even if Public Procurement Procedures were not followed)”*.

One of the cases related to payments made to a service provider in relation to adverts for the Christmas Village campaign, amounting to €16,909. Given the amount involved, MRRA should have issued a call for tenders or quotations, but no such evidence of this course of action was traced in file, indicating a clear bypass of Procurement Regulations.

Another two cases related to printing of the Christmas Village leaflets, as well as the rental of lighting equipment, each from different companies. NAO again noted that no prior approval or even quotations were requested. The total payments made to these two suppliers in a span of eight months (May to December 2013), for different events

including the Christmas Village, totalled €18,905 and €23,431 respectively.

### Consultancy Services by Direct Order

Two consultants were directly engaged by the Ministry to provide studies for two separate projects, bypassing standing regulations, as detailed below:

- a. In April 2013, an individual was commissioned to conduct a geological and geotechnical study on the Azure Window in Dwejra, Gozo, by means of a direct order, valued at €7,000. It also transpired that the pertinent invoice was issued on 28 March 2013, thus before the Notification Letter was sent and also prior to the completion of the study in question, which was handed over to MSDEC on 17 July 2013.

The invoice was settled by means of a downpayment of €2,000 on 20 May 2013, with the remaining balance of €5,000 being paid on 19 July 2013. A review of the relative file did not provide any details concerning the selection of this service provider, nor was any MFIN approval requested for this direct order.

- b. MRRA requested a consultancy company to furnish a quotation to cover a cost-benefit analysis for the project, in order to study the impact of a commercial wind farm on *Avifauna* at *Sikka l-Bajda*. The consultant proposed that the study be conducted in two separate phases; Phase I for a cost of €10,800 and Phase II for a cost of €4,130. To this effect, MRRA requested a direct order approval from MFEI, which approval was granted on 28 September 2012 for the total amount of €14,930. The following shortcomings were noted.

#### *i. Justification for Direct Order request lacking*

In MRRA's request for direct order approval from MFEI, it was stated that the rates offered by the respective consultant were considered fair and reasonable, based upon recent offers received in another tender.

The Ministry also emphasised that the study was urgently required, whilst the consultant in question was the most experienced. However, no evidence was traced in file to support this statement, except for the single quotation from the consultant in question. Although giving its approval, MFEI urged MRRA to ensure adherence to PPR when procuring consultancy services.

Moreover, despite the urgency involved and the premise that the studies had to be completed within one month, *i.e.* by the end of October 2012, it transpired that whilst the payment of €10,800 for Phase I was effected in October 2013, no invoice for Phase II was traced in file, which could indicate that this was not accomplished by the service provider.

*ii. Request for Retrospective Direct Order declined*

An amount of €9,809 was also paid in two tranches to the same consultancy company in 2012 in connection with a proposal for reviewing Malta's Energy Policy. Testing revealed that the service in question was not procured in line with PPR, and no quotations were obtained from other service providers, on the basis that the service provider "*... was the most suitable expert for the job*".

Prior to settling the above-mentioned balance, MSDEC requested approval for direct order from MFIN on 27 March 2013, which was instantly declined, stating that, "*... this office is not in a position to grant retroactive approval for direct orders. However, if the service was given to your satisfaction, you may wish to proceed and settle the outstanding invoice, provided funds for the purpose are available ....*", also emphasising that "*... this is not to be considered to be any form of direct order approval, implied or otherwise*".

## *Non-compliance with Contract Agreement*

### *Background*

A Tender was issued by MRRA in April 2010 for the supply and delivery of laboratory equipment, as well as consumable accessories to the National Veterinary Laboratory. This was adjudicated to five distinct suppliers, one of which was engaged to provide 12 items amounting in total to €12,155.

A Contract agreement between MRRA and the selected bidder was subsequently signed on 19 November 2010, stipulating the time limit for the delivery of items to be three to six weeks from the date when the Contract agreement was signed, this being 31 December 2010.

### *Time Limit as per Contract not respected*

NAO noted that the related four invoices issued by the supplier in question were dated between 30 October 2012 and 5 April 2013, implying that the delivery of goods well exceeded the established time limit as per Contract agreement. It also transpired that the respective payments to this supplier, amounting to €12,834, were effected in September 2013, almost eleven months after the issuance of the first invoice. The difference in the amount paid is explained hereafter.

### *Discrepancies in Amounts charged*

It transpired that in two invoices, the supplier charged additional VAT on 10 of the 12 items delivered. Unit prices as per Contract agreement, which were quoted inclusive of VAT, were in fact quoted erroneously on the respective invoices, thus leading to a double-charge of VAT applicable on these items. As a result, the aggregate overpayment totalled €576.

Furthermore, in the case of one particular item, the contracted price was €125, whilst the gross amount as per invoice (VAT excl.) read €232. Upon enquiry, it was verbally claimed that MRRA opted for a more expensive version of this particular item, due to technical reasons. However, no approval and related correspondence for such decision was traced in file.

### **Bank Guarantee not renewed**

Similar to the observation already reported upon under the second 'Key Issue', although a Bank Guarantee was provided by the supplier upon signing the Contract agreement, valid for one year up to 19 November 2011, no renewals for such Guarantee were traced in file, covering the period up to when the items in question were delivered to MRRA. The absence of this Guarantee puts Government in a precarious situation in the case of default by the supplier.

### ***Invoice dated before concluding Contract Agreement***

Whilst reviewing a Tender for the supply of ear tags for bovine and small ruminants, NAO noted that an invoice of €7,782 issued by the selected supplier on 11 February 2012, was dated prior to the evaluation decision taken by MRRA Departmental Contracts Committee, which was signed on 12 March 2012. The relative Contract agreement between MRRA and the selected supplier came into force as from 11 April 2012. Thus, it is clear that the supplier in question was engaged before the procurement process was concluded.

### ***Approval for Payment of Contributions not traced***

On 20 August 2013, the Ministry paid the annual contribution of €22,460 to an international organisation, located in Paris. On the same date, a minute in file from the Accounts Section MRRA, indicated that formal approval from the Permanent Secretary was to be sought prior to the payment of the relative invoice pertaining to the 2013 contribution. However, such approval could not be traced in file.

### ***Insufficient Details on Invoices and Payment Vouchers***

MSDEC is charged a monthly incineration fee by WasteServ Malta Ltd. in respect of animal by-product from the public abattoir, in accordance with established rates for the treatment of non-hazardous waste at the Thermal Treatment Facility. Rates, ranging up to €500 are in accordance with LN 203 of 2011.

During the testing of four invoices, in total amounting to €47,552, it transpired that the applicable rate charged by the provider was €50 per ton throughout. However, the invoices, as well as the relative PVs, did not indicate which category of waste was being disposed of, including the applicable rate charged. These lacked sufficient detail as required by Article 52(2) of the General Financial Regulations, stating that "All vouchers shall contain full particulars of each service, such as dates, numbers, quantities, distances and rates, so as to enable them to be checked without reference to any other document, and shall be accompanied by the relative invoices ...". Moreover, NAO could not trace any form of approval prior to the payment of such fees.

### ***Letters of Acceptance or Purchase Orders dated after Suppliers' Invoices***

In 48 cases tested, representing 56% of the sampled transactions, and amounting to €709,987, the respective LA or Purchase Order was issued following receipt of invoice, which implies that sufficient authority was not obtained prior to the purchase.

### ***Bank Guarantee not available***

Besides the two instances reported upon earlier in this write-up, another two cases were encountered, where the respective Bank Guarantee of 10%, as specified in the Contract agreement, was not traced in file. These related to awarded tenders whose value in aggregate totalled €351,564.

## **Compliance Issues**

### ***Lack of Compliance with Standing Travel Regulations***

Upon testing payments effected in relation to a trip abroad during 2013, it transpired that in the process of obtaining three quotations for the said travel, no quotation was obtained from Air Malta plc, as required by PSMC. In addition, the original invoice for three air tickets costing €3,600 was not traced in file.

## ***Non-submission of Fiscal Receipts or Tax Invoices***

From the audit sample selected, it transpired that a total of 17 transactions, representing 20% and collectively amounting to €360,002, were not supported by a valid fiscal receipt or tax invoice. In two of these cases where a tax invoice was presented, it was noted that both invoices did not comply with the specifications required in terms of VAT Act, since they failed to display the VAT Registration Number of MSDEC.

None of these defaulters were reported to VAT Department as required by MFEI Circulars No. 7/2011 and No. 2/2012. MSDEC also failed to submit the Quarterly Returns during 2013 as per aforementioned Circulars. This lack of compliance with existing directives indirectly contribute to a loss of revenue to the Government and the possible undeclared income by the service provider.

## **Recommendations**

### ***Key Issues***

#### ***Lack of Sufficient Audit Trail and Documentation***

All Government officials are to ensure that adequate and sufficient audit trail is kept without any exception or fail, not only to enhance accountability, but also to substantiate the transparency of the procurement process followed.

#### ***Retrospective Approval for Variation Order***

Prior to awarding tenders, proper planning, necessary on-site inspections, and designs of projects, are to be carried out by the Ministry, in order to minimise any substantial changes that may arise. It is imperative that variations for additional works, if required, are approved before tasks are actually executed and that such approvals are duly documented.

## ***Control Issues***

### ***Payments for Veterinary Services not substantiated***

The Ministry is expected to improve the manner in which information on the procurement process is held, in order to ensure transparency. All signed agreements are to contain the necessary detail, especially applicable rates to be charged by service providers.

In addition, a mechanism is to be in place to control the use of medicines and other consumables paid by the Ministry, based on the number of treated animals admitted to the Clinic. This will enable efficient monitoring and supervision on the service rendered and related costs disbursed from public funds.

### ***Non-adherence to Procurement Regulations***

Procurement regulations are to be invariably followed in order to ensure accountability and provide equal opportunity to all interested parties. This is also the only way to obtain the most competitive prices for goods and services.

### ***Non-compliance with Contract Agreement***

The terms and conditions outlined in the Contract agreement are to be fully respected. Any changes that occur thereafter are expected to be adequately documented and duly endorsed by both parties. Bank Guarantees should be renewed up till the instance when the contracted suppliers fulfill their obligations.

Moreover, the Ministry is to ensure that it has adequate controls in order to safeguard its interests, by verifying all invoices against the respective documentation before these are approved for payment. Any overpayments effected by the Ministry are to be recouped as expeditiously as possible.

### Invoice dated before concluding Contract Agreement

NAO strongly recommends that proper procurement procedures are followed. Thus, the service provider is only to be notified to deliver the service in question after the selection process has been successfully concluded and approved by the appropriate authority.

### Approval for Payment of Contributions not traced

Adequate approval from authorised official(s) is to be sought to substantiate any payment, including those covering membership fees.

### Insufficient Details on Invoices and Payment Vouchers

It is important that all invoices issued contain appropriate information that enables the Ministry to carry out the necessary verifications before processed for payment. Such payments are to be accompanied with proper authorisation.

### Letters of Acceptance or Purchase Orders dated after Suppliers' Invoices

Whenever possible, a LA or Purchase Order, as applicable, is to be raised before placing an order for works or services. This will ensure that proper authorisation for the purchase is obtained and adequate funds are committed to cover the expense.

Both the Procurement and Finance Departments are to insist that all documents are properly authorised and certified as necessary, to enhance the control on expenditure from public funds.

### Bank Guarantee not available

MSDEC is to ensure that suppliers honour the terms and conditions specified in the relative agreement, in particular by issuing the required Bank Guarantee on signing the Contract.

## Compliance Issues

### Lack of Compliance with Standing Travel Regulations

Officers entrusted with the responsibility of official visits are expected to adhere to the pertinent regulations to enhance accountability in relation to the expenditure incurred.

### Non-submission of Fiscal Receipts or Tax Invoices

In cases where VAT is applicable, MSDEC is to ensure that it is invariably issued with a valid fiscal receipt or a tax invoice by all suppliers, depending on the VAT status of the Ministry. Management is also to ascertain that applicable regulations are adhered to, and complete returns are submitted to VAT Department on a regular basis to report defaulters.

## Management Comments

Management comments were received from MSDEC following a number of period extensions granted to the said Ministry by NAO to submit its response on the concerns that were raised. An exit meeting was subsequently also held to discuss Management's feedback.

In its reply, the Ministry reiterated the fact that MSDEC was only set up as a distinct Ministry in mid-March 2013, and it had to resort continuously on the support services structure and resources of the former MRRA, which were primarily retained at MTI. It was also remarked that despite their wide responsibilities, complexities and high level of European Union regulations, MSDEC line Departments, such as Rural Development as well as Veterinary and Animal Welfare, do not have a separate Recurrent Vote. Thus, upon the setting-up of MSDEC, such Departments did not have the necessary resources to stand up on their own, since the centralised support they were used to receive from MRRA was no longer available. In addition, it was claimed that with regard to its environment

and climate change responsibilities, which were previously the remit of the former Ministry for Tourism, Culture and the Environment, MSDEC did not inherit any proper structure.

A summary of other comments provided are listed hereafter:

### ***Limitations on Scope of Audit***

According to Management, since the missing PVs were primarily related to Transfer Schedules between MSDEC and MTI, the associated risks to public funds are minimal. At the time when MSDEC Accounts Section was practically inexistence, these Schedules were raised by MTI staff, who had full access to MSDEC accounts.

With regards to the encountered inconsistencies in the VAT status of MSDEC, Management stated that following the new set-up, MTI continued to make use of the former MRRA VAT Number, whilst MSDEC sought to revert to the VAT Number used up till 2008 by the then MRRA. To-date, the necessary verification and liaison with VAT Department to re-activate this number was not carried out, but is now in the process of being resolved.

### ***Lack of Sufficient Audit Trail and Documentation***

This Ministry is seeking to locate any missing documentation from 2010 and 2011 files, to ensure that a proper audit trail is maintained and that payment verification may take place.

### ***Retrospective Approval for Variation Order***

The Ministry acknowledged that the former MRRA should have requested prior approval in terms of PPR and that approved variations should have been published in the Government Gazette.

### ***Payments for Veterinary Services not substantiated***

According to MSDEC, the cost to Government, covering the selected clinic, remains significantly lower than the administratively and technically compliant offers submitted for the expression of interest.

Meanwhile, the Directorate is not in a position to verify whether all medicines and consumables listed on the individual invoices have actually been utilised, since this would necessitate the employment of at least four officers with a veterinary background to monitor the administration of treatment. The price-list forwarded to NAO was the original list submitted at the time of the signing of the Agreement, which was not included in the Agreement and Memorandum of Understanding.

### ***Invoice dated before concluding Contract Agreement***

Management stated that this case is considered as a genuine mistake in invoice date, which was overlooked by the Accounting Officer. All verifications conducted by the Department indicate that the earliest purchases were made in August 2012, and that the respective invoice was dated 9 September 2012.

### ***Insufficient Details on Invoices and Payment Vouchers***

The Ministry claimed that since invoices pertaining to incineration fees are duly certified by Management at the public abattoir, no additional approvals are deemed necessary prior to settlement of the amount due.



### ***Lack of Compliance with Standing Travel Regulations***

MSDEC confirmed that the failure to obtain a quote from Air Malta was a genuine error from the Officer's side, who was new to the job.

### ***Concluding Remarks***

Despite the shortcomings inherited from former MRRA, and notwithstanding the fact that a strong support services function is still in the process of being developed at MSDEC, the Ministry is still committed to utilise the Audit Report as a basis for improvement, in a bid to avoid a recurrence of the shortcomings flagged by NAO.

Management comments made no reference to observations raised under the following titles and sub-headings:

- Non-compliance with Contract Agreement
  - Time Limit as per Contract not respected
  - Bank Guarantee not renewed
- Letters of Acceptance or Purchase Orders dated after Suppliers' Invoices
- Bank Guarantee not available
- Non-submission of Fiscal Receipts or Tax Invoices



Ministry for Transport and  
Infrastructure

# Enhancement of Public Areas

## Capital Expenditure

### Background

The Ministry for Transport and Infrastructure's (MTI) approved budget allocation in respect of Item 7044 'Enhancement of Public Areas' for 2013, stood at €1,600,000, a decrease of €200,000 from the previous year's allocation.

On 2 August 2013, approval was obtained from the Ministry for Finance (MFIN), whereby the budgetary provision under Item 7044 was augmented by a further €1,500,000. This increase was granted for the purpose of meeting expenditure in respect of the Cospicua Dock No. 1 Project. However, during the year, MTI's budget for the Enhancement of Public Areas was revised downwards by €200,000, thus resulting in a final allocation of €2,900,000.

In 2013, MTI paid €2,554,581 out of the revised budget allocation, 77% of which were expensed on Contractual Services, €1,971,110, followed by Operating Materials and Supplies, €445,474, Overtime, €106,746 and Lease of Equipment, €31,246.

### Audit Scope and Methodology

The main scope of the audit was to ensure that capital expenditure on the Enhancement of Public Areas, incurred by MTI during 2013, was appropriately recorded and processed according to the General Financial Regulations, 1966 and other pertinent Regulations and Circulars. The

adequacy of adopted procedures in procurement, as well as compliance with the Public Procurement Regulations, 2010, and any Legal Notices issued thereafter, was also ascertained.

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.

The list of projects whose expenditure was charged to Item 7044 'Enhancement of Public Areas' was obtained from MTI. Although in the year under review, expenditure on these projects included materials, labour and hire of plant, testing focused on payments for contractual services, being the most material item of expenditure.

Audit work ultimately covered a sample of 43 transactions, totalling €770,891, charged to the Contractual Services Account. These transactions related to nine agreements covering the procurement of contractual services, as well as two contracts which related to consultancy services.

### Key Issues

#### *No Departmental Call for Tenders issued for Procurement of Consultancy and Project Management Services*

- a) The Service Contract Agreement, entered into between MTI and an Architect, for the

provision of consultancy services during 2013, covered a period of 12 months and was for the equivalent of €60,000 exclusive of Value Added Tax (VAT). No departmental call for tenders was issued in respect of these services, as, according to the Ministry, the incoming administration wanted to ensure that no European Union (EU) funds earmarked for the Cospicua Dock No. 1 Project would be lost. Instead, the Architect was engaged directly from the open market, by means of MFIN approval.

- b) Similarly, no departmental call for tenders was issued prior to procuring the professional services of a Project Manager<sup>1</sup>. The respective agreement covered a period of 35 weeks, commencing on 2 April 2013, at a retainer fee of €600 (VAT excl.) per week, thus leading to a total contract value of €21,000 (VAT excl.). These project management services were procured following a direct order approval obtained the day following the commencement date of the agreement.

### *Retrospective Approvals for Direct Order*

- a) MTI requested direct order approval to procure the services of the above-mentioned Architect on 2 May 2013, with MFIN granting its authorisation on 21 May. However, since the Agreement with the consultant was effective from 14 March 2013, National Audit Office (NAO) concluded that the approval was requested when MTI had already placed a commitment with the service provider.
- b) On 1 April 2013, MTI requested authorisation from MFIN to place a direct order with the Project Manager, for services costing €21,000 (VAT excl.). The Agreement was entered into the next day. No other correspondence from MFIN was traced in file, other than the direct order approval which was granted ‘in principle’ on 3 April. Therefore, once again, MTI entered into a commitment before the necessary approval was obtained.

MTI had to revert to MFIN for a definite approval once the actual cost was established. The actual definite approval was obtained on 1 October 2014, at a maximum amount of €21,000 (VAT excl.).

## **Control Issues**

### *Service Contract Agreement with Architect providing Consultancy Services*

#### **Inconsistencies between Contract Agreement and the respective Direct Order Approval**

A review of the agreement for the provision of consultancy services during 2013 and the respective direct order approval obtained from MFIN, revealed a number of inconsistencies. The granting of a disturbance allowance, car cash allowance and free mobile facilities, although authorised by MFIN, were not specifically mentioned in the consultant’s agreement<sup>2</sup>. Apart from being subject to different interpretations, such inconsistencies resulted in additional requests for direct orders, leading to overspending of public funds, as detailed in the following observation.

#### **Amount approved by Direct Order exceeded**

As mentioned previously, the approval for placing a direct order in respect of consultancy services rendered by the Architect during 2013, was to cover a 12-month period commencing from 14 March 2013, and for a maximum contract value of €60,000 (VAT excl.).

Following receipt of invoices for services carried out between September and 17 November 2013, as well as car and mobile allowances granted during the same period, MTI realised that the value of the direct order was going to be exceeded. Consequently, it referred to MFIN for approval to settle outstanding amounts due to the Architect. Finance approval was obtained for an additional amount of €27,172, and all pending invoices were settled. In its approval, MFIN stated that “... *this authorisation is not construed as being any form of direct order approval (implied or otherwise)*”

<sup>1</sup> When queried on this engagement, MTI explained that the Project Manager was recommended by the Architect.

<sup>2</sup> The 2013 Contract Agreement stipulated that “*The Service Provider shall not be entitled to any other benefit unless requested and agreed upon in writing by the Permanent Secretary (MTI) or his appointee*”.

which would not be covered by the Public Procurement Regulations, but is only meant to settle any outstanding dues”.

In total, the Architect was paid €95,804, thus exceeding the value of the direct order by €25,004. This translated in an excess of 35%.

#### Excessive ‘After Office Hours’ claimed by the Service Provider

According to the direct order approval dated 21 May 2013, the Architect was to be paid a retainer fee of €45 (VAT excl.) per hour, up to a maximum of 40 hours of service per week. He was also entitled to a disturbance allowance of 15% of the hourly rate (*i.e.* €51.75 (VAT excl.)) for work carried out after office hours. MFIN approval specified that this 15% premium was to be levied in exceptional circumstances.

An examination of the 2013 invoices under review revealed that out of a total of 1,684 hours performed by the service provider, 429 hours (*i.e.* 25%) were claimed as carried out after office hours.

Consequently, from the total of €95,804 billed by the Architect, €26,166 (*i.e.* 27% of amount paid) was incurred by MTI for hours claimed at the disturbance rate of €51.75 (VAT excl.). Therefore, it is evident that the incidence of charge of the 15% disturbance allowance was not applied solely in ‘exceptional circumstances’, thus going against MFIN’s recommendation.

#### Overpayment of Mobile Facilities

During 2013, the Architect enjoyed free mobile facilities for the equivalent of €691. However, since in the mentioned year, the consultant performed his duties for a period of eight months, the Architect should have been entitled to €544 (based on the annual threshold of €815). Therefore, the reimbursed amount exceeded the entitlement by €147.

#### Works in connection with Dangerous Structure re Falling Rocks near Bathing Area at West Cove Ghar Lapsi, Siggiewi

Engagement of Contractor not covered by a Formal Agreement and a Performance Guarantee

No agreement was entered into between MTI and the foreign company entrusted to carry out stabilisation works to the dangerous rock formation at the West Cove area at Ghar Lapsi. Although both the contract price of €146,550<sup>3</sup> (VAT excl.) and the completion period for the required works were communicated to the contractor through the Letter of Acceptance, this document was not endorsed by the latter. Details on the terms of engagement, such as applicable penalties in case of non-satisfactory works or delay in delivery, were also not formalised and agreed upon by the contracting parties. Furthermore, MTI failed to request the contractor to submit a Performance Guarantee, intended to protect the Ministry’s interests in case the obligations under the agreement for works were not duly performed.

While MTI justified the absence of a Performance Guarantee by claiming that payments are only carried out on satisfactory completion of works, an interim payment of €52,345 (equivalent to 36% of the actual contract cost) was issued.

#### Letter of Acceptance issued prior to obtaining Permit

On 23 May 2013, the Malta Environment and Planning Authority (MEPA) granted MTI permission to carry out stabilisation works. However, MTI’s application was received by MEPA on the same day on which the Letter of Acceptance of direct order was issued to the company performing the works, implying that the commitment was made with the contractor before the necessary permits to carry out the stabilisation works were obtained.

<sup>3</sup> This was corrected to €146,883 (VAT excl.) in a second Letter of Acceptance issued on 10 July 2013.

### Incorrect Contract Value quoted in Request for Direct Order Approval and Letter of Acceptance, leading to Overpayment

- a) Following a decision to upgrade the type of rock bolts to be used in the stabilisation interventions at the West Cove of Ghar Lapsi, a second request for direct order approval was submitted to MFIN to cover the increase in cost. The additional cost was erroneously indicated as €2,183 (VAT excl.) instead of €1,850 (VAT excl.), and the authorisation issued on the former amount. The Letter of Acceptance was also reissued to indicate that the total price was to read €146,883 (VAT excl.). Thus, both the approved cost and the total contract price were inflated by €333, plus the VAT element.
- b) The inflated cost of the rock bolts utilised on the project was reflected in the final Bill of Quantity (BOQ) prepared by MTI prior to effecting payment to the contractor. As a result, the latter was overpaid €348, while the VAT paid on the total cost of the project was also inflated by €63.

During the audit, this overpayment was brought to MTI's attention. A refund was claimed and eventually received from the contractor.

### Water Feature in Dunes Area at the Cottonera Dock No. 1 Project

#### Payment for Variations prior to obtaining Approval

The payment claim of €21,145 in respect of works carried out on the water feature in the dunes area at the Cottonera Dock No. 1 Project included a charge for quantities, for the value of €239, not included in the original BOQ. MTI effected the respective payment, in spite of the fact that the approval for this variation was not yet obtained. Although the amount in question was not material, similar practices of meeting contractors' claims for payment for unapproved quantities could result in control over the project cost being lost.

### Expired Performance Guarantee

The one-year Performance Guarantee submitted by the selected bidder following the adjudication of the Tender for the water feature expired before the project was in fact completed. No renewal of this Guarantee was traced to the respective file.

### Non-compliance with Tender Document Requirements

Although required by the Tender document, the selected bidder failed to attach the proof of purchase, *i.e.* a copy of the receipt issued by the Cash Office when purchasing the Tender, to the respective offer. This omission seems to have gone by unnoticed by the Tender Evaluation Committee (TEC), who failed to request the bidder to rectify the situation and submit the missing documentation within two working days from notification. Such rectification should have triggered the payment of a non-refundable administrative penalty of €50, whilst failure to comply would have resulted in the submitted Tender not being considered further.

The contractor also failed to submit a sample of the synthetic fibre reinforcement, as well as the 'Programme and Method Statement for Concrete Work' with the Tender bid. These omissions might have resulted in the respective offer not being considered further. Although MTI claimed that concrete works were discussed in detail with the contractor, and documentation indicating details of the concrete mix design were presented during the course of works, compliance with materials requirements and design should have been ensured at the outset.

### Incorrect Calculation of Payment due and related Shortcomings

The BOQ supporting the second claim for payment in respect of the water feature at the Cottonera Dock No.1 was prepared by the contractor himself, and evidenced no endorsement by the Engineer in charge of the project. Mathematical errors in this BOQ led to the total due to the contractor being overstated by €1,057. In fact, the contractor claimed payment of €13,050 when the total invoice amount should have read €11,993.

The certificate for payment issued by the Quantity Surveying Section, following the preparation of the BOQ, confirmed the amount due to the contractor as €13,050 and payment was effected accordingly. However, it was apparent that figures quoted in this certificate were increased in order to compensate for the errors made by the contractor when preparing the BOQ. This ensured that the total amount due as per certificate tallied with the invoice amount, which was already established.

### *Archaeological Monitoring Services at the Mtarfa Play Area*

#### *Substantial Cost Variances incurred and Retrospective Approval*

The contract for the procurement of archaeological monitoring services at the Mtarfa Play Area, awarded following the issue of a departmental call for quotations, was for the value of €6,000. However, the amounts paid to the contractor totalled €15,473, thus resulting in an adverse variation of €9,473, equivalent to 158% of the contract value.

Approval for the variations was sought and obtained only after the respective invoices were issued, and therefore by the time works were already carried out.

#### *No retention of Documentation in support of Hours charged by Contractor*

According to MTI, hours billed by the contractor for archaeological monitoring works were tallied against hours recorded on site by the Ministry's foreman, to ascertain the accuracy of amounts charged. However, this claim could not be corroborated since, when the respective documents were requested for audit purposes, they could not be traced.

### *Supply and Installation of Mechanical and Electrical Services at the Mtarfa Play Area*

#### *Shortcomings in Tender Rectification Procedure*

- a) One of the bidders for the Tender for the supply and installation of mechanical and electrical services at the Mtarfa Play Area, failed to include technical literature when

presenting the Tender document. Following an electronic notification of this omission, sent by MTI, the bidder submitted the required documentation within the stipulated deadline.

However, whilst rectification was permissible, TEC should have requested it only after having obtained approval from the Departmental Tenders Committee. This shortcoming was also remarked by the Departmental Contracts Committee.

- b) Furthermore, this rectification was subject to a non-refundable administrative penalty of €50. However, no evidence of such payment by the bidder was traced to the respective file.

#### *Sanitary Ware purchased not utilised on Project*

- a) Although the contract for the mechanical and electrical works included the supply of sanitary ware and plumbing works, following MTI's decision to reduce costs, plumbing works were carried out by the Manufacturing Services Directorate (MSD). Since the cost of each sanitary ware item, as indicated in the Tender, was inclusive of installation costs, the prices actually charged by the contractor were in fact less than those agreed upon. However, no quotation was obtained from the contractor identifying the price of each sanitary item net of installation costs. MTI stated that the rates for each item were established by the Quantity Surveying Section, based on the contractor's own submissions, as well as on verbal agreements made.
- b) Furthermore, none of the sanitary ware purchased from the contractor awarded this Tender was used on the Mtarfa Project. In fact, all items were delivered to the Mrieħel Stores and were expected to be utilised on other unspecified projects. The Architect in charge of the Mtarfa Project stated that, since MSD was responsible for the plumbing works, the Directorate bought the sanitary ware which it deemed were best suited for the fittings being utilised. The invoice forwarded to NAO in this respect indicated

the purchase of a number of sanitary ware items costing €1,747. However, this invoice was dated seven weeks before the issue of the Letter of Intent following the awarding of Tender for mechanical and electrical works, thus raising doubt on whether it truly related to the sanitary ware purchased and installed on the Mtarfa site.

### Goods Received Notes not issued by the Mriehel Stores

The delivery of the above-mentioned sanitary ware to the Mriehel Stores was not supported by a Goods Received Note<sup>4</sup>. In fact, MTI confirmed that Notes are only issued when goods are taken out of the Stores. The absence of Goods Received Notes suggests that a weak stock control system is in place at the Mriehel Stores. This might lead to lost, misplaced or even stolen items going by unnoticed.

### Construction of Water Culvert for Flood Relief at Triq Saver Zarb, San Ġwann

#### Error in Tender Document leading to Variation<sup>5</sup>

Approval for a variation of €6,160, equivalent to 9.43% of the original contract value, was requested only four days after the issue of the formal 'Order to Start Works'. This variation was attributed to a typing error in the Tender document.

#### Non-compliance with Conditions set out in the Letter of Intent

Although the Letter of Intent required the contractor to furnish a Performance Guarantee of €6,531 valid for 12 months, the submitted Guarantee only covered a six-month period.

Furthermore, the contractor was to sign the Agreement within five working days from the date of the Letter of Intent, *i.e.* by 10 December 2012. However, the agreement was endorsed on 26 December.

### Service Contract Agreement with Project Manager

#### Lack of Supporting Documentation

The Contract Agreement entered into with the Project Manager mentioned earlier under the first 'Key Issue', outlined a list of services that were to be carried out. Apart from the report drawn up by the service provider 15 days following his engagement, no other reports were made available for audit purposes. Therefore, it could not be ascertained that the services rendered by the Project Manager were actually performed and that these were satisfactory.

#### Weaknesses in the Contract Agreement

- a) The contract for the procurement of project management services was drawn up by the Project Manager, as clearly indicated on the direct order request which MTI sent to MFIN on 1 April 2013. Thus, it may be implied that MTI accepted the terms and conditions outlined by the service provider. It also cannot be excluded that certain clauses might have been advantageous to the contractor, while deemed unfavourable to MTI.
- b) The contract was for a duration of 35 weeks, at a retainer fee of €600 (VAT excl.) per week. However, the number of hours to be performed by the service provider were not stipulated in the Contract Agreement.

### Shortcomings common to Various Projects

#### Arithmetical Errors in estimated Project Costs

- a) According to the Tender Originators Form, the 'Construction of Water Culvert for Flood Relief at Triq Saver Zarb, San Ġwann' was estimated to cost the then Ministry for Resources and Rural Affairs (MRRA) €72,334. However, the aggregate of the detailed itemised estimate totalled €74,834, thus resulting in a difference of €2,500.

<sup>4</sup> Confirmation was done through endorsement of the Delivery Note issued by the supplier and a minute in the respective file.

<sup>5</sup> In spite of this variation, overall savings of 2.93% resulted by the end of the project.



- b) Similarly, the itemised estimate prepared by the then MRRA, prior to issuing the departmental tender for the provision of ‘Mechanical and Electrical Works in connection with the New Civic Centre and Recreational Area at Swieqi’, was understated by €10,145, due to arithmetical errors.

This error led to an inadequate method of procurement utilised by the Ministry, since the correct estimate should have solicited procurement through the Department of Contracts, in accordance with the Public Procurement Regulations, rather than an issue of a departmental call for tenders.

### Unreliable Estimates prepared by MTI

The actual contract value of eight agreements for the provision of contractual services, and for which an estimate was prepared by MTI prior to the issue of tender or quotation<sup>6</sup>, differed from the projected cost. These variances ranged from a 244% increase over MTI’s estimate, to a contract value of 30% less than the projected cost. Underestimation of projected costs could result in a strain on the financial position of the Ministry during the year, possibly disrupting the execution of other scheduled projects.

### Differences between Contract Values and Actual Payments

Apart from one case where the actual total payments exceeded the original contract value by 158%<sup>7</sup>, in the remaining seven sampled agreements<sup>8</sup>, MTI experienced positive variations. These savings on contract costs ranged from less than one percent to over 30%. Reasons for such variations included works forming part of the original Tender eventually carried out by MSD, amounts included in Tender document for contingency purposes not utilised, differences in quantities and types of materials used, as well as errors in calculations and inexact estimates.

While cost savings can be viewed as an advantageous situation, these are actually unutilised committed funds which could have been efficiently invested in other projects.

### Delays in Completion of Works

Contractual services provided through seven out of the nine agreements selected in the audit sample were not concluded within the stipulated timeframe. Delays ranged from less than one week to 54 weeks.

Except for two cases, where the call for quotations and Tender document did not include clauses for delays in performance, no penalties in respect of late completion were charged to the respective contractors. According to MTI, in the remaining five cases, the late delivery was justifiable and therefore, the penalty clause included in the Tender document was not applied.

Notwithstanding this, none of the above-mentioned contracts was formally extended to cover the prolonged contract period.

### Late Communication of ‘Order to Start Works’

Out of the nine agreements relating to the provision of contractual services, three instances were noted whereby the respective contractor was formally notified of the date of commencement of works, after such date had already elapsed.

### Minister’s Approval not traced

Requests for Minister’s approval in respect of expenditure on goods, works and services were raised by MTI prior to issuing two Tenders for paving works on the dunes area at the Cottonera Dock No. 1 Project, estimated at €119,923 and €70,088, respectively. However, both requests traced in the Ministerial file featured up to the Permanent Secretary’s signature, but both lacked the Minister’s signature. The absence of the latter endorsement implies that the intended appropriate authorisation for the respective expenditure was not obtained.

<sup>6</sup> No estimate was prepared prior to awarding the contract for the provision of works in connection with the dangerous structure at Ghar Lapsi.

<sup>7</sup> This variation was incurred on the archaeological monitoring services at the Mtarfa Play Area.

<sup>8</sup> Only those projects, which were fully paid by the time of audit, were considered for this test.

### Uncommitted Funds on Consultancy Services due to lack of awareness

- a) The contract between MTI and the Architect mentioned earlier on in this Report was brought to the Ministry's Accounts Section's attention more than three months after the agreement was entered into. This was confirmed through correspondence between the Director General (Support Services) and the Permanent Secretary. As a result, the funds covering the projected cost up to the end of the year were not committed by the aforementioned date.
- b) Similarly, as evidenced by correspondence in the respective file, the Director General (Support Services) was made aware of the agreement entered into with the Project Manager two months after the contract's effective date. Funds were once again not timely committed in the appropriate Line Item, and could have resulted in MTI not having enough funds to honour the actual expense.

## Compliance Issue

### *Defaulters' Lists not submitted to VAT Authorities*

MTI verbally confirmed that quarterly lists of fiscal defaulters were not submitted to VAT Authorities, as per the Ministry of Finance, the Economy and Investment (MFEI) Circular No. 2/2012.

## Recommendations

### *Key Issues*

#### No Departmental Call for Tenders issued for Procurement of Consultancy and Project Management Services

Procurement regulations are to be invariably followed in order to ensure transparency, as well as to provide equal opportunity to all interested

parties, and obtain the most competitive prices for goods and services. MTI is to ensure that direct order approvals are resorted to only in exceptional circumstances, as specified in MFIN Circular No. 3/2013 'Public Procurement Regulations – Direct Orders'.

### *Retrospective Approvals for Direct Order*

MTI is to refrain from entering into commitments with service providers unless all the necessary approvals have been timely obtained.

### *Control Issues*

#### *Service Contract Agreement with Architect providing Consultancy Services*

##### *Inconsistencies between Contract Agreement and the respective Direct Order Approval*

MTI is to ensure that, where applicable, the direct order approval is obtained prior to entering into a contract agreement, whilst the agreement is to reflect the same contract price, terms and conditions set out in the respective approval.

##### *Amount approved by Direct Order exceeded*

When drafting agreements, MTI is to ascertain that the contract value realistically reflects the service which is expected to be provided, thus reducing the necessity to request additional funds.

##### *Excessive 'After Office Hours' claimed by the Service Provider*

MTI is to exercise more control over similar contracts in the future, in particular when resorting to extra hours.

##### *Overpayment of Mobile Facilities*

Free mobile facilities, under whatever form of contract or authority, are to be regulated by the ceiling as established in MF Circular No. 4/2002. MTI is to recoup the extra amounts reimbursed to this consultant.

### Works in connection with Dangerous Structure re Falling Rocks near Bathing Area at West Cove Għar Lapsi, Siggiewi

#### *Engagement of Contractor not covered by a Formal Agreement and a Performance Guarantee*

All services purchased by MTI are to be duly backed by signed agreements between the parties involved and supported by Performance Guarantees, where applicable. The conditions of service, the duration of the contract, as well as applicable penalties in case of default, are to be clearly spelled out in the agreement. Both contracts and Performance Guarantees are to be retained by the Ministry for future reference.

#### *Letter of Acceptance issued prior to obtaining Permit*

MTI is to ensure that it duly and timely obtains the necessary permits as required by law, both before works are executed and the respective contracts entered into.

#### *Incorrect Contract Value quoted in Request for Direct Order Approval and Letter of Acceptance, leading to Overpayment*

While the unintentional error was acknowledged by MTI after this was brought to its attention by NAO and the situation was rectified, more care is to be taken when quoting and/or calculating contract prices, to avoid similar overcharging.

### Water Feature in Dunes Area at the Cottonera Dock No. 1 Project

#### *Payment for Variations prior to obtaining Approval*

Materials purchased or works carried out not included in the original Tender document are to be duly authorised prior to being procured or executed by the contractor.

#### *Expired Performance Guarantee*

MTI is to ensure that, whilst selected bidders are to be requested to duly submit Performance

Guarantees as and when required, these Guarantees are to cover the entire contract period. If this period elapses and works are still in progress, extensions to the Guarantees are to be requested from the respective contractors as necessary.

#### *Non-compliance with Tender Document Requirements*

When evaluating Tender documents, TEC is to ensure that all required documentation and samples, where applicable, are duly and timely submitted. In case of non-compliance, the procedure indicated in the Tender document is to be invariably followed and action taken accordingly in line with procurement regulations.

#### *Incorrect Calculation of Payment due and related Shortcomings*

The Architect or Engineer in charge of projects is expected to prepare BOQs as necessary, clearly indicating the value of works carried out. Whilst these BOQs are to be duly endorsed, MTI is to ensure that payments effected to contractors reflect the approved works to-date.

### Archaeological Monitoring Services at the Mtarfa Play Area

#### *Substantial Cost Variances incurred and Retrospective Approval*

While it is acknowledged that, given the nature of work required, archaeological services can be unpredictable, MTI is to, as far as possible, try to avoid incurring hefty negative variances. This can be partly achieved through appropriate planning prior to issuing calls for quotations and/or tenders, as well as by ensuring that the Tender document and work specifications include all materials and services necessary for the satisfactory execution of the project.

In the event that variations to projects are unavoidable, approval to increase the project cost is to be requested and duly obtained before works are carried out.

*No retention of Documentation in support of Hours charged by Contractor*

All relevant documentation is to be attached to the respective invoices and systematically filed for future reference, thus enabling possible independent verification by third parties.

*Supply and Installation of Mechanical and Electrical Services at the Mtarfa Play Area**Shortcomings in Tender Rectification Procedure*

All clauses of the Tender document are to be strictly adhered to by MTI, to ensure fair competition, as well as transparency in the tendering process.

*Sanitary Ware purchased not utilised on Project*

- a) Justifiable price variations from the Tender document are to be supported by quotations or similar documents, endorsed by the contracting parties. MTI is also to ensure that the new prices are reasonable and competitive.
- b) MTI is to refrain from purchasing items unless it is certain that they will be utilised for the intended purpose.

*Goods Received Notes not issued by the Mriehel Stores*

MTI is to insist that, whilst pre-numbered Goods Received Notes are issued by the Mriehel Stores, these are backed by an efficient and reliable stock control system.

*Construction of Water Culvert for Flood Relief at Triq Saver Zarb, San Ġwann**Error in Tender Document leading to Variation*

The Tender document is to be thoroughly reviewed prior to being issued, so as to avoid, as much as possible, having to effect changes after it has been awarded.

*Non-compliance with Conditions set out in the Letter of Intent*

MTI is to ensure that contractors invariably comply with all the conditions laid down in the respective Letter of Intent.

*Service Contract Agreement with Project Manager**Lack of Supporting Documentation*

Any reports or written recommendations drawn up by the Project Manager are to be retained and duly filed for ease of reference and possible verification by third parties.

*Weaknesses in the Contract Agreement*

All contract agreements are to be drawn up and formalised by MTI itself, as well as scrutinised by a legal officer, independent from the selected service provider. Expected hours of work, remuneration, perks and all terms and conditions, are also to be clearly outlined.

*Shortcomings common to Various Projects**Arithmetical Errors in estimated Project Costs*

Since project estimates very often are crucial in selecting the procurement procedure to be followed, MTI is to ensure that these are thoroughly checked to reduce the incidence of mathematical errors.

*Unreliable Estimates prepared by MTI*

Prior to establishing project estimates, detailed research is to be carried out by MTI, so as to approximate the contract value, thus ensuring the efficient use of public funds.

*Differences between Contract Values and Actual Payments*

Amounts paid for goods and services are to compare, as much as possible, to the cost agreed upon in the respective contract. Project planning is to be given the required importance, so as to reduce the occurrence of significant variations and inefficient utilisation of public funds.

### *Delays in Completion of Works*

Whilst contract periods are to be adhered to as much as possible, penalties detailed in the respective Tender document are to be charged whenever delays in completion of works are not justifiable. MTI is also to ensure that all Tender documents include clauses specifically outlining the applicable penalties when the stipulated target dates are not reached.

Furthermore, extensions to contracts are to be agreed upon by the contracting parties and duly documented.

### *Late Communication of 'Order to Start Works'*

MTI is to ensure that a formal 'Order to Start Works' is timely issued for all agreements for contractual services.

### *Minister's Approval not traced*

All requests raised prior to procuring goods and services are to be approved by the appropriate level of authority, and all documentation retained for future reference.

### *Uncommitted Funds on Consultancy Services due to lack of awareness*

MTI's Finance Department is to be duly informed of known expenditure prior to commitments being made with the respective contractors, suppliers and service providers, thus ascertaining the availability of funds and that payment requests can be met, without unnecessary delay, when they fall due.

### *Compliance Issue*

#### *Defaulters' Lists not submitted to VAT Authorities*

Whilst MTI is to ensure that it is invariably issued with tax receipts, defaulting suppliers are to be reported in the quarterly VAT defaulters' lists, as per MFEI Circular No. 2/2012. In the event that it identifies no VAT defaulters, a 'Nil' return is still to be submitted to VAT authorities, as per the foregoing Circular.

### **Management Comments**

Whilst thanking NAO for its valid comments, Management undertakes to effect the recommendations. In fact, Management concurred with a number of NAO observations and commented that corrective measures were already taken to comply accordingly. These included:

- setting up a National and EU Projects Monitoring Committee, as well as a Budgetary Monitoring and Advisory Committee, as measures of control over expenditure and overseeing project management;
- issuing a reminder Circular on the obligations of requesting a Performance Guarantee from contractors awarded a direct order exceeding the threshold value;
- circulating a Memo reminding officers of the procedures to be followed in requesting quotations, financial approvals, as well as variations and extensions to contract agreements;
- releasing another Internal Memo, targeted at officers within the Project Design and Engineering Directorate, highlighting NAO's observations and the required course of action on inaccurate tender estimates and quantities, late communication of 'Order to Start Works', delays in completion of works and applicable penalties, variations and contract extensions; and
- requesting a clarification meeting with VAT Department in order to discuss compliance issues relating to MFEI Circular No. 2/2012.

However, Management expressed its reservations on NAO's observations relating to the consultancy services provided by the Architect and Project Manager. MTI claimed that it would have been more pertinent for NAO to audit the entire Cospicua Dock No. 1 Project, which is an EU funded project, rather than considering expenditure, such as payments to the above-mentioned Architect and Project Manager, separately. At the same time, Management reiterated that EU funded projects are constantly being audited by various entities,

including the Ministry itself, the Planning and Priorities Coordination Division and the Internal Audit and Investigations Department.

Management was also in disagreement with NAO's observation on the differences between the Architect's Contract Agreement and the respective direct order approvals, since it claimed that the *"Extra allowances, perks etc. were subject to negotiation based on performance..."*. Furthermore, it insisted that a distinction is to be made between normal contractual works and services usually paid under Capital Vote Item 7044, and commercial architects paid in the EU projects scenario. According to Management *"Experience reveals that these are two separate markets even though the contracting authority remains the same"*.

However, NAO differs from the above-mentioned opinions. The audit was performed on expenditure charged to Capital Vote Item 7044, which included payments to the said Architect and Project Manager. Contrary to Management's claim, the benefits granted to the Architect were not related to performance, but merely subject to approval by the Permanent Secretary or his appointee. In addition, contracts charged to the Capital Vote are not to be treated differently from those relating to EU funded projects.

As regards the missing documentation relating to the hours billed by the contractor in respect of archaeological monitoring services, these were traced by MTI and forwarded to NAO subsequent to the audit. On the other hand, although Management confirmed that it is in possession of relevant documents pertaining to the actual service provided by the Project Manager, these were still

not submitted to NAO with the Management Comments. In respect of NAO's observation regarding the overpayment of mobile facilities to the Architect, amounting to €147, although MTI did not concur with NAO's workings, it made the necessary arrangements and recouped the said amount.

Furthermore, Management failed to address the following NAO observations:

- Letter of Acceptance issued prior to obtaining permit
- Non-compliance with Tender document requirements
- Incorrect calculation of payment due and related shortcomings
- Substantial cost variations incurred and retrospective approval
- Shortcomings in Tender rectification procedure
- Sanitary ware purchased not utilised on project
- Goods Received Notes not issued by the Mriehel Stores
- Weaknesses in the Contract Agreement
- Minister's approval not traced
- Uncommitted funds on consultancy services due to lack of awareness





Ministry of Gozo



# Gozo Channel Company Limited

## Background

Gozo Channel Company Limited (GCCL) was formed in 1979, and is fully owned by the Malta Government Investments Ltd.

In April 2004, it was awarded a direct contract through the then Ministry for Competitiveness and Communication, to provide sea transport services as stipulated in the Public Service Obligations (PSO) set out in the same contract, which was valid for a period of six years. On expiry of this contract, following a public call for tenders by the Government of Malta, GCCL, in a joint venture with Gozo Ferries Company Limited (GF), was awarded a Public Service Concession Contract (PSCC) for the exclusive provision of services between the ports of *Ċirkewwa* and *Mġarr*, and the non-exclusive provision of the services between the ports of *Valletta/Marsamxetto* and *Mġarr*, for a further period of six years, with effect from 30 September 2011.

This joint venture agreement, entered into by the parties on 15 March 2011, stipulates that the vessels, owned by GF, will be delivered to GCCL for the exclusive employment thereof, in the provision of services pursuant to PSO. No hire or additional fees and/or consideration are due by GCCL in respect of the chartering of the vessels. However, compensation is due to GF, which compensation amounts to 85% of the joint venture free cash flow.

## Statistics and Financial Performance

According to Management Accounts' figures, 19,431 trips were performed on the *Ċirkewwa* route during 2013, while 199 trips took place on the *Sa Maison* route. The number of passengers and vehicles making use of GCCL's services during the same period amounted to 4,396,583 and 1,186,544 respectively, registering increases of 7% and 9% over the same figures for 2012.

During the year under review, GCCL managed to reduce the loss of €1,670,835 registered in 2012, by €635,583, *i.e.* 38%, ending 2013 with a net loss of €1,035,252. The Company registered a profit between May and October (both periods included). However, from a profit of €26,579 in October, it suffered a loss of €283,973 in November. Further analysis revealed that the Company only made a monthly profit when ticket sales revenue (net of discounts payable) for that particular month exceeded €900,000.

Net revenue generated by the Company during 2013 amounted to €12,238,658, of which €10,899,620 and €695,564, *i.e.* 89% and 6% were derived from the sale of tickets and PSO contribution respectively. The other income was mainly generated from cafeteria sales, as well as the rental of outlets, and advertising on board the three vessels and *Mġarr* terminal.

Budgeted expenditure for 2013 totalled €13,106,962, while the actual expenditure incurred amounted to €13,638,545. The largest divergences between budgeted and actual expenditure were noted in the Maintenance and Engineering Overheads and Cafeteria Expenses categories. In the former case, actual expenditure exceeded that budgeted by 36%, but was partly mitigated by the savings from expenditure related to Cafeteria, which was 23% less than that budgeted. In both instances, the main contributors to the said variance were Wages and Salaries, where those paid to engineering staff went up from €219,067 in 2012, to €300,772, exceeding the 2013 budgeted amount by 35%. On the other hand, wages and salaries paid to cafeteria staff in the year under review were €105,932 less than the budgeted amount of €433,229, mainly due to the resignation of 10 employees.

### Human Resources

As at 31 December 2013, the Company was headed by the Board of Directors comprising an Executive Chairman, Deputy Chairman, and six Board Members, and had 211 employees. The total basic salary paid for the year amounted to €4,234,277, besides a further amount of €2,082,373 covering overtime, allowances, as well as statutory and performance bonuses. This translates into an average wage of €30,964<sup>1</sup> per employee. The highest and lowest gross salary disbursed by the Company during 2013 amounted to €54,603 and €11,905 respectively, with the former amount being paid to a Permanent Chief Engineer and the latter to a Cafeteria Attendant<sup>2</sup>.

### Physical Resources

The Company's Operations and Human Resources (HR) functions are carried out from Channel House based in *Mġarr*, *Ċirkewwa* terminal and *Mġarr* tower. These properties are administered, managed and operated by GCCL for a consideration of €950,000 *per annum*, payable to the Authority for Transport in Malta, (Transport Malta) as stipulated in the Port Facilities Agreement entered into on 30 September 2011.

In addition to the above, GCCL rents out from third parties, an office situated in Victoria, housing the Finance Unit, comprising an accounting team of three employees and a messenger. Rent payable during 2013 for this property amounted to €24,387, while a further amount of €2,128 was paid in respect of common charges.

### Audit Scope and Methodology

The main objectives of the audit were to ensure that resources were used judiciously, and that adequate controls were in place to safeguard Government's interests. Other aims were to assess the reliability and adequacy of information available for decision-making and accountability purposes, and to make recommendations where warranted.

The focus and extent of audit work was based on an assessment of materiality and related risk. A review of GCCL's financial position was carried out. This mainly comprised a scrutiny of the Budget, monthly Management Accounts, Board minutes, as well as various reports presented to the Board.

During the assignment, audit concerns were further refined through information gathered from various sections, and interviews held with the Management team and other staff members.

### Audit Period

Testing covered transactions effected during financial year 2013, however, other issues encountered during the audit, falling outside the said period, were also reported upon.

### Audit Disclaimer

- a. Discrepancies were registered between the quantity of fuel invoiced and that actually delivered. GCCL was aware of the situation. Thus, no other testing was carried out by the National Audit Office (NAO). As at 31 December 2013, the amount in dispute totalled €23,111.

<sup>1</sup> Calculated on 204 employees; *i.e.* excluding six Directors, Executive Chairman, Deputy Chairman, five Cadets, and two employees who are on loan.

<sup>2</sup> These amounts are based on a report provided by GCCL, which however was incomplete as highlighted further down in this write-up.

- b. As reported further on in this Report, discrepancies relating to ticketing were identified. However, no testing was carried out on the reliability of the Information Technology systems in place, since this fell outside the audit's scope.

### Limitation on Scope of Audit

- a. An exercise, to reconcile the medical visits performed on employees while on Sick Leave (SL) with the number of visits invoiced, was attempted by the Auditors. However, it transpired that apart from the documented requests, there were other visits which were allegedly requested through the phone by the Manager in charge of HR, and which were not documented. As a result, Auditors were not in a position to confirm whether the number of invoiced and paid visits was correct.
- b. An annual payroll report covering all employees was requested from HR section. However, Auditors were informed that this report was not available at the Company's end and had to be generated by the accounting software provider. After a considerable time-lapse and a number of reminders, the report was provided, but it transpired that a number of employees were omitted, and thus it could not be considered as reliable.
- c. The original Change of Duty request forms were not made available, as they could not be traced. As a result, it could not be ascertained whether the respective changes were duly approved by Management.
- d. Physical inspection of assets was hindered since most of the items verified were not tagged and records lacked vital details enabling identification. Furthermore, the Fixed Assets Register included only items acquired from 2012 onwards. All other assets were reflected under one aggregate value as opening balance, supported only by copies of invoices. Similarly, records for store items were also deemed unreliable, while records for tools did not indicate the respective location.

## Key Issues

### *Financial Sustainability and Going Concern*

As at end 2013, the financial sustainability and going concern of GCCL were in serious jeopardy. Notwithstanding the slight improvement reported in the year under review over the prior year, the situation remained very critical, with the Company edging closer to a "... *situation in which there shall be insufficient funds for wages to be paid*", as stated by the Chairman. Further evidence to this is the fact that in February 2014, the Financial Controller was relying on PSO refund from the Ministry for Transport and Infrastructure, in order to be in a position to settle the wages.

The serious financial problems of the Company were also clearly evident in 2013, with cash at bank and in hand decreasing by 64%, from €1,238,538 to €446,224, and a parallel fall of 34% in reserves, from €3,061,545 to €2,026,292. On the other hand, creditors increased by 13%, from €11,459,217 to €12,961,241. This strategy, *i.e.* delaying to pay creditors to improve the cash flow position, has given rise to late-payment penalties, and interest payable on unpaid bills, totalling €18,737 as at 31 December 2013, mainly arising on balances due to a private company (€9,961), the Commissioner of Inland Revenue (€5,652) and the Automated Revenue Management Services Ltd (€3,069).

Although it was noted that the Company reduced its losses compared to the previous year, mainly through cost-cutting measures aimed primarily at reducing overtime needs, various operational deficiencies, as reported further down in this Report, were still observed during the audit, leaving ample room for other measures to be taken, in order to enhance efficiency and effectiveness of all operational aspects of the Company.

The current precarious financial situation was brought about by two main factors, namely, the adverse effect arising as a result of PSCC, and the outstanding balance of €8 million due from GF, in relation to the installation of hoistable decks and overhauls as explained hereafter.

In the former case, as a result of the provisions of PSCC, which the Company won in 2011 together with GF, Government subsidy in view of PSO

was reduced from €4 million in 2011, to €695,564 during the year under review. As per the Board minutes, the Company's PSO bid, drawn up with the assistance of a private company, was based on overly optimistic projections, and according to the latter, a business plan provided by GCCL was not eventually actioned upon. An analysis carried out by GCCL also revealed that:

- a. PSO projections did not include the considerable amount of expenses involved in the addition of the hoistable deck on *MV Ta' Pinu* ferry, and overhaul costs were predicted to be much less than actual expenses involved;
- b. initial quotations for regular vessel overhauls were substantially less than the final bills;
- c. on-board rental and advertising were predicted to increase substantially, but revenue from the said operations remained constant;
- d. PSO bid contemplated operational income from the *Mgarr* terminal which never materialised;
- e. predicted wage bill, which was expected to reduce as a result of employees reaching retirement age, was not correct; and
- f. increase in fuel prices affected the cash flow negatively.

With respect to the outstanding balance due from GF, during a Board meeting held in 2012, it was highlighted that, in terms of the joint venture agreement reached with GF, the latter could be held responsible for the expenses related to the hoistable decks. However, in the absence of a formal agreement about the nature and extent of the projects, this entity could not be forced to pay the relative expenses.

Further to the above, from a review of the joint venture agreement carried out by NAO, it transpired that it is not clear as to which of the two entities should bear the cost of modifications or improvements to the vessels, that are of a capital nature, but which are not necessarily required in order to comply with the obligations

and specifications set out in PSCC or any other legislations, regulations or directives.

In addition, as indicated in minutes of Board meeting held in December 2013, GCCL was informed that GF has no funds, and thus is not in a position to pay the outstanding amount of €8 million to GCCL. GF's revenue consists mainly of the contribution stipulated in the joint venture agreement, namely 85% of the joint venture free cash flows, which in fact failed to materialise. Technically, this would warrant a provision in GCCL's Financial Statements, which would in turn wipe out the Company's reserves. In reply to NAO's queries about the matter, the Chairman stated that "... after seven months of negotiations, GF accepted these bills. The next step will be the payment by GF of this long outstanding amount". However, no evidence to substantiate this statement was provided.

### ***Weak Control Environment***

Weak control environment prevailing within the Company was evident in various areas, especially those highlighted hereunder. Each of these issues will be discussed in detail further down in this write-up.

- a. Cafeteria pilferage;
- b. expired contracts;
- c. weak budgetary control;
- d. inefficient utilisation of personnel;
- e. lack of control on overtime;
- f. lack of synergy between the Management team, as well as lack of co-ordination between the various Units; and
- g. untraced records.

### ***Lack of Strategic Direction***

The Company lacks a clear strategic vision, as well as adequate co-ordination of the various internal functions. Evidence to this is the fact that there were no set objectives for the Heads of Department (HoDs) and other employees, providing the

basis against which their performance could be assessed. This lack of strategic direction was also reflected in a report dated June 2012, prepared by a private company specialised in operational risk management, wherein it was made clear that “... *the system is operating on auto pilot, with considerable risk in all aspects – legal; business and operational*”.

Further to the above, notwithstanding weekly operational meetings held up till July 2013, the four HoDs, together with their subordinates, were working independently without taking into consideration the other Departments. This was confirmed in an internal audit report, prepared by externally engaged auditors, where it was stated that the “... *attitude of complacency is partly the result of inappropriate synergies between departments ...*”, and was further evidenced in areas such as Budgeting, Overtime, and Purchasing, each of which will be discussed in more detail in this write-up.

Certain issues started being addressed by the Chief Executive Officer (CEO), on his appointment in December 2012, however, the action plan was aborted following his resignation in March 2013.

## Control Issues

### *Lack of Budgetary Control*

Although a budget for the year under review was drawn up by GCCL, the following shortcomings were noted:

- a. The final version of the budget was only approved on 6 March 2013, when more than two months of the year had already elapsed.
- b. No reference to budgets was made in the monthly Management Accounts. Auditors were verbally informed that actual figures are only compared to budgets at the end of the year. However, there was no documentary evidence to this effect either. As a result of this practice, variances remain undetected and no corrective action can be taken in a timely manner.
- c. Although the budget was based on past results and discussed with HoDs, as well as

CEO, no specific targets were set for these Heads, aimed at respecting and/or achieving the budgeted figures. Consequently, these varied considerably from the actual amounts.

- d. Only the Maintenance and Engineering, and the Commercial Units prepared a budget for 2013, albeit in the former case this was limited to the vessels’ repairs and maintenance expenses. No individual projections were provided by the Operations, HR, as well as the Finance and Administration Units.
- e. The aforementioned repairs and maintenance budget was drawn up in April 2013, thus after the main budget had been concluded and approved. This resulted in significant divergences between the two documents.

### *Increase in Salaries*

New salary structures, for both seaborne and other employees, came into force with effect from 1 January 2012, as a result of the new Collective Agreements negotiated by Management. In turn, the latter’s salaries were also revised by the Board of Directors, with the new salaries coming into effect a year later. These increases came at a time when serious financial difficulties were being encountered by the Company. Such improper attitude was already pointed out by Board Members in 2012, in a paper presented to the Directors, wherein it was made clear that besides other factors, impacting on the profitability of the Company, are the “... *high wages and promotions of unqualified staff – some awarded under collective agreements but others (managerial) without apparent justification and outside any wage structure ... which in turn has raised other calls for salary increases in grades outside the collective agreement*”.

Further to the above, from an in-depth analysis of the provisions of the Collective Agreements, it transpired that there are significant variances between the remuneration policies applicable for GCCL staff, and those applicable to other public officers covered by the Public Service Management Code (PSMC). Such variances were particularly evident in the case of overtime performed on a Public Holiday, as well as the night shift allowance. These significant divergences had a substantial financial impact on the Company.

## Management Salaries

### Background

Board minute 3435, dated January 2013, refers to the Proposal for the introduction of Managerial and Administrative Grades Wage Structure 2012-2015. According to the said minute, this proposal was approved by the then Ministry of Finance, the Economy and Investment (MFEI), except for the package in the Executive grade. The following issues were noted:

### Finance Approval not traced

The aforementioned approval from MFEI was not attached to the Board minutes. An attempt was made by GCCL to trace this authorisation, however, by the time the audit was concluded, only approval covering 2014-2015 salaries was provided. This posed a limitation on scope of audit since testing was based solely on the details of the said Board minute and the attached Wage Structure, which as per Board's decision should have come into effect as from 1 January 2013.

### Divergences from the Presumably Approved Salary Structure

From a review of 17 addenda, reflecting the amended salaries and conditions of the respective employees in Managerial grades in line with the approved structure, the following were encountered:

- a. The Managerial and Administrative Grades Wage Structure attached to the Board minutes, which according to the same minutes came into effect as from 1 January 2013, differed from the structure provided by the Manager responsible for HR. It could not be confirmed that the latter version was approved by the Board, as verbally claimed, and officially superseded the proposal attached to the Board minutes.
- b. One of two officers occupying the same grade, and entitled to a travelling allowance, was making use of a fully expensed Company vehicle, *in lieu* of this allowance.

- c. An officer who was in scale 4a (2013: €26,500), according to the aforementioned Managerial and Administrative Grades Wage Structure, was paid a higher amount equivalent to scale 3 of the same structure (€30,888), in line with an addendum to his employment contract dated 11 April 2011.

### Executive Grade Salary

As per the aforementioned Board minute, the proposed salary increases in the Executive grade were only accepted by MFEI in principle, spread over a three-year period. Nonetheless, the Board decided to approve the full increases in the said grade, as proposed by the HR Manager, with effect from 2013, ignoring MFEI's instructions.

### No Performance Measures

- a. While the Management team is entitled to a performance bonus, performance measures were completely lacking. As shown hereafter, the manner in which the said bonus was being awarded was in no way related to the performance of the individual managers, but as claimed by the Board in 2013, it was seen as an extension to the salary and expected to be paid in full.
- b. During a Board meeting held in July 2012, the importance of employees bearing their responsibilities was highlighted. Similar comments were made in a report titled 'GCCL Strategic Plan 2013-2017', drawn up by the then CEO in February 2013, stating that the principal concern of the Company is its management style which is "... *seen as very aggressive and unprofessional with many incidents of conflicts arising due to the serious lack of respect being practiced*".
- c. With respect to the 2012 performance bonus, during another Board meeting held in February 2013, "... *the Board noted that the performance of the Company officials entitled to performance bonuses in the year 2012 was unsatisfactory in a number of aspects*". A Board Member also stated that "... *there were too many incidents during the year where the responsible persons showed serious lack of management skills*", while

other Members maintained that “... *HoDs were not fully bearing the extent of their responsibilities ...*”, claiming that “... *no action was being taken against heads and employees who did not perform their work properly ...*”.

- d. Notwithstanding the above, during the same Board meeting, it was agreed that the six Company officials in question should be given a full bonus, *i.e.* 10% of basic salary, which was paid in February 2013, and amounted in total to €18,951 (before tax).
- e. On the other hand, in 2013, the Board “... *decided that the annual performance bonus shall be set at 6% for the performance of the year 2013, in view of the current situation of the Company*”. According to the Chairman, “... *it was decided that the rate of 6% ... is to be given across the board in view of the significant financial improvements in the last eight months, and the fact that no targets were agreed with Management by the previous Board*”.

### ***Ex-Gratia Payment to Heads of Department***

In December 2012, the Board discussed a request made by three Managers (HoDs) to roll forward untaken leave in 2012 to the following year. The same request included a claim for compensation for additional duties carried out by the same HoDs in the absence of a CEO.

- a. Based on legal advice, it was agreed that only 80 hours each of the annual leave entitlement of two of these HoDs would be rolled forward to 2013, with the balance remunerated by an *ex-gratia* payment. This proposal, with a direct financial impact of an aggregate amount of €11,622<sup>3</sup> was approved by the Board, despite that in the same Board meeting the unsustainable financial position of the Company was discussed.
- b. The two HoDs concerned claimed that leave was not taken due to pressure of work. Although the Board did not agree in full

with this assertion, the requests were still acceded to. It also transpired that while Vacation Leave (VL) applications of another two HoDs were approved by the Chairman, no such authorisations were evident in VL applications of HoDs who made these assertions. Thus, their claims could not be validated.

- c. The *ex-gratia* payment of €5,811 was paid to each of the two HoDs concerned “... *in the light of exceptional circumstances in connection with the delivery of service ...*”. Furthermore, this amount was paid without prejudice to any other bonus payable in terms of their contracts of employment. Thus, in addition to the said payment, the two HoDs also received the full performance bonus with respect to 2012, amounting to €3,500 (before tax).
- d. The aforementioned one-off bonus paid was based on leave not rolled forward. However, significant discrepancies were noted in the upkeep of VL records, as highlighted in the next observation, implying that these records were not reliable. The accuracy of the basis of the payment in question is also considered doubtful.

### ***Discrepancies in Vacation Leave Records***

#### ***Study Leave***

Neither requests nor respective approvals were in place up to 2013, to authorise paid study leave availed of by GCCL employees, which leave could not be quantified.

#### ***Temporary Absence***

A reconciliation exercise of the palming records for 2013 revealed that all four HoDs had several hours short, ranging between 65.75 and 226 hours, which were not accounted for in VL and SL records.

<sup>3</sup> Amount quoted covers *ex-gratia* payment inclusive of tax to the two HoDs.

## Inconsistent Records

On the other hand, there were several instances where HoDs were availing themselves of VL which they applied for, however, such absence was not always being deducted from their entitlement.

## Communication Costs

### Background

Apart from the Chairman, as at 31 December 2013, there were 22 employees making use of a mobile phone at the expense of the Company. The related costs in 2013 amounted to €18,214; *i.e.* over 65% of the total communication expenses, which amounted to €27,726 for the same year.

### Access to place Mobile Calls

- a. As at 31 December 2013, five officers were provided with a mobile phone, even though they were not included in the structure from which such benefit emanates. While in the case of one officer this entitlement was stipulated in his employment contract, no such sources were traced, covering the said benefit in the case of the other four officers.
- b. Apart from the four HoDs, six other employees, not in managerial grades, having direct access to place mobile calls from the fixed line of their respective offices, were also entitled to the use of a mobile phone at the Company's expense as mentioned above. Since the duties of most of these employees are mainly office-based, the need for a mobile phone in such cases is highly questionable.

### Mobile Capping

- a. Apart from the Chairman and the four HoDs, who are not subject to mobile capping, another four out of the 22 officers making use of a Company expensed mobile phone were also not subject to any limit. This contrast was particularly evident in the case of employees in the same grade, whereby only four out of six employees were subject to a restriction on their mobile phone expenditure.

- b. While mobile capping is highlighted in the Managerial and Administrative Grades Wage Structure, the limit is not stipulated therein, but is recorded in a separate spreadsheet. Thus, it could not be confirmed that the amounts indicated in this latter document have been duly approved by the Board and communicated to employees.
- c. The capping limits set by GCCL applicable to nine officers exceeded the annual threshold of €815 each per year established by PSMC, with one of the said employees having a threshold of €1,620.

## Company-owned Vehicles

Total Motor Vehicle costs amounted to €63,048 during the year under review, of which €30,436 were incurred on fuel, €15,821 on car leasing and hire, €8,657 on insurance and licensing, €4,543 on other transport expenses, and €3,591 for repairs.

- a. Although written policies are in place with respect to the upkeep of logbooks for Company-owned and/or hired vans, including specimen logbook and logbook certification forms, it was confirmed that no logbooks were kept for any of the Company's vehicles to control the use of such vehicles and fuel consumption.
- b. Fuel capping for certain officers entitled to a fully expensed car is also applicable, according to the Managerial and Administrative Grades Wages Structure. However, the capped limit is not specified.

## Human Resources Management

### General Overtime

- a. During the year under review, overtime paid by the Company amounted to €757,632. Although this amount is 10% less than that paid in 2012, certain categories still registered substantial increases over the previous year.
- b. Certain provisions of the standing Collective Agreements are giving rise to exorbitant payments. By way of example, 8.75 hours



of overtime performed by a Chief Engineer on a Public Holiday costed the Company €459 (gross of tax). Under the same circumstances, payment to a public officer in an analogous grade who is subject to PSMC provisions would have totalled €229 (gross of tax). This is to be seen in the light of a Company having 211 employees.

### *Engineering Staff*

#### *Exchange of Roles*

Three Second Engineers were officially appointed as Acting Chief Engineers to carry out the latter's duties as and when required. In turn, these three officers received an allowance, referred to as Substitution Allowance, equivalent to the difference between the salary of Second Engineer and that of Chief Engineer, for each hour of work performed in the latter grade. Testing carried out in this area covered the period 21 January to 14 April 2013. The following issues were noted:

- a. Deployment Records of the shifts worked during the selected period show that in a number of instances, Chief Engineer duties were assigned to the three Second Engineers referred to above, rather than the officers in the respective grade. As a result, the Company was ending up with a shortage of Second Engineers, and falling back on the Chief Engineers to cover both posts.
- b. The above gave rise to the illogical situation where Chief Engineers were paid overtime to perform duties of Second Engineers, and at the same time, the latter were paid an allowance to carry out the duties of the former, which amounted to €2,578 during the three-month period reviewed.

#### *Adverse Implications arising from Change of Duty*

According to the Deployment Records, in at least nine cases where Change of Duty was undertaken during the sampled period, the said change had an adverse impact on the Company. Such impact was both financial, as a result of additional compensation in the form of Substitution Allowance, as well as in terms of non-compliance

with the set Safety Manning Policy, arising from the fact that Second Engineers, with no apparent official authority to act as Chief Engineers, were performing the duties of the latter.

#### *Change of Duty Applications not traced*

Change of Duty applications, covering the period January to December 2013, were not provided for audit purposes as they could not be traced. Thus, in the absence of the original applications, it could not be confirmed that such changes were approved and authorised by Management.

#### *Unreliable Records*

- a. Testing to ensure correctness of overtime payments effected to Engineers, covering the sampled period January to March 2013, revealed significant variances between shift hours as indicated in the Deployment Records, and actual hours worked as per punch clock records.
- b. Management stated that although there is an evident discrepancy between these two records, it could be ascertained that the payroll has been correctly paid, and this can be further verified with the Crew List compiled by the Captain. However, no payroll computations were provided, hindering verifications. Moreover, divergences were still noted in the Crew Lists when compared with palming records.
- c. A review of a sample of Crew Lists, from the period between January and March 2013, revealed further shortcomings in the said documents, amongst which are incorrect dates and shift times, as well as unsigned records. It was also noted that at least in two instances, the name of the vessel as well as the sequence number originally indicated on the Crew List were changed, resulting in an identical Crew List being provided for two different vessels on the same date and time. Instances where shifts overlapped were also identified. However, in the absence of payroll records it could not be confirmed whether such hours were actually paid for.

### No Records to substantiate Overtime paid

It could not be ascertained whether recorded hours beyond the official timetable, as per punch clock records, were justified and duly authorised to be paid as overtime. The officer in charge of salary computations maintained that overtime performed by engineers is approved by a Senior Manager. However, no such approvals were made available. As a result, correctness of overtime payments effected to engineers could not be ensured.

### Terminal Staff

- a. The three Terminal Managers' (two with effect from August 2013) rosters catered for 24-hour attendance, seven days a week, resulting in significant overtime. Consequently, the overtime expense registered one of the largest adverse variances in individual line items, increasing from €6,520 in 2012 to €22,133 in 2013, significantly deviating from the budgeted assumption of a reduction of €27,500 in terminal overtime.
- b. As at 31 December 2013, the terminals were catered for by a total of 15 employees, comprising two Terminal Duty Managers, one Liaison Manager, five Terminal Duty Officers, six Terminal Duty Co-ordinators and one Terminal Maintenance Officer. A review of the main duties and responsibilities revealed that those for the officers outlined above, except for the Terminal Maintenance Officer, are very similar, with both Terminal Duty Officers and the Terminal Co-ordinators required "to cover for Terminal Duty Managers for out of rota hours ...". This implies that the presence of the Terminal Duty Managers is not required on a 24-hour basis.

### Drivers

It was understood that the main reason for overtime performed by the two drivers employed by GCCL was that of chauffeuring six Maltese crew members from *Sa Maison* to *Ċirkewwa* and *vice versa*, beyond their normal hours of work. Their

time-table was based on a 40-hour week, however, up to June 2013, both drivers were working the same shifts.

- a. During the year under review, these two employees were paid a total amount of €18,432 in overtime, and a further aggregate amount of €4,755 in night, Sunday and Public Holiday allowances. These were in total equivalent to more than 79% of their basic salary.
- b. Various options, aimed at reducing overtime, were already being considered by Management in August 2012, however action was only taken in July 2013.
- c. Albeit the changes made to drivers' rosters, the overtime recorded following these instructions was still significant, with overtime and allowances amounting to €9,464 for a period of less than six months. Trips effected on Sundays and Public Holidays were still resulting particularly expensive, with two return trips on a Sunday amounting to €180 (excluding fuel and wear and tear), when similar trips by private contractors were offered at quoted rates ranging between €19 and €25 per trip.
- d. Despite prevailing instructions to roster the concerned crew together, it was noted that this was not always the case. By way of example, on 31 August 2013, which fell in the four-week sample reviewed, the two Maltese seaborne employees on duty were deployed on two different shifts, which translated into a total transport cost of €227<sup>4</sup> in respect of two return trips between *Sa Maison* and *Ċirkewwa*.
- e. Payments to these drivers were based on overtime records kept by the same drivers. Notwithstanding the amounts involved in overtime payments, with cost per trip ranging from €21 to €118, such record was neither endorsed by any officer to ensure correctness of details recorded therein, nor was it counter-signed by the employees making use of the service as confirmation that the trip has in fact been performed.

<sup>4</sup> This amount comprised 16 hours overtime at time and a half, six hours night allowance and four hours Sunday allowance. It excludes fuel and wear and tear.

- f. While “*the Company shall at its own expense provide adequate transport to all Employees travelling to and from the vessel*”, such benefit is only stipulated in the Seaborne Officers Collective Agreement which does not include Bosuns and Seamen, being the grades of the officers making use of the transport referred to in the previous observations. Management maintained that they have a legal obligation to provide this service, but this claim was only supported by a side-letter dated 2012 stipulating that the Company offers the said transport service on a *buona fede* basis, but may refrain from providing this service for viability reasons after discussions with Union representatives.

### Other Personnel

- a. No documentation was provided in support of overtime of €843 paid to an officer for the period 7 January to 3 February 2013. As a result, it could not be determined whether such overtime was justified. Correctness of the respective payments could also not be ensured.
- b. The same period was reviewed in the case of another officer. In this instance, overtime and allowances aggregated to €2,137, with the latter amount exceeding the officer’s basic pay. Auditors were verbally informed that the bulk of the overtime, in total amounting to €1,864, related to the docking of *MV Gaudos*. However, it was noted that the officer concerned was not even included in the list provided, showing the personnel who were granted permission to access the shipyard during the docking period. Furthermore, as in the case above, no documentation was provided in support of the overtime paid.

### Safety Manning Policy

All vessels are issued with a Minimum Safe Manning Document by the Malta Maritime Authority, stipulating a number of conditions. One of these, namely condition three, stipulates that “... *total crew on board including Master shall not be less than: up to 500 passengers – 11 crew; more than 500 passengers – 15 crew ...*”.

Mainly between 08:00 and 18:45 during weekdays, and 17:00 and 01:00 during weekends, GCCL was employing additional staff members on each boat in service between Malta and Gozo, in order to be able to take a capacity of 500+ passengers. These are referred to as Top-up Crew and are contributing to the already high overtime expense. A review of Deployment Records as well as Crew Lists, covering a sample falling between January and March 2013 revealed the following:

- a. During the audited sample, the number of crew on board vessels was not always in line with the provisions of the aforementioned Minimum Safe Manning Document. Instances were identified where Top-up Crew varied between one and five while the number of total crew spanned between 10 and 17, resulting in both under and over-manning.
- b. As highlighted above, on several occasions, the total crew on the vessels exceeded the minimum crew of 11, but was less than the required 15 to be in a position to take the increased capacity on board.
- c. An exercise was carried out, wherein *MV Ta’ Pinu* deck logbook, covering a two-week period, was reviewed in order to determine the number of passengers on board. It was noted that only on six days was the 500 passenger threshold exceeded, with the highest number of passengers registered between 09:45 and 17:15. In view of this, the decision of engaging Top-up Crew, at times such as rosters between 17:00 and 01:00, as well as 18:30 and 04:30, may not be economically feasible.

### Cafeteria Pilferage

- a. Notwithstanding that in July 2012 the Board of Directors was aware that a number of cafeteria employees were colluding together and committing pilferage, and the matter was already referred to the police, up till May 2013, the employees in question were still in employment and receiving their full salary.

- b. According to media reports, the said embezzlement spanned over six years and amounted to at least €500,000. However, GCCL did not confirm this amount since, according to one of the HoDs “... *it would be highly irresponsible and inaccurate to assume the amount stolen based on the information available ...*”. This implies that any controls in place, if any, were not sufficient, as they hindered quantification of identified discrepancies.
- c. During criminal court proceedings, nine of the 10 employees involved in the aforementioned embezzlement pleaded guilty, while one pleaded not guilty. As a result, this latter officer was suspended on half pay as from April 2013, in line with the provisions of the collective agreement, and was still receiving 50% of his salary accordingly. With respect to the other nine employees, Board minutes indicated that due to lack of evidence, the Board was advised by the then legal advisor to reach an agreement with the said employees, wherein the latter shall be requested to resign with immediate effect. In line with this advice, the Company waived all claims against these employees, while the latter also gave up on claims for outstanding balances due to them by the Company. The Court concluded that the employees in question are put on a three-year probation. In view of the above, no money whatsoever was recouped by the Company.
- d. According to periodic stock-take records, significant discrepancies were being identified in every stock-take. During 2013, a global net adverse variance of €14,935 was registered, however, the action taken was limited to a write-off of the said discrepancies.
- e. While acknowledging that stock discrepancies decreased significantly following the resignation of the aforementioned employees, differences were still being registered between the system’s stock records and actual stock, since verifications were carried out when the cafeteria was still open for passengers on board.
- f. As part of audit testing, a full cafeteria stock-take was carried out on *MV Gaudos*. Notwithstanding that the ferry was not in operation at the time of the stock-take, discrepancies in a number of stock items were still detected, even though these were not of a material nature.

### **Fixed Assets**

- a. In an attempt to carry out a physical inspection, NAO requested a record of the fixed assets owned by the Company and their respective location. However, the report provided, lacked vital details such as serial numbers, hindering traceability. Furthermore, as also indicated under ‘Limitation on Scope of Audit’, all assets acquired prior to 1 January 2012 were reflected as one line item, under the heading Opening Balance.
- b. These lump amounts were only supported by a number of invoices, however, the location was nowhere indicated on the said documentation. Thus, reliance had to be placed on staff to recall the location of assets selected for verification.
- c. Although the items purchased in 2012 and 2013 were given a unique asset code on inventory records, out of the 10 selected for review, only three were tagged, enabling reconciliation.
- d. Several entries included in the inventory report, such as masking tape, fuel for rented van, sticky tags, rental of van and forklifts, by no means could be classified as fixed assets.
- e. It was confirmed that “*the Company does not have the practice to carry fixed asset inspections*”.
- f. Although according to the Incident Reports, two Very High Frequency (VHF) radios were reported as fallen into the sea, while other items went missing, no write-off was evident in the records.

### Tools

- a. While a proper system was in place for the recording of spare parts, tools acquired prior to January 2012 were only covered by the respective invoices. On the other hand, those purchased after the said date were duly recorded, however, as verbally confirmed by a Senior Manager, the location is nowhere indicated. Although this was pointed out in June 2012, during a General Health and Safety Risk Assessment, no action was taken to address this shortcoming.
- b. The provisions of the Collective Agreement state that, “*an employee who is supplied with Company tools has to sign a receipt indicating what tools he has taken into his custody*”. Notwithstanding this, no such record was being kept.

### Store Items

- a. Although records of store items were being maintained by the storekeeper, these did not enable effective control over the stock in hand, as there was no link between the respective issues, receipts and balance.
- b. An attempt was made by the Finance Department to draw up proper stock documentation with effect from June 2013. Nevertheless, it transpired that, at times, issues recorded exceeded the balance giving rise to a negative position, thus rendering the records unreliable. Moreover, store items kept on board the vessels were not included, since only those issued from *Mgarr* terminal were covered.

### Budget Overrun

In January 2013, *MV Gaudos* underwent a major overhaul for which the estimated cost, as indicated in the repairs and maintenance budget prepared by the respective Senior Manager, amounted to €38,752. Two quotations were sought for this service, with the selection falling on the cheapest bid at €48,078 exclusive of Value Added Tax (VAT). However, it later transpired that the quote

was not conclusive as it was based on information at hand. A number of jobs were left unquoted, necessitating the issue of a revised quotation, amounting to €77,558 (VAT excl.), which however in aggregate was still less than that of the other bidder. The following shortcomings were encountered:

- a. No public call for quotations was made for the required overhaul services. GCCL specifically requested two local service providers to submit their proposals. It was alleged that, “... *quotations were acquired from the only two local third parties who can offer such a service to our vessels*”.
- b. On completion of overhaul works on the *MV Gaudos*, the actual amount billed was of €95,837, on which a discount of 6% “... *as discussed and agreed ...*” was given, with the final amount paid totalling €90,087 (VAT excl.), exceeding the revised quoted cost by €12,529, and the budgeted amount by €51,335, *i.e.* 132%. Apart from the invoice, no other documentation was available in support of this agreed discount.
- c. The above was just one case in point whereby the actual expenditure incurred substantially surpassed the budgeted figures. An internal audit report, drawn up by independent auditors in October 2013, indicated various other instances whereby the budget was exceeded; including the installation of the car deck and ramps being underestimated by €593,113, as well as other structural modifications planned at €896,450 and actually costing €1,100,115.

### Lack of Segregation of Duties

- a. Notwithstanding the significant amount involved for the overhaul on the *MV Gaudos*, the invoice and related documentation were approved by just one officer, namely a Senior Manager, who happens to be the one with whom the aforementioned discount was discussed and agreed, and who coordinated and directed all the works carried out on the vessel.

- b. Although a detailed breakdown was provided with the invoice, items included therein, relating especially to man-hours and quantities, could not be independently verified as no other supporting documentation was provided.

### **Passenger and Vehicle Count Discrepancies**

Discrepancies came to light between two different sets of records comprising the number of passengers and vehicles carried by GCCL during 2013.

- a. It transpired that passengers and vehicles crossing from Gozo to Malta in 2013, as extracted from the ticketing database were 2,136,209 and 582,512 respectively. However, those departing from *Mġarr*, as per actual manual counts were 2,154,194 and 585,500, *i.e.* a discrepancy of 17,985 and 2,988 in passengers and vehicles respectively in one year.
- b. Another incongruity was noted between the manual count of the number of passengers and vehicles departing from *Mġarr* and *Ċirkewwa*. While as reported above, those departing from *Mġarr* were 2,154,194 and 585,500 respectively, those leaving from *Ċirkewwa* were 2,242,387 and 601,044, thus, a considerable difference of 88,193 in the case of passengers, and 15,544 for vehicles. GCCL alleged that there are instances where passengers use the Company's services to travel from *Ċirkewwa* to *Mġarr*, but then use other means of transportation for the return trip. While this could occasionally take place for passengers, it definitely does not explain the divergence in the number of vehicles.
- c. The concern related to ticketing issues was also raised following an audit exercise commissioned by the Board, and carried out during 2013, wherein it was reported that "... *the Operational Manager confirmed the possibility of scanner resetting issues which could lead to serious abuses in ticket recording*".

### **Ticketing Sales Revenue**

A three-month sample was selected for testing in order to determine the time-lapse up to the eventual deposit of cash and cheques into bank.

- a. During the sampled period, instances were noted where the time-lapse for the eventual remittance of cash to bank was as long as 15 days, while that for cheques lasted even 35 days after collection by the ticket seller. As a result of this practice, ticket sellers' outstanding undeposited balances as at year-end amounted to €71,865<sup>5</sup>.
- b. On a number of occasions, cash and cheques collected by security officers on a particular day were not remitted to bank together, but on separate days.

### **Medical Visits**

From a review of records related to medical visits carried out on Gozitan employees reporting as sick, covering a sample of three months, various shortcomings were revealed. Thus, accuracy and completeness of these documents could not be ascertained.

- a. A reconciliation exercise of two reports, kept by separate persons in connection with these medical visits, showed that during the selected period, at least 10 cases were omitted from one of the reports.
- b. In view of the outcome indicated above, an exercise was carried out by NAO, wherein, for the three-month sampled period, data included in the reports was traced to source documentation in order to determine the actual number of visits performed. However, a number of discrepancies were again noted between the number of visits as identified by NAO, and those invoiced and paid for.
- c. It was alleged that, in cases of employees having a particularly high rate of SL, extra visits were requested on the same day at different times. It was also maintained that

<sup>5</sup> As per Debtors' List Report.

such orders were placed through the phone. Thus, no documentation was available to support this claim.

- d. Except for medical certificates, no other feedback was evident from the doctor, for the visits he was paid for, not even for the alleged extra visits on employees on the same day. Consequently, it could not be determined on what basis were the invoices being certified as correct.
- e. The said doctor has been providing GCCL with his services since 2009. However, an agreement covering the provision of medical services was only entered into on 7 November 2013. As a result, no source documentation was available confirming that the rates charged during this period were in line with those agreed to by the Company. Moreover, GCCL officials were not in a position to confirm how the said service was acquired prior to this date.
- f. At least between 2011 and 7 November 2013, the said medical practitioner was charging GCCL the rate of €15 per visit. GCCL was accepting this fee notwithstanding that such a service constitutes an exempt without credit supply, and VAT paid thereon cannot be recouped.
- g. The agreement covering medical visits performed on employees in Malta, was entered into with a Maltese medical company on 28 January 2001, stipulating a rate of €8.15 per visit, and effective for a period of one year. Although 13 years later this entity was still providing medical services at a charge of €8.75 for each visit, no other agreements were entered into.

### ***No Valid Agreements in place***

#### ***Mġarr Terminal Cafeteria***

- a. The agreement entered into on 15 January 2010, covering the operation of the cafeteria situated at the *Mġarr* terminal, does not stipulate an expiration date.

- b. Notwithstanding requests by NAO for a copy of the respective tender document, this was not made available. Thus, it could not be ascertained whether an extension acknowledged informally *via* e-mail dated 27 July 2012 was allowable, according to the terms and provisions stipulated therein.

#### ***Advertising on board Vessels***

While the agreement entered into on 1 April 2003 was to remain in effect until 30 September 2011, a new tender for the rental of advertising space was still awaiting final approval from the Board as at 31 December 2013. Thus, rental income received between October 2011 and year-ending 2013 was not covered by an official document.

#### ***Residential Lets for Foreign Employees***

No contracts were in place covering the rentals of two residential properties provided by GCCL to two foreign employees at a total cost of €3,191 during the year under review.

#### ***Cleaning Services***

- a. As at December 2013, cleaning services in *Mġarr* and *Ċirkewwa* Terminals were performed by two different private companies. While the latter is covered by MFEI's direct order approvals for the amount of €30,200 (VAT excl.) for the period January to November 2013, no information was provided as to how the supplier for the services in *Mġarr* terminal has been contracted. Furthermore, although GCCL has been using the services of this provider since 2008, no contract was ever in place between the two parties.
- b. Direct order approvals for cleaning services of the *Ċirkewwa* Terminal were requested from MFEI in piecemeal. Following an approval granted on 7 January 2013 for a three-month period, a further temporary approval was granted by the latter on 22 April 2013 for another period of three months or until the tender is awarded. Notwithstanding that in this last approval GCCL was strongly advised by MFEI to publish the tender, as

the procedure of awarding direct orders on a piecemeal basis is not believed to be tenable, tenders issued in 2013 for the provision of cleaning services at *Ċirkewwa* and *Mgarr* terminals were still being adjudicated as at 23 December 2013, necessitating a further direct order approval on 25 October 2013.

### ***Discrepancy in Clocking Records***

Differences were noted between the clocked hours recorded by the time and attendance software, and those extracted through the payroll system. Management alleged that these could have happened as a result of manual adjustments which are effected when employees fail to palm in or out.

## **Recommendations**

### ***Key Issues***

#### **Financial Sustainability and Going Concern**

A thorough cost-cutting exercise at all levels of the Company is recommended to pinpoint any unnecessary expenses. At the same time, GCCL is to identify alternative sources of revenue and ensure that such income is eventually received. Expenditure is to be controlled through strict budgetary measures and timely action taken in case of deviations. Discussions with GF are to be taken at the inception of capital projects, and these are to be formally documented in order to avoid future disputes.

#### **Weak Control Environment**

Internal control procedures are fundamental to the successful operation and day-to-day running of the Company. 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 identified weaknesses and significant control failings to appropriate levels.

Sound internal controls cannot completely 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 are ready to put forward relevant queries when necessary, and take timely action to address any shortcomings.

#### **Lack of Strategic Direction**

Performance plans are to be drawn up for all the staff. Ideally, these should involve employees' participation, with the latter setting their own measurable objectives, based on identified Company targets. This approach allows Management to focus on goals, thus reducing significantly the apparent unfocused activity. It also enables teams to concentrate on solid outcomes and make the best use of available resources, while at the same time provide a basis against which individual performance could be assessed and compensated. This would eventually lead to improved organisational efficiency and greater alignment of goals at each operational level.

#### **Control Issues**

##### **Lack of Budgetary Control**

Functional and capital budgets are to be drawn up by the individual HoDs in a timely manner, enabling the Finance Unit to consolidate into one Budget, and have it approved by the Board of Directors by the beginning of the financial year. This will permit its implementation from the onset. Once approved, the final version is to be communicated back to HoDs, who are to be held responsible for the achievement of the set targets. Regular reconciliations between forecasted and actual results are to be carried out with any significant divergences reported to the Board of Directors for the necessary timely action.

##### **Increase in Salaries**

Directors are to ensure that all actions taken are in the best interest of the Company. Measures are to be put in place to ascertain goal congruency and the achievement of set Company objectives.

##### **Management Salaries**

It is to be ascertained that contracts entered into are in line with the prevailing Managerial and



Administrative Grades Wage Structure, and that instructions by the Ministry for Finance are abided with.

### No Performance Measures

GCCL is to implement an effective performance appraisal process, comprising clear targets, regular appraisals and evaluations of the individual managers' accomplishments. Criteria serving as a yardstick against which performance could be measured are also to be identified, thus providing a solid basis for the payment of the respective bonus.

### Ex-Gratia Payment to Heads of Department

In order to be effective, the Board needs to be transparent, willing to take strong positions and, whenever necessary, make tough decisions for the benefit of the Company. Claims for compensation by employees are to be duly verified and evaluated, so as to avoid unnecessary expenses and precedents.

### Discrepancies in Vacation Leave Records

For control purposes, absences other than VL and SL are to be documented, enabling both internal and external verifications. Furthermore, regular reconciliations between the different records are to be carried out, clearly indicating the officer carrying out such checks.

### Communication Costs

GCCL is encouraged to draw up a policy on the lines of PSMC, stipulating the capping applicable for all officers entitled to the use of a mobile phone, without making any distinction between the grades. Once set, it is to be ensured that beneficiaries are aware of their maximum entitlement, which is to be included in their employment contracts.

### Company-owned Vehicles

Management is to ensure that policy measures are implemented and regularly monitored so as to control the use of vehicles, as well as fuel consumption, where applicable. Moreover, GCCL is encouraged to follow the provisions of standing rules regulating Government-owned vehicles.

### Human Resources Management

Overtime is to be utilised only as a last resort and invariably kept to the barest minimum.

### Engineering Staff

Overtime and Change of Duty are to be supported by documentation, showing approval of the requested change or overtime payment. Moreover, all records are to be updated, enabling reconciliation between the different sources, which exercise is to be carried out on a regular basis. Management is to be held accountable for any adverse financial impact or any other unnecessary costs incurred as a result of their actions.

### Terminal Staff

Common grounds should be sought in order to bring employees on board, and implement the required shift changes as smoothly as possible, with the aim of ensuring cost-cutting targets.

### Drivers

In the Company's best interest, the financial viability of this service is to be assessed immediately, and more cost-effective solutions are to be adopted should the Company decide to continue to provide the transport.

### Other Personnel

Clear policies are to be drawn up with respect to overtime. Ideally, a Request for Overtime form is to be introduced, wherein extra hours required are recorded and approved, prior to the actual work being performed, clearly indicating the officers who will be assigned the respective tasks, and where possible hours involved. Once the form is approved by the respective Head of Unit, it shall be forwarded to HR section, to be verified and attached to payroll records in support of overtime payments.

### Safety Manning Policy

The Company is encouraged to consider and evaluate alternative solutions in order to reduce the overtime burden. One option could be the

introduction of an on-call allowance, applied on a rotational basis.

### Cafeteria Pilferage

Ideally, stock-takes are to be carried out when the ferry is not in motion, thus ascertaining that any variances identified are not related to stock movements during the trip. Moreover, these are to be performed at different dates, to keep the element of surprise. Material discrepancies detected are to be immediately communicated in writing to the Board, who is expected to take appropriate action, including initiating disciplinary proceedings if so required, without unnecessary delays. Moreover, procedures are to be implemented, enabling perpetrators to be identified in case of detected shortcomings.

### Fixed Assets

Management is to be guided by standing Inventory Control Regulations to address the highlighted concerns. Furthermore, regular physical inspections are to be carried out to detect any missing items and take the necessary actions in a timely manner.

### Tools

A record is to be drawn up by the Company, clearly showing all tools held by GCCL and their respective movements, allowing traceability at any point in time.

### Store Items

The upkeep of stock records is outlined in Treasury Circular 6/2004 – ‘Stock Control Procedures’. Regular physical inspections on store items are also recommended to detect variances as they arise.

### Budget Overrun

Budgets are to be prepared as accurately as possible, ensuring that the amounts involved, including those related to capital projects, are realistic. Thus, where feasible, these could be supported by quotations, comprising any discounts applicable, so as to avoid drastic deviations from

the originally planned figures. Furthermore, constant monitoring should be in place, with significant variations reported in writing to the Board of Directors in a timely manner to enable immediate corrective action.

### Lack of Segregation of Duties

For transparency purposes, any agreements are expected to be discussed with the Board and made in writing. In addition, where possible, invoices are to be certified by more than one officer.

### Passenger and Vehicle Count Discrepancies

It is strongly recommended that the Company seriously investigates the discrepancies and identifies, as soon as possible, any loopholes there may be in the system. It is of vital importance that tests are carried out on the scanners to ensure that these cannot be tampered with, and that data produced therefrom is reliable. Once accurate data is available, this is to be regularly reconciled to the manual counts’ records, with discrepancies reported to the Board of Directors in writing, and in a timely manner, for the required corrective action.

### Ticketing Sales Revenue

The Company is encouraged to investigate instances highlighted in the Report, in order to determine the reason for the delay to deposit money collected from ticket sales and take any action deemed necessary.

### Medical Visits

In order to enable reconciliation, one complete record is to be kept, indicating all medical visits ordered. Such requests should be in writing, showing also whether the visit has been performed or otherwise. Only in such a way can verification of invoices be carried out.

### No Valid Agreements in place

The Company is to ensure that official agreements, duly signed by both parties, are entered into. These should clearly specify the respective provision of service, and are to be adequately filed for future

reference. Moreover, GCCL is expected to review these documents on a periodical basis, allowing ample time to issue a public call for tenders in line with the Public Procurement Regulations before the contract in force elapses.

### Discrepancy in Clocking Records

Regular reconciliations of payroll data are to be carried out, with any discrepancies noted between the different records, verified and documented. Furthermore, whenever manual adjustments are required, which ideally are to be authorised by senior management, these are to be recorded in the system itself or in a separate log, including the reason necessitating the amendments.

### Management Comments

Management accepted, and have already taken on board several recommendations, aimed primarily at enhancing internal controls and introducing checks and balances which may have been lacking. Management stated that albeit lack of staff and financial constraints, the Company is doing its best to implement and effect as many internal controls as possible. Amongst the issues being addressed are:

- a. cost-cutting exercise, comprising the issue of calls for quotations and/or tenders, control on overtime, preparation of monthly budget variance reports, as well as prior discussions with GF about capital projects;
- b. traceability of documents;
- c. the issue of expired contracts;
- d. review of the Performance Measure mechanisms in place in line with the Government's Performance Review and Planning Process;
- e. upkeep of records for tools and store items;
- f. measures to ensure that monies are deposited in bank more promptly;
- g. revamp of the Company's SL reconciliation

process, including feedback from the Company's doctor and the cessation of random re-visits requests; and

- h. introduction of an external yearly Information Technology audit.

The following comments were also expressed by Management:

### Financial Sustainability and Going Concern

The explanations below were given for the differences between PSO bid projections and the actual results:

#### Hoistable deck and overhauls

*MV Gaudos, MV Ta' Pinu and MV Malita* are owned by GF, and thus any capital investments are payable by the owners of the vessels. In fact, GCCL has issued the respective invoices to GF who currently owes GCCL over €8 million. It was also stated that GF has accepted these invoices in January 2014, and a "... VAT set-off has been carried out between the two companies".

#### On-Board rental

The PSO tender bid had assumed that the income from the cafeteria at *Ċirkewwa* terminal would be €100,000. However, this tender had to be issued three times to be finally awarded at a much lower rental income than that projected, since no bids were received meeting the established minimum income expected.

#### Advertising on board Vessels

The tender for advertising was issued, but it had to be cancelled due to an inadvertent genuine mistake committed during the opening of the tender. Subsequent appeals were filed and the case is being heard by the Public Review Board.

#### Operational Income from the *Mġarr* Terminal

This income never materialised since there was resistance from the respective Ministries to keep the *Mġarr* terminal car park free of charge.

## Wage Bill

Contrary to PSO projections, whereby the wage bill was expected to reduce as a result of employees reaching retirement age, two Collective Agreements were subsequently negotiated and signed. These included substantial increases in payroll.

## Increase in Fuel Prices

No clause exists in PSO agreement to cover fuel price variances should these arise. Furthermore, PSO bid had projected that a fuel hedging agreement would be entered into by the Company. However, up till now, this was not possible, mainly due to the small amounts of marine gas oil purchased by the Company. Notwithstanding this, the Company stated that it is presently awaiting for the signing of 2011 Audited Financial Statements to be forwarded to hedging Companies for their evaluation.

## Lack of Strategic Direction

GCCL rebutted the statement that “... *it lacks a clear strategic vision*”, stating that Management is determined to turn the Company from a loss making to a profit making one. In view of this, it is setting up a system of performance measures in order to allow HoDs to focus on goals and concentrate on solid outcomes.

## Management Salaries

Management maintained that salaries are being paid as agreed and duly authorised by the Chairman, Deputy Chairman and the respective employee, and are paid exactly in line with the approved salary structure of Public Administration Collective Bargaining Unit (PACBU). It was also affirmed that the use of a fully expensed vehicle by the officer mentioned in observation (b)<sup>6</sup> is part of his employment contract, and when a new contract was being negotiated in 2012, this same employee did not accept to relinquish the use of the car. The two employees in question are aware of the situation. On the other hand, the salary increase

of the officer referred to in observation (c)<sup>6</sup> was approved by the previous Board of Directors and a new contract was signed.

## No Performance Measures

It was claimed that Management succeeded at keeping the Company running without a CEO, concluded satisfactorily two Collective Agreements, and for five months managed to fulfil service obligations with only two vessels available.

## Discrepancies in Vacation Leave Records

Management alleged that the variances in VL records arise when, due to the Company's exigencies, HoDs are required to report for work when they are on leave.

## Communication Costs

It was claimed that the two drivers have a mobile phone due to Company's exigencies. The remaining mobile phones are in accordance with PACBU agreement or the respective personal contracts of employment, except for one mobile phone given to an officer by the previous Board of Directors, which benefit is going to be removed. It was also remarked that one of the mobile phones is for general use at the Cafeteria Stores rather than for the use of a specific officer.

No answer was provided in connection with observation (b)<sup>7</sup>, questioning the need of a mobile phone in the case of office-based employees.

With respect to capping limits, Management stated that these are approved by PACBU, are in line with the Company's internal policies and the personal contractual obligations, and have been officially communicated to all the employees concerned. Two officers who previously had no capping will now be subject to a maximum limit. It was further maintained that the communication expense of these two officers was over and above that of others in the same grade because of the nature of their work, and this higher plan was approved by the Board of Directors.

<sup>6</sup> Observations under subtitle 'Divergences from the Presumably Approved Salary Structure' on page 181.

<sup>7</sup> Observation under subtitle 'Access to place Mobile Calls' on page 183.

### **Company-owned Vehicles**

Although Management submitted a record showing logbook entries for 2014, no documentation was provided with respect to the period under review.

### **Human Resources Management**

Management claimed that the increase in overtime of the Terminal Managers category was temporary, when the new *Ċirkewwa* terminal was opened abruptly in February 2013, while construction work was still in progress. Thus, additional manning had to be in place for safety reasons. According to GCCL, a cost-cutting exercise has now been implemented but at times, operations still require additional overtime.

### **Engineering Staff**

Management stated that given the shortage of qualified and skilled staff within the Industry, it is necessary to make use of all personnel available, including the use of Acting Chief Engineers. It was further indicated that the Company has invested in five cadets who are currently studying to acquire a qualification which would enable them to act as Second Engineer, thus, reducing overtime drastically.

### **Adverse Implications arising from Change of Duty**

NAO's comment referring to the non-compliance with the set Safety Manning Policy was also rebutted. It was argued that an engineer holding a class two Certificate of Competency<sup>8</sup> can work as Chief Engineer on Gozo Channel vessels and satisfy fully Ports Directorate requirements. Procedures relating to Change of Duty will also be reviewed to ensure an application is duly filled and authorised. No comments were received *vis-à-vis* the adverse financial impact arising therefrom.

### **Unreliable Records**

The reply stated that the logical explanation to the differences recorded is attributed to human error. Moreover, it was alleged that while there could be an error in the records, there could not be any

overlap of shifts, as there are checks which will not allow for the payment of such overlapping.

### **No Records to substantiate Overtime paid**

GCCL maintained that due to the nature of operating a ferry service, sometimes one cannot get prior approval for overtime. It was further stated that the lack of overtime records are isolated cases involving emergency requirements, such as breakdowns and accidents, since generic overtime which is attributable to operational delays is covered by operational reports, and on such occasions a whole crew would palm within the same timeframe, in contrast to the individual overtime which is being approved by Management through standard forms.

### **Terminal Staff**

The rostering of Duty Managers on a 24-hour basis was only temporary due to the additional requirements to operate the newly opened *Ċirkewwa* terminal.

### **Other Personnel**

Management stated that from the records checked by GCCL when *MV Gaudos* was being docked, it can be ascertained that the officer concerned was in fact rostered at the Drydocks. They also remarked that the list provided to Auditors, showing personnel granted permission to access the shipyard, did not include the names of the Workshop personnel who were rostered at the Drydocks.

### **Safety Manning Policy**

The reply specified that the vessel cannot operate unless it has a minimum safe manning complement. It was also indicated that GCCL is currently negotiating with Transport Malta to reduce the safety manning requirements.

### **Cafeteria Pilferage**

NAO's recommendation, that stock-takes should be carried out when the ferry is not in motion was agreed to by GCCL. However, due to

<sup>8</sup> Standards of Training and Certification of Watchkeeping (STCW) Second Engineer.

operational exigencies, where GCCL is required to operate a 24-hour timetable, necessitating two vessels which are in operation for most of the day, GCCL will incur overtime to two employees on each vessel in order to be able to implement the recommendation. It was also stated that since the Company employs 11 Cafeteria Attendants rostered from 04:30 till 00:15 hours, it is difficult to take action on a particular individual as one cannot attribute end-of-month discrepancies unless all sales are checked with security cameras.

### ***Fixed Assets***

Management indicated that where possible, assets purchased in 2012 and 2013 will be tagged by the end of 2014. The relevant details will also be included in the asset list. It was further stated that the items mentioned under observation (f)<sup>9</sup> have been capitalised since these were all incurred during the shift of the Company's workshop. On the other hand, since 2010, VHF radios have been expensed in view of their short life span. Management also remarked that the lack of fixed asset inspections is due to shortage of staff, however, the Company will do its best to carry out the inspections.

### ***Budget Overrun***

Management is doing its utmost to avoid budget overruns. It was also alleged that the two service providers from whom quotations were sought for the vessel's overhaul are the only two shipyards in Malta which have enough capacity for the docking of Gozo Channel's vessels.

NAO is of the opinion that Management replies provided for the observations highlighted under the headings below did not address the issues raised:

### ***Increase in Salaries***

The reply only stated that in view of the forthcoming 2013 General Election, the salary structure had been agreed and approved between all parties concerned.

### ***Management Salaries***

The approval provided covered salaries for the period 2014-2015, however no documentation was made available with respect to the period reviewed.

### ***Ex-Gratia Payment***

Reply was limited to stating that the said payments were granted by the previous Board of Directors and that VL is now being authorised by the Chairman for all HoDs. It was also remarked that the latter are on call 24/7 without palming in and out outside office hours.

### ***Discrepancies in Vacation Leave Records***

Only the issue titled 'Inconsistent Records' was addressed in the reply. No comments were received with respect to the other issues relating to study leave availed of by GCCL employees, and temporary absences which were not accounted for in VL and SL records.

### ***Drivers***

Although the side-letter provided allows the Company to stop the service for viability purposes, Management gave no indication that any action will be taken to this effect. The only other feedback received related to observation (e)<sup>10</sup>, stating that as from 3 March 2014, the drivers' overtime is being endorsed by the Liaison Manager.

### ***Lack of Segregation of Duties***

It was merely pointed out that the Company agrees with the recommendations, but due to lack of personnel, it cannot always be done.

### ***Passenger and Vehicle Count Discrepancies***

Management's comments only indicated that the Company is working hard to reduce the problem of discrepancies to a bare minimum.

<sup>9</sup> Observation under title 'Fixed Assets' on page 187.

<sup>10</sup> Observation under title 'Drivers' on page 185.

### ***Medical Visits***

Observations (d) and (e)<sup>11</sup>, concerning the procurement of service prior to 2013, as well as the feedback received, were not adequately answered, with the Company simply declaring that the respective officer involved in the engagement of the Company doctor is no longer in employment with GCCL.

### ***No Valid Agreements in place***

With respect to advertising on board vessels, it was stated that the Commercial Manager has sought approval to issue the tender on various occasions, but this was never forthcoming. The foreign employee has moved to another apartment

and a rental contract has now been signed. On the other hand, the replies provided for *Mgarr* terminal cafeteria and cleaning services did not properly address the observations raised.

### ***Discrepancy in Clocking Records***

In its reply, Management stated that when an employee fails to palm in, the Company has specific forms to be filled. Manual adjustments are made *ad hoc* while computing the Time and Attendance, and are strictly in line with what the employees have worked, meaning that the payroll paid is the actual payroll due to the employees.

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<sup>11</sup> Observations under title 'Medical Visits' on page 190.



Ministry for the Family and  
Social Solidarity



# Department of Social Policy

## Expenditure

### Background

The Department of Social Policy (DSP), which forms part of the Ministry for the Family and Social Solidarity (MFSS), had an approved budget of €220,873,000 for 2013 under Recurrent Vote 25, Social Policy. The majority, *i.e.* €214,463,000 was allocated under Programmes and Initiatives, mainly to cover State Contribution in terms of the Social Security Act, 1987. Another €5,142,000 was assigned for Personal Emoluments, with the remaining €1,268,000 for the Department's Operational and Maintenance Expenses.

The Department is responsible for the administration of social security legislation provisions, and operates from its 24 District Offices found around Malta and Gozo.

### Audit Scope and Methodology

The main scope of the audit was to evaluate the level of existing internal controls over the procurement and related payment, incurred by DSP from selected line items classified under Operational and Maintenance expenditure during the year 2013. To ensure a prudent and judicious use of Government resources, the audit also aimed to ascertain that standing laws, regulations, policies and procedures were being followed.

An introductory meeting was held with DSP officials, with the aim of discussing the audit objectives, and obtaining a general understanding

of relevant policies and procedures adopted by the Department, in relation to procurement and payment of different items of expenditure.

For the purposes of this audit, a sample of 37 transactions, totalling €323,367 and representing 31% of the amounts expensed from the sampled accounts under Operational and Maintenance expenditure, was taken. Transactions were selected on the basis of their nature and materiality. Targeted accounts consisted mainly of Rent and Office Services, Transport, Travel, as well as Contractual and Professional Services. In general, verifications were made against the Public Procurement Regulations (PPR). Reference was also made to the Public Service Management Code (PSMC) in relation to Government-owned vehicles and travel. Physical inspections were also carried out on inventory items held at Valletta Head Office, and Cottonera and Paola District Offices.

### Key Issues

#### *Services rendered by Direct Order outside the Period covered by Tender*

##### Carriage Services

In December 2009, a service provider was awarded a departmental tender for the year 2010, for the provision of carriage services. According to DSP, carriage services comprised transport of furniture and building material, cleaning of stores and

deposit of cheques for postage at MaltaPost p.l.c.. At the selection stage, the Adjudicating Board estimated the value of this tender to reach approximately €48,000.

A review of the relative files indicated that no contract was ever in place between DSP and this service provider. Only an Acceptance Letter was sent to the latter, notifying the award of the tender, “... according to the conditions as specified in the tender document”. It transpired that although the tender was extended until 30 June 2011, services continued to be rendered at least up to June 2014, *i.e.* at least up to the date of audit. To this effect, total payments made to the service provider during this period amounted to €160,929.

### Security Services

A departmental call for tender for the provision of security services at three different locations within DSP, was issued on 24 June 2011. The selected bidder entered into a Contract agreement for one year commencing from 21 May 2012. In its Evaluation Report, the Departmental Contracts Committee capped the relative award of this tender at an estimate of €44,840. Upon expiry of the contract term, seven extensions were granted by DSP by direct order, with the same terms and conditions, the last one valid up till July 2014. Moreover, the extension of the four-week contract period from 21 June to 23 July 2013 could not be traced in the relative file.

It resulted that total payments to the service provider, since the contract inception on 21 May 2012, amounted to €57,080, of which €38,284 was disbursed during the period of the contract, whilst the remaining was paid during the extended term.

### Open-ended Tenders/Contracts

The original Tender document of the above-mentioned carriage service provider stated that “*The validity of the contract may be extended ... for further periods at the same rates, terms and conditions after the due termination date or unless a new contract has been awarded*”. Likewise, the Contract with the selected bidder of security

services stated that it “... *may be renewed for further periods with the same rates, terms and conditions*”. The fact that the Tender and related Contract provided for extensions for unlimited future periods, is indicative that the provision of such services could be renewed indefinitely, which may in turn lead to unfair competition and lack of transparency.

### Non-renewal of Bank Guarantees

In the case of the selected bidder of carriage services, the Bank Guarantee, which expired on 31 December 2010, was never renewed notwithstanding that services were rendered up till at least June 2014. Similarly, the Bank Guarantee provided by the security service provider expired on 21 May 2013 and was only renewed during the course of the audit, *i.e.* on 30 June 2014, up to 30 September 2014. In the absence of this document, the Department is not protected, should the latter service cease to be provided abruptly.

### Retrospective Agreement and Late Approvals for Legal Services

The Ministry entered into a contract for service with an individual for the period 28 March to 30 June 2013, for the provision of legal services, at the value of €5,980, exclusive of Value Added Tax (VAT). This contract was signed on 5 August 2013, *i.e.* after the same contract had already expired. This instance is indicative that the service provider was not officially bound with any terms and conditions during the service period.

Furthermore, it transpired that the service was also approved retrospectively by the Permanent Secretary on 4 July 2013, *i.e.* after the contract period elapsed. This implies that funds were committed without adequate authorisation. Moreover, no clearance by MFIN, in accordance with Section 1.4.1.1 of the PSMC, was traced to cover this contract.

In the case of a separate legal services contract, valued at €17,500 (VAT excl.), a retrospective direct order approval was obtained from MFIN on 26 June 2013 for services that started being rendered on 1 April 2013 upon engagement.

## Control Issues

### *Letters of Acceptance issued after Supplies' Invoice*

In the case of five transactions tested, amounting to €31,798 and representing 10% of the audit sample, the respective Letter of Acceptance was raised after receipt of the invoice. Thus, the commitments to reserve the required funds in the Departmental Accounting System were not timely placed, even though these expenses were already determined through various signed contracts.

### *Lack of Control on the use of a Government-owned Vehicle*

Audit testing revealed that there were insufficient controls on the use of the only departmental general-use vehicle during 2013. Whilst testing whether this vehicle's logbook was properly kept, as per the requirements of Sections 8.2.4 and 8.2.5 of PSMC, the following shortcomings were noted:

- a. The purpose of journeys, as well as their duration, was not indicated on the logbook on various occasions.
- b. The officer making the journey did not always endorse the respective trip.
- c. Issues of petrol were never recorded<sup>1</sup>.
- d. The end-of-month certification of the logbook was only traced once for the period under review.

## Compliance Issues

### *Payments on Account made before receipt of Invoice*

#### Postage Services

During the year under review, DSP issued payments to MaltaPost p.l.c., which exceeded the amounts invoiced by the supplier, thus leaving prepaid balances on account. As at year-end, the prepaid balance on account with this service

provider amounted to €10,372, which balance was reduced to €1,142 by the last week of January 2014.

DSP stated that a forward payment has to be made to the service provider in question, in order for the Department to be eligible for bulk postage rates, which are more favourable than the normal rates. However, no official confirmation of this procedure was forthcoming from MaltaPost p.l.c. up to the date of the audit. Furthermore, a formal approval was not obtained prior to the issue of such advance payments, as required by the provisions of Article 20 of PPR.

#### Printing Services

Audit testing revealed that four payments on account by means of Transfer Schedules of Payments, amounting in aggregate to €40,500, were made by DSP to the Government Printing Press for services rendered during 2013. These amounts were then offset against invoices received from the latter, leaving a prepaid balance of €5,265 as at 4 April 2014.

### *Expenditure not covered by Fiscal Receipts*

Six transactions tested, amounting to €44,062 and representing 14% of the audit sample, were not supported by a fiscal receipt as required by MFIN Circular No. 2/2012. Furthermore, in five of these instances, totalling €41,162, the defaulting suppliers were not reported to VAT Department in the respective Returns which were submitted by DSP, as required by same Circular.

### *Non-compliance with Fiscal Obligations*

DSP obtained a direct order approval from MFIN on 23 May 2013, to enter into a contract for service with a Portuguese service provider, for the provision of consultancy services in connection with European Union funds. The contract was signed on 27 May 2013 for a period of six months, for a value of €41,250 (VAT excl.).

Instructions obtained from VAT Department stated that the service provider need not register in Malta for VAT purposes but should charge VAT

<sup>1</sup> Issues of fuel are recorded into the Fleet Management System.

at the rate of the Member State where registered, *i.e.* Germany. Testing however revealed that the service provider did not charge any VAT for this service and was eventually paid through the Multi-Payment function by means of two payments of €20,625 each, on 2 October and 20 December 2013, respectively.

Furthermore, the two payments made to this service provider, were not supported with any invoices, as stipulated in the relative contract for services.

### ***Lack of Compliance with Standing Travel Regulations***

During the review of two travel visits to attend meetings of the Council of Europe's Governmental Committee of the European Social Charter, the following shortcomings were noted:

- a. Section 8.5.1.2 of PSMC requires Permanent Secretaries "*... to request individual Directors General/Directors to prepare at the beginning of each year, a tentative programme of duty visits abroad, with a contingency for unforeseen visits*". Such programme, which ought to have included the visits in question, was not prepared, thus hindering the Department's ability to budget adequately for travel costs.
- b. In the case of both meetings, only two quotations for air travel were traced, none of which was from Air Malta. This goes against the provisions of PSMC Section 8.7.1.4.
- c. In both cases, a report containing the purpose and benefits achieved from these visits, as well as other related information was not prepared, as required by Section 8.10.1.1 of PSMC.

## **Recommendations**

### ***Key Issues***

#### **Services rendered by Direct Order outside the Period covered by Tender**

NAO opines that a new call for tenders or quotations is considered as best practice in order to ensure fairness, and provide equal opportunity to all interested parties in the provision of services. This would also ensure that the best market price would be obtained.

#### **Open-ended Tenders/Contracts**

No open-ended contracts are to be awarded to prospective bidders. Definite extensions are only to be granted if specifically provided for in the tender document.

#### **Non-renewal of Bank Guarantees**

It is in the Department's interest to ascertain that Bank Guarantees are not left to expire without being renewed, thus ensuring appropriate coverage should the supplier default.

#### **Retrospective Agreement and Late Approvals for Legal Services**

Contracts for service should only be entered into after the appropriate authorisation has been obtained in line with Article 20 of PPR and Section 1.4.1.1 of PSMC. This would ensure that the basic principles of transparency and accountability are adhered to.

Furthermore, such contracts are to be signed before delivery of the service, to ensure that both parties are knowledgeable of, and accept the contract conditions, thus ensuring that a proper vetting process of the agreement is undertaken prior to issuing payment.

### ***Control Issues***

#### ***Letters of Acceptance issued after Supplies' Invoice***

Management is to invariably ensure that whenever the value of the goods or services being acquired is determined by a contract, the Letter of Acceptance is prepared beforehand. This will not only ensure that adequate funds are committed to cover the expense, but also that the required authorisation for such purchase is obtained.

#### ***Lack of Control on the use of a Government-owned Vehicle***

DSP is expected to maintain a proper logbook for its general-use vehicle, in line with Government standing regulations. An officer is to be in charge of the certification of the logbook on a monthly basis, thereby ensuring that recorded trips were made on official duty and fuel consumption was reasonable.

### ***Compliance Issues***

#### ***Payments on Account made before receipt of Invoice***

If advance payments are strictly necessary, approval to this effect is to be sought and obtained from MFIN.

#### ***Expenditure not covered by Fiscal Receipts***

Management is to ensure that expenditure is invariably supported with proper fiscal receipts. All defaulting VAT registered suppliers are to be duly reported to VAT Department, so that appropriate and timely action can be taken to this effect.

#### ***Non-compliance with Fiscal Obligations***

The Department is to ensure that before payment is made it is in possession of proper invoices to cover the services it is being provided. Additional documentation, such as timesheets, can also be requested to support the details on the invoice, as necessary.

#### ***Lack of Compliance with Standing Travel Regulations***

The provisions of PSMC are to be invariably adhered to in respect of travelling expenses. Moreover, reports on each visit are to be compiled by the attending officers by not later than one month after the visit; this to enhance accountability and to make sure that any issues are adequately followed-up.

### ***Management Comments***

In its reply, Management agreed to most of the recommendations put forward by NAO and stated that corrective action has already been taken to address certain areas. The following comments further refer:

#### ***Open-ended Tenders/Contracts***

DSP stated that in line with NAO's recommendation, all recently issued tenders provided for specific contract time periods and definite extensions.

#### ***Retrospective Agreement and Late Approvals for Legal Services***

Management is of the opinion that since the contract for service was in line with PPR, MFIN clearance was not required.

#### ***Payments on Account made before Receipt of Invoice***

DSP stated that the advance payments made to the Government Printing Press were no longer being made as from September 2014, and the respective funds on account were duly refunded on 19 September 2014. NAO was further informed that, invoices received for printing jobs, are now being checked and referred for payment by the end of each month.

#### ***Expenditure not covered by Fiscal Receipts***

Receipts in relation to another two invoices issued by the security services provider were forwarded to NAO together with the Management Comments. It was noted that these fiscal receipts were consecutively numbered and undated.

### ***Lack of Compliance with Standing Travel Regulations***

Management confirmed that when the national airline has no direct or connecting flights to a destination where air travel is necessary, it does not inform the Advance Section of this in writing. Therefore, DSP feels that Section 8.7.1.4 of PSMC cannot be adhered to in instances where Air Malta cannot provide the required service.

# Collection of Social Security Contributions by the Inland Revenue Department

## Background

In terms of Articles 8(1) and 10(1) of the Social Security Act, 1987, employed, self-occupied and self-employed persons, as well as employers, are liable to pay Social Security Contributions (SSC) in accordance with the provisions of the same Act. Such contributions are classified into two categories, namely Class One and Class Two.

Class One SSC represent the payments that are disbursed by the employers, including contributions due by their respective employees, which payments are directly related to the Final Settlement System (FSS). Class Two contributions consist of those disbursements that are paid by either self-occupied<sup>1</sup> or self-employed<sup>2</sup> persons, and are made on a four-monthly basis in the form of indirect collection, *i.e.* by means of a Provisional Tax Claim raised by the Department of Inland Revenue (IRD), and based on the net profit declared the year before.

Prior to year 1998, IRD was vested with the responsibility of collecting both Class One and Two SSC, whereas the Department of Social Security (DSS) was in charge of the enforcement of contributions due. With effect from 1998, the enforcement action of Post-1998 SSC was transferred to IRD.

Responsibility for the enforcement of Pre-1998 SSC was later on also transferred to IRD with the coming into force of Act III of 2005, amending the Social Security Act, by which the powers of enforcement, initially vested in the Director of Social Security, became also exercisable by the Commissioner of Inland Revenue.

It was only at the end of 2012 that, for the first time, IRD included the outstanding SSC balances in their Arrears of Revenue Return (ARR) for that year. To this effect, the gross opening and closing balances reported for Class One SSC amounted to €90,063,929 and €84,825,616 respectively, whilst for Class Two contributions, these totalled €54,420,544 and €55,669,308. However, the reported balances excluded the arrears relating to Pre-1998 SSC. Further details in relation to such omission can be found under the first 'Key Issue' in this write-up.

The 2012 ARR submitted by IRD also revealed that, from the gross closing balances, the amounts of €56,500,970 and €34,864,032 were considered as not collectable, thus resulting in net collectable arrears as at 31 December 2012 of €28,324,646 and €20,805,276, for Class One and Class Two respectively.

The ageing of the net collectable arrears can be analysed as follows:

<sup>1</sup> Self-occupied means individuals who earn their income from trade, business, profession, vocation or any other economic activity that exceeds €910 *per annum*.

<sup>2</sup> Self-employed are persons who receive income from rents, investments, capital gains or any other income.

**Table 1: Ageing Analysis of Net Collectable Arrears as at 31 December 2012**

	Class One	Class Two
	€	€
Amounts outstanding for over ten years but less than fifteen years (2002 - 1998)	3,449,598	-
Amounts outstanding for over five years but less than ten years (2007 - 2003)	7,288,086	-
Amounts outstanding for over two years but less than five years (2010 - 2008)	11,362,460	10,281,801
Amounts outstanding for over one year but less than two years (2011)	6,219,754	3,299,590
Amounts outstanding for less than one year (2012)	- <sup>3</sup>	7,223,885
<b>Net Closing Balances</b>	<b>28,319,898<sup>4</sup></b>	<b>20,805,276</b>

(Source: Supporting documentation submitted by IRD during the 2012 Arrears of Revenue review)

The net collectable amounts for Class One were derived by multiplying aged closing balances with arbitrary percentages according to the ageing of the debtor, as reported in the 2012 Annual Audit Report. On the other hand, the net collectable amounts for Class Two represented contributions due pertaining to the last five years, since in terms of Article 116(5)(ii) of the Social Security Act “... any request by the self-employed or self-occupied person to pay such contributions ... shall be deemed null and void if submitted after attainment of pension age or after the lapse of five years from the time when the proper rate of contributions was due, whichever is the earlier ...”.

In 2012 and 2013, IRD carried out a number of key enforcement exercises in relation to Class One contributions. Table 2 depicts a list of these exercises. On the other hand, only one exercise was carried out in relation to Class Two contributions, consisting of 1,265 Notices being sent to defaulters during July and August 2012.

The Financial Estimates for Vote 22 – Social Security Benefits show that a total revenue of €641,000,000 was estimated to be collected by way of SSC during year 2013, whereas actual revenue collected as per the Departmental Accounting System amounted to €645,295,435, i.e. an increase of nearly €4.3 million over the revenue budgetary estimate.

## Audit Scope and Methodology

The main scope of the audit was to determine the level of existing internal controls over the collection of revenue due to Government from SSC. The assignment also aimed to ascertain that appropriate and timely enforcement action is taken to collect outstanding contributions.

The audit was conducted in accordance with generally accepted auditing standards. In addition to an introductory meeting held with IRD officials, further discussions were held with respective Officers in charge, particularly for the collection and enforcement of SSC due. Based on information gathered, a systems overview for each class was prepared, outlining procedures and controls in place, areas of concern, and other risks within the current systems. Detailed substantive testing, to confirm the existence and the correct application of recorded procedures as well as relevant controls, were also carried out.

In addition, a meeting with officials from DSS was held, in order to acquire knowledge about the enforcement of Pre-1998 arrears, as well as on the transfer of information to IRD concerning Class Two Credits<sup>5</sup> and Exemptions<sup>6</sup> related to contributions.

As indicated later on in more detail, under ‘Limitations on Scope of Audit’, the requested breakdown of the arrears of revenue, for the years

<sup>3</sup> These balances were not yet due as at date of reporting of arrears.

<sup>4</sup> The Net Closing Balance in the ageing analysis did not agree with the total Net Collectable Arrears reported in the Arrears of Revenue Return, by €4,748, this being the difference between the aggregate of the breakdown lists of arrears provided by IRD and the balances reported in the Return.

<sup>5</sup> Credits represent contributions which are not payable by a person, but are still accredited to the individual for the purposes of the Social Security Act, 1987, such as in the case of Sickness Benefit and Invalidity Pension.

<sup>6</sup> A number of exemptions from payment of contributions exist, including for seasonal work and persons studying overseas.



**Table 2: Class One - Key Enforcement Exercises carried out throughout 2013 and 2012**

Enforcement Type	2013		2012	
	Date	Count	Date	Count
Current Year FS5 Defaulters Notices	18 January 2013	2,539	9 February 2012	2,592
Prior Year FS7 Default Notices	26 March 2013	3,827	15 May 2012	2,721
FSS/SSC Employers Default Notices	29 October 2013	378	15 February 2012	887
FSS/SSC Employers Demand Notices	-	-	15 February 2012	655
FS7 Defaulters Warning Letters	31 May 2013	2,154	12 September 2012	1,839

ended 2011 and 2012, were not made available within a reasonable time. Thus, a random sample of defaulters for each class had to be selected from the lists provided by IRD, that were prepared following an exercise on key enforcement recently carried out by the latter. However, such lists did not have all necessary details, such as the respective outstanding balances.

In order to be able to audit a full cycle of enforcement procedures, the National Audit Office (NAO) deemed it appropriate to extend the testing to enforcement action taken by the Department also during the year 2012. As a result, this Office could verify whether up to the date of the audit, any relevant follow-up was performed by IRD.

A total of 37 employers under Class One and 10 defaulters under Class Two, collectively having SSC due<sup>7</sup> of €4,981,928 and €59,372 respectively, were selected and reviewed to ensure that IRD was carrying out appropriate and timely enforcement action for the collection of outstanding contributions. Moreover, this Office also examined all contributions due by the sampled employers, even though such balances may be related to other basis years, and thus were not included in the relative Enforcement Notice or Letter.

### Settlement Agreements

IRD provided this Office with lists of settlement agreements entered into between defaulters and the Department, during the years 2009 to 2013 under Class One, and for 2010 to 2013 under Class Two. Ten individual agreements from each class included in the audit sample were selected from these lists, on the basis of their duration and materiality, to verify that IRD was properly monitoring and following up the settlement of the respective amounts in line with the applicable arrangements.

In addition, if the 37 employers under Class One and 10 taxpayers under Class Two had signed a settlement agreement with IRD, these were also reviewed. In all, NAO examined 29 agreements pertaining to 22 Class One employers, and 11 agreements under Class Two, which in aggregate had amounts due totalling €6,034,930 and €78,413 respectively.

For each of the 47 employers<sup>8</sup> and 20 taxpayers<sup>9</sup>, an examination of all the relevant Enforcement Notices, agreements and other relevant documents in the Virtual File System, was performed. In addition, an enquiry on the payments made by the respective defaulters, and any outstanding SSC balances featuring in the Accounts Receivable

<sup>7</sup> These balances represent the aggregate amounts of contributions due included in the Enforcement Notices and Letters that were selected for testing purposes, excluding any related additional outstanding contributions, resulting from late payments (penalties).

<sup>8</sup> The total of 47 cases tested for Class One contributions is made out of the aggregate of 37 employers who were selected from the lists of the key enforcement exercises carried out by IRD, and 10 employers who had their settlement agreement selected from the respective lists.

<sup>9</sup> Total of 20 taxpayers tested for Class Two contributions, consisting of the 10 defaulters which were selected from the enforcement lists provided, and 10 other taxpayers as selected from the lists of agreements.

System (ARS) as at date of audit testing, was also carried out. This verification was effected on 23 January 2014 and 31 January 2014 for Class Two and Class One contributions respectively. Thus, these two dates were established as the cut-off dates for reporting purposes in this write-up.

## Limitations on Scope of Audit

A number of limitations were encountered during the audit, hindering the objectives and completeness of the review in question, as detailed hereunder.

### *Class One Social Security Contributions*

#### *Breakdown of the Arrears of Revenue provided late*

Requested breakdowns of arrears of revenue by employer and year, as at 31 December 2011 and 2012, were not made available in time to be used in the sample selection process. This data only reached NAO eight weeks from the date it was originally requested, in spite of the various reminders sent.

Due to this limitation, the sample had to be chosen from various lists compiled by the Department when carrying out the key enforcement exercises itself during the period under review. However, these lists excluded the actual outstanding balances for each employer. As a result, the sample could not be selected on the basis of recurrence and materiality as originally planned, but at random.

#### *Payments under a Settlement Agreement not easily identifiable in the System*

Payments are recorded in ARS, indicating the type of transaction (FSS, SSC, Additional FSS and Additional SSC), the basis year, the amount received and the corresponding receipt number.

The majority of settlement agreements drawn up by IRD cover FSS, SSC and penalties due from separate years, which balance is shown as one whole amount and then divided into equal monthly instalments. Although the System allocates these instalments against their respective tax and basis year, setting off older balances first,

there is no reporting facility to separately identify pending SSC due for each year. Moreover, in the case of agreements established through Phase Two of the Exemption Order Scheme, payments are posted in a separate account in ARS, and are only allocated in the employer's proper account when the agreement is fully honoured. Therefore, throughout this Report, the outstanding balances reported include both FSS and SSC, as well as related penalties when applicable.

### *Class Two Social Security Contributions*

#### *Breakdown of Arrears of Revenue by Taxpayer and Year not available*

Notwithstanding the various reminders sent, IRD only provided the list of Class Two SSC in arrears, as at end December 2011 and 2012, by year, and not by taxpayer as originally requested, since the latter were not available.

In the absence of such information, NAO had no option but to select the sample from the list of Notices issued by IRD during the period under review. However, since this list, similar to that of Class One, also excluded the details of balances due, the sample had to be selected on a random basis and not on materiality.

## Key Issues

### *No Enforcement on Pre-1998 Arrears of Revenue*

As already highlighted in the 'Introduction', the arrears relating to Pre-1998 SSC were not included in ARR submitted by the Department for the year ended 31 December 2012. It was confirmed that Pre-1998 Class One contributions were forwarded to IRD by DSS in hard copy files, in February 2006. However, the former stated that most of these files lacked important information, whilst the status of pending cases was not properly identified, due to lack of availability of DSS staff. It transpired that the transfer of responsibilities between the two Departments in question, to enforce the collection of SSC relating to Pre-1998 following the 2005 amendment of the relative law, was not carried out in such a manner to ensure a continuation of enforcement on defaulters. To this

effect, IRD confirmed that no enforcement action was performed by the latter on Pre-1998 arrears, since the available data for these years is not reliable, with the increased risk that these continue to become statute-barred. Furthermore, as already mentioned in the introductory part of this write-up, only Post-1998 arrears were reported in ARR as at end 2012.

## Class One Social Security Contributions

### Enforcement Measures

#### Background

#### Civil Procedure

Once FSS forms<sup>10</sup> are submitted to IRD, the latter has the right to proceed to collect any outstanding amounts through the legal procedures when employers, although submitting the required documents, do not effect part or full payment. Action may be taken on such defaulters as follows:

- a. A 'FSS/SSC Default Notice' is sent to all those defaulters featuring in one of the Enforcement Run Reports issued by the Computer Section within IRD, to make employers aware that they are in default. However, the following are excluded from the report, thus a Default Notice is not sent when:
  - i. balances are covered by a settlement agreement reached with the Collection Section, either directly or through the Reduction in Penalties Scheme; and
  - ii. defaulters have a balance below a set threshold.
- b. If the Default Notice is not contested within 10 days by a letter to IRD, a 'Demand Notice' may be issued which, if not contested before a Court of Law within 15 days from the date of notification, gives the Department an Executive Title, as regulated by Article 24 of FSS Rules.

- c. Following the lapse of the 15 days credit granted by the Demand Notice, a Judicial Letter filed before the Civil Courts may be sent, requesting payment within two days from the date of notification.
- d. A Garnishee Order may then be issued by IRD after two days from date of notification of the Judicial Letter.

#### Criminal Procedure

Where an employer does not submit the required FSS forms, IRD has the right to request the Commissioner of Police to charge the said employers, or directors of a company, with a criminal offence in terms of Article 23(13) of the Income Tax Management Act.

The following action is taken on the targeted defaulters:

- a. An 'FS7 Default Notice' is sent to all those featuring in the respective report, issued by IRD. This will serve to inform employers that they failed to submit one or more FS7 and FS3 forms.
- b. If a Default Notice is not contested within 10 days, a Warning Letter may be issued, requesting the employer to submit missing documents and outstanding payments within 15 days.
- c. Following a Warning Letter, in case the defaulter has still not complied, the Department may then issue a Writ of Summons.

Both civil and criminal procedures may be carried out simultaneously.

#### Late Enforcement Action

During the course of the audit, it transpired that enforcement action by IRD was not carried out in a timely manner, as detailed below:

- a. In 2013, IRD issued 378 'FSS/SSC Default Notices' to employers, only late during the

<sup>10</sup> Employers are required to submit FS5 forms on a monthly basis, as well as end-of-year documents. The latter being the FS7 form and the related FS3 forms. Upon submission, the employers are also required to effect the respective payment of any contributions due.

year, on 29 October, in contrast with the previous year where 887 similar notices were issued on 15 February. Notices raised during 2013 covered an aggregate outstanding SSC balance of €3,574,107.

- b. It transpired that after the lapse of the 10-day credit granted in the Default Notices issued in 2013, as at date of audit testing, *i.e.* 31 January 2014, IRD did not issue any related Demand Notices to follow-up the matter.

### Lack of Appropriate Enforcement Action

From a review of the 47 sampled employers, lack of enforcement by IRD was evident. *Table 3* at the end of this write-up depicts a list of the limited enforcement action taken by the Department on the 10 defaulters having the highest outstanding SSC, out of the ones selected for review. As a result of lack of follow-up, as at 31 January 2014, the top 10 employers still had an aggregate outstanding SSC of €5,091,591, pertaining to years 2000 to 2012. Related payments made by these defaulters from the original amounts, which totalled only €62,791, is considered relatively insignificant.

More details on the lack of appropriate enforcement action by IRD related to the audit sample is given hereafter:

#### a. *Default Notices*

In seven cases where the employers submitted their end-of-year documents for basis years 2011 and 2012, without effecting full payment of SSC due, at an aggregate outstanding amount of €1,226,769, no action was taken by IRD, in the form of an official Default Notice, to submit missing end-of-year documents, with the aim to recoup these amounts. As at date of audit testing, these still totalled €1,141,633.

#### b. *Demand Notices*

It transpired that 14 employers in the audit sample did not effect any payments of contributions due after the Default Notice was received. Notwithstanding that the deadlines specified in such notices

were long overdue, one of them dated 22 April 2009, IRD did neither carry out any enforcement by means of a Demand Notice, nor was any other action taken. As at date of audit, aggregate outstanding balances relating to these cases totalled €3,545,088. Additionally, NAO noted that pending contributions in the audit sample dated back from year 2000.

#### c. *Judicial Letters*

Despite that in eight cases where a Judicial Letter was sent, the 15-day period granted to defaulters through Demand Notices had elapsed by approximately 22 months up to the date of audit, NAO noted that no appropriate action was taken in nearly two years to recoup these balances. A total of €328,288 was still outstanding as at date of testing.

#### d. *Writs of Summons*

No further legal action was taken following the issue of seven Warning Letters, even though after the lapse of the 15-day deadline, aggregate outstanding SSC related to basis years 2009 to 2012, totalled €294,927. Following the receipt of the Warning Letter, all seven employers submitted the required end-of-year documents, but failed to settle the outstanding SSC.

In another case, following receipt of two Warning Letters, one for basis years 2010 and 2011 issued on 12 September 2012, and another for basis year 2012 issued on 31 May 2013, the employer did not submit the relative end-of-year documents as required by virtue of such Letters. Notwithstanding this, no further legal action was taken by IRD.

#### e. *Garnishee Orders*

In nine cases involving a Garnishee Order, even though the defaulters did not effect payment of outstanding contributions totalling €276,677, after the receipt of a Judicial Letter, no further legal action was taken against them. This fact was upheld by

IRD officials. These Judicial Letters were sent between October 2006 to March 2010, for basis years ranging from 1998 to 2008.

The lack of enforcement action by IRD, against those who have failed to pay their outstanding contributions, is resulting in loss of Government funds. The increase in arrears is also evidenced from the ageing analysis of 2012 reports mentioned in the introductory part of this write-up, showing that the net balance of €22,100,144 has been due for more than two years, and nearly half of this amount has been outstanding for over five years.

### *Insufficient Monitoring and Follow-up of Settlement Agreements*

The then Ministry of Finance, the Economy and Investment announced Phase Two of the Exemption Order Scheme on 7 July 2010. This Scheme was intended to provide employers who fell behind in the payments of FSS and SSC in respect of their employees for the calendar years 1998 to 2009, with the opportunity to regularise their position and benefit from a reduction in additional tax and SSC to which they may have become subject. Regularisation was made through settlement agreements.

During the audit, it transpired that some defaulters were also given the possibility to enter into a specific agreement with the Department to settle their dues through an instalment plan, which plans normally span over a period of time depending on the pending balances.

A review of the lists provided by IRD indicated that during the years 2009 to 2013, a total of 2,631 employers entered into one of such agreements with the Department to settle their outstanding FSS and SSC, totalling €132,401,788. This amount included any additional charges. However, as mentioned under 'Limitations on Scope of Audit', it was not possible for NAO to identify which of the instalments related to FSS or SSC, due to lack of reporting facilities and time constraints.

In 20 out of the 29 instances in the audit sample (*i.e.* 69%), the respective employers breached their settlement agreement, without the Department

carrying out any monitoring and consequent follow-up, including the revocation of the agreement. These dishonoured commitments related to 15 different defaulters who failed to abide with the payment schedule, in aggregate having an original outstanding amount of €4,660,560. As at the date of audit testing, *i.e.* 31 January 2014, total unpaid balances covered by such dishonoured agreements aggregated to €1,171,237.

In particular, one employer dishonoured three different settlement agreements, covering a total unpaid balance of €102,080, whilst three other employers, having a total of unpaid balances of €169,470, €114,571 and €9,794 respectively, did not honour either of their two existing agreements.

## **Class Two Social Security Contributions**

### *Lack of Appropriate and Timely Enforcement Action*

- a. Once data concerning any National Insurance 'credits' and 'exemptions' applicable to taxpayers is received from DSS, IRD initiates the enforcement of collection with the issue of an Informative Notice, requesting payment of contributions due for the last five years. Following this Notice, a Judicial Letter may be served to the defaulter if the latter fails to submit any contributions due within three months as prescribed in the Informative Notice. Finally, the Department may issue a Garnishee Order after 10 days from date of the Judicial Letter.

However, the only enforcement exercise carried out by IRD for the period under review, took place during July and August 2012, whereby the Department sent a total of 1,265 Informative Notices. These Notices were sent to a number of Class Two taxpayers with material<sup>11</sup> outstanding balances covering the last five years, *i.e.* pertaining to basis years 2007 to 2011, and totalling €7,286,507, excluding those taxpayers having any credits and/or exemptions from this exercise.

<sup>11</sup> Defaulters who had a balance below a set threshold were excluded from this enforcement exercise.

- b. During the course of the audit, NAO was also informed that a number of Informative Notices, covering balances due for the years 2009 to 2012, were actually issued to defaulters during January 2014. Such Notices did not cover the year 2013 since at the date of their issue, DSS was not yet in a position to provide credits for 2013.
- c. In seven out of the sample of 10 cases examined under this category, NAO noted that as at date of audit, even though approximately 16 months had elapsed following the Informative Notices issued in July and August 2012, no action was yet taken in terms of a Judicial Letter or any other type of enforcement measure, when the selected defaulters failed to settle outstanding dues, amounting to €42,615.
- d. In four of the above instances, it transpired that another Informative Notice, covering an aggregate value of €13,535, was issued on 20 January 2014, this time relating to SSC due for years 2009 to 2012, rather than issuing a Judicial Letter which was expected to be sent in September 2012.

Since in terms of Article 116(5)(ii) of the Social Security Act, pension benefits are not granted in respect of SSC submitted after the lapse of five years from the time when the proper balance was due, it is highly unlikely that the respective taxpayer will now pay his outstanding contributions.

### *Insufficient Monitoring and Follow-up of Settlement Agreements*

During the years 2010 to 2013, 210 defaulters were given the possibility to enter into an agreement with the Department to settle outstanding SSC, totalling €976,414, by means of an instalment plan over a period of time as determined by IRD.

Except for one part-payment, there was no response from the remaining nine defaulters, some of which had instalments outstanding since 31 July 2010. Even though SSC due from the 10 sampled defaulters totalled €67,449, IRD made no follow-up, thus increasing the probability that such arrears remain outstanding.

## *Credits and Exemptions*

### *Background*

DSS only forwards information to IRD regarding ‘credits’ and ‘exemptions’ upon request from the latter, prior to any enforcement exercise, consisting mainly of:

- a. Credits granted to Class Two taxpayers, resulting from Social Security benefits, such as in the event of sick leave; and
- b. Exemptions to individuals studying overseas and those self-occupied taxpayers whose profit is below an established threshold.

The above-mentioned information may be used by IRD to adjust the accrued National Insurance Contributions accordingly, of those taxpayers who are not liable to pay any of the monthly Contributions or part thereof during a particular period.

However, IRD confirmed that these adjustments are not being carried out since the data forwarded by DSS is extracted from a different system from that available to DSS Area Offices. As a result, inconsistencies between the two data sets most often arise, and consequently cannot be relied upon by IRD for enforcement purposes. To this effect, IRD requested DSS to rectify the situation in order to ensure consistent information, which matter was still pending when the audit was concluded.

### *No Enforcement Action carried out on Taxpayers with ‘Credits’ and ‘Exemptions’*

Until data is considered reliable, IRD has ceased enforcement action on individuals having unpaid SSC, but also entitled to any credits and/or exemptions. In fact, such data received from DSS is only used to eliminate the relative taxpayers from any enforcement exercise that the Department intends to carry out, in view of the possibility of any adjustments that the latter would not be fully aware of. Therefore, the probability of collecting outstanding SSC from taxpayers whose pending amounts require to be adjusted for credits and exemptions is minimised.

### Net Collectable Arrears overstated

It was confirmed that information on credits and exemptions was only requested prior to any enforcement exercise, and that such data is not used to update taxpayers' statements of arrears. This indicates that amounts for Class Two contributions, reported as falling in arrears in the Department's ARR, are overstated by any adjustments required for credits and/or exemptions of SSC that are not actually collectable. As a result, the reliability of reported net collectable contributions falling in arrears, as reported in IRD's annual ARR, is also questionable.

## Control Issues

### *Class One Social Security Contributions*

#### No Enforcement Action on Outstanding Balances below a set Threshold

The audit revealed that throughout enforcement exercises, Notices are not sent to all defaulters, since employers having outstanding SSC lower than a threshold pre-established by the Department, are normally excluded from the targeted population. This may lead to a situation where amounts from defaulting employers with individual small balances are not collected, although collectively, their outstanding SSC could be quite substantial.

#### Penalty Remissions not automatically accounted for in the System

Any reductions in penalties, resulting from settlement agreements, are accounted for manually in ARS, since the System has no function to reduce such penalties. Consequently, the balances due in the 'Employer Statement' in ARS is not always correct, unless the responsible officers immediately post the necessary adjustments.

Until these adjustments are carried out, penalties continue to accumulate on incorrect balances, even though such amounts would have been settled by employers. It was also noted that any payments are initially allocated against the

accumulated additional contributions (penalties), leaving balances of FSS and SSC showing as still due in the System. To this effect, from the audit sample, three cases were identified in which the aggregate balance of €5,060, that was reported as outstanding in the relative 'Employer Statement', was not actually due.

Moreover, even though these agreements were settled by the respective defaulters between 6 December 2012 and 13 May 2013, up to the date of audit, *i.e.* nearly one year later, IRD officers had not yet posted the necessary adjustments in ARS, to write-off the above-mentioned balance.

#### Lack of Timely Enforcement Action on missing FS5 Submissions

FSS Rules, 1998, require every employer to remit to IRD a monthly return, comprising the total amount of tax deductible from emoluments paid to employees, as well as the latter's share of SSC deductible from their salaries, together with that part of the contribution payable by the employer. Rule 15 of FSS Rules stipulates that such remittance should be made by the last working day of the month, following that during which the employer has made payment of emoluments, using the appropriate FS5 Form.

As shown earlier in *Table 2* under the 'Background', on 18 January 2013, IRD issued 2,539 FS5 Defaulters Notices, to employers who failed to submit one or more FS5 forms, together with the related payments due for basis year 2012. A year before, on 9 February 2012, the Department had issued 2,592 similar Notices, relating to the preceding year.

NAO noted that during both 2012 and 2013, the only enforcement exercises on missing FS5 submissions were carried out once at the beginning of each year, by means of FS5 Defaulters Notices. No subsequent follow-up was made against those who failed to send the missing documentation and the respective payment, thus increasing the likelihood of late payments of contributions by employers and untimely follow-up action by the Department.

## ***Class Two Social Security Contributions***

### ***Outstanding Contributions not traceable in the Taxpayer Statement***

IRD verbally confirmed that SSC related transactions cannot be viewed in the 'Taxpayer Statement' menu in ARS, since the latter portrays only those entries related to tax. As a result, users within the Department cannot easily access outstanding contribution balances for each basis year, by any defaulter, in real-time. Such information is only retrievable, either by going through the entries in the individual 'Taxpayer History' in ARS, by accessing the Return Capture Module, or by requesting a list of outstanding balances from the Computer Section.

However, when requested to confirm pending balances of selected taxpayers, the Computer Section only provided this Office with data relating to the balances due as from 1 January 2009 onwards. Consequently, NAO had to go through individual transactions in order to trace any payments made by the respective defaulters. This approach was very time consuming.

Unless SSC balances due are directly accessible from ARS, this could impinge on the users' ability to respond to queries and eventually act promptly in the Department's interest.

## ***Compliance Issue***

### ***Class Two Social Security Contributions***

#### ***No Enforcement on Penalties inflicted***

In terms of Article 14(1) of the Payment of Provisional Tax Rules, when any provisional tax is not paid by the due date, additional tax at 1% per month or part thereof is charged as a penalty, until such tax remains unpaid. In view of the fact that, for practical reasons, SSC Class Two claims are issued along with claims for Provisional Tax, the same rules apply to outstanding contributions.

The audit revealed a lack of consistency in the application of this tax, depending on when self-occupied individuals settle their outstanding dues. This non-compliance with existing regulations on the late payment of contributions, results in a loss of revenue to Government.

## ***Recommendations***

### ***Key Issues***

#### ***No Enforcement on Pre-1998 Arrears of Revenue***

The Department is to review the information it has available in order to assess the possibility of identifying any Pre-1998 defaulters that could be acted upon. The results could be reported in the forthcoming ARR.

### ***Class One Social Security Contributions***

#### ***Enforcement Measures***

IRD is expected to increase its efforts to ensure that defaulters are followed up in a timely manner. Official reminders are to be sent to the respective employers as soon as the amounts become due.

After the lapse of the 10-day credit granted by means of Default Notices, the Department is expected to adhere to its established procedure of issuing the relative Demand Notices, followed by appropriate legal action, if necessary.

#### ***Insufficient Monitoring and Follow-up of Settlement Agreements***

IRD is to ensure that each agreement is monitored on a regular basis for compliance, in order to ensure that what is due to Government is duly collected without unnecessary delays.

In cases where an agreement has been dishonoured, the Department is expected to issue a Notice of Default immediately, to inform the respective employers of any missed payments. The Department is then to proceed with the revocation



of the said agreements, implying the reversal of the reductions in penalties, where necessary.

### ***Class Two Social Security Contributions***

#### ***Lack of Appropriate and Timely Enforcement Action***

Defaulting taxpayers are to be continuously monitored and invariably followed up periodically. In addition, following the lapse of the 15-day credit granted as per the Informative Notice issued, immediate follow-up action by way of a Judicial Letter is expected. Further enforcement as necessary is to be ensured, in order to maximise collections as much as possible.

#### ***Insufficient Monitoring and Follow-up of Settlement Agreements***

Management is to ascertain that an effective mechanism is in place to monitor and follow-up all settlement agreements, in order to maximise collection of revenue to Government.

#### ***Credits and Exemptions***

Enforcement and compliance can be increased through further liaison between IRD and DSS. The former is to follow-up its request to create a common source, from where the required information may be accessed by both Departments, and collaborate with DSS in order to attain such records through an on-line system. This would ensure that officers working in either of both Departments are dealing with the same data, and that specific queries raised by taxpayers, whether addressed to IRD or DSS, are replied to in a consistent manner. As a result, IRD would be better equipped to perform enforcement action on taxpayers having adjustments for credits or exemptions, and thus ensure that outstanding SSC reported in ARR is more accurate.

### ***Control Issues***

#### ***Class One Social Security Contributions***

#### ***No Enforcement Action on Outstanding Balances below a set Threshold***

An annual statement is to be invariably sent to all defaulting employers, requesting settlement of pending SSC. This would prompt defaulters to settle any balances and maximise Government's revenue.

#### ***Penalty Remissions not automatically accounted for in the System***

Management is encouraged to enhance ARS, to provide the function of automatic reduction of penalties in line with the conditions of agreements reached. Until this function is implemented, regular reconciliations are recommended to ensure that the necessary adjustments are posted in ARS within the least possible delay.

#### ***Lack of Timely Enforcement Action on missing FS5 Submissions***

FS5 Defaulters Notices are to be sent on a more frequent basis, to ensure timely payment of SSC and minimise instances of balances falling in arrears. Defaulting employers are to be continuously monitored and periodically followed-up.

### ***Class Two Social Security Contributions***

#### ***Outstanding Contributions not traceable in the Taxpayer Statement***

Users are expected to have access to SSC outstanding balances at any point in time, enabling them to have a more complete and up-to-date overview of each case. Thus, Management is to consider submitting a request to enhance the System.

## **Compliance Issue**

### **Class Two Social Security Contributions**

#### ***No Enforcement on Penalties inflicted***

IRD is to ensure that the appropriate penalties are fairly imposed on all defaulters, in particular those who settle their arrears in the following years when these become due. NAO also recommends that the respective penalties on unpaid balances are included in all Informative Notices issued by the Department, and that the penalties are properly enforced.

## **Management Comments**

Management concurred with the majority of findings, and has already acted upon a number of SSC defaulters mentioned in this write-up, either by means of Court action, or by entering into a settlement agreement. The general recommendations put forward by NAO will be considered in the upcoming review of the FSS/SSC and SSC Class Two systems.

As a general comment, IRD stated that over 76% of active employers do not have any arrears due, whilst the arrears' balances of Class One SSC as at December 2012, represented only 4% of amounts collected since the year 2000.

With regards to payments relating to a settlement agreement not easily identifiable in the system, Management stated that efforts are underway to amend the current remittance system, enabling payments to be allocated to the respective balance on a real-time basis to ensure traceability. A summary of other comments submitted by IRD are detailed below:

#### ***No Enforcement on Pre-1998 Arrears of Revenue***

Whilst acknowledging the course of events that led to the lack of enforcement on Pre-1998 contributions, IRD maintained that the employer data capturing system was not designed to capture any information related to SSC, since the assessment system operated at that time could not

generate such claims. The system limitations, together with the limited information passed on by DSS in 2006, resulted in unreliable and incomplete information, which could hardly be followed-up more than nine years after they occurred. To this effect, it is practically impossible to derive the amounts due for such periods.

### **Class One Social Security Contributions**

#### **Enforcement Measures**

Management stated that regarding the performance of the collection function, during 2012, IRD coordinated the arraignment of 2,428 employers to Court, whereas in 2013, the number increased to 4,700. The majority of these employers regularised their position by availing themselves of an instalment plan. The Department also stated that automation of issuing Default and Demand Notices is planned for 2015.

#### **Insufficient Monitoring and Follow-up of Settlement Agreements**

The Department highlighted the fact that approximately 88% of employers who entered into an instalment plan with IRD, relating to Phase Two of the Exemption Order Scheme, have honoured their agreement in full.

#### **No Enforcement Action on Outstanding Balances below a set Threshold**

IRD is revising its approach in enforcement action. To this effect, in the employer statement which started being issued recently, the threshold is being based on the number of months elapsed since the last action taken. This would ensure that all employers are subject to action on a rotation basis, at least once annually, irrespective of the amount due.

#### **Penalty Remissions not automatically accounted for in the System**

IRD has requested the Malta Information Technology Agency to implement the required enhancement, to cover the reduction in penalties *vis-à-vis* settlement agreements, which task is now in an advanced stage of development.

### Lack of Timely Enforcement Action on missing FS5 Submissions

The Department is considering to review the submission frequency of the FS5 for small employers, so that follow-up action may be carried out more effectively.

### *Class Two Social Security Contributions*

#### Credits and Exemptions

Management agreed that the implementation of a real-time web service between IRD and DSS would be a possible solution to ensure consistency of information provided to the public by both Departments, besides assisting the Department's enforcement efforts.

Table 3: Class One – Lack of Enforcement Action

Employer	Basis Year(s)	SSC Due	Default Notice	Demand Notice	Warning Letter	Judicial Letter	Garnishee Order/Writ of Summons	Payments	SSC Balance as per date of testing
		€						€	€
Employer 1	2004 - 2010	2,077,046	13 February 2013	Not sent	NA	Not sent	Not sent	-	2,077,046
	2011 - 2012	789,622	Not sent	Not sent	NA	Not sent	Not sent	-	789,622
		<u>2,866,668</u>							<u>2,866,668</u>
Employer 2	2000 - 2009	838,257	8 April 2009, 4 March 2010	Not sent	NA	Not sent	Not sent	-	838,257
	2010	191,489	15 May 2012	15 February 2012	NA	Not sent	Not sent	-	191,489
	2011	201,866	15 May 2012	Not sent	12 September 2012	Not sent	Not sent	-	201,866
	2012	235,819	15 March 2013	Not sent	NA	Not sent	Not sent	-	235,819
		<u>1,467,431</u>							<u>1,467,431</u>
Employer 3	2012	198,206	Not sent	Not sent	NA	Not sent	Not sent	-	198,206
Employer 4	2002 - 2005	24,563	Issued prior to year 2007	Issued prior to year 2007	NA	18 July 2007	Not sent	16,908	7,655
	2006 - 2009	93,022	4 April 2009, 9 July 2010	Not sent	NA	Not sent	Not sent	-	93,022
	2010	42,613	7 December 2011	15 February 2012	NA	Not sent	Not sent	-	42,613
	2011 - 2012	48,188	Not sent	Not sent	NA	Not sent	Not sent	-	48,188
		<u>208,386</u>						<u>16,908</u>	<u>191,478</u>

Table 3: Class One – Lack of Enforcement Action cont./

Employer	Basis Year(s)	SSC Due €	Default Notice	Demand Notice	Warning Letter	Judicial Letter	Garnishee Order/Writ of Summons	Payments €	SSC Balance as per date of testing €
Employer 5	2005 - 2010	53,489	7 December 2011	15 February 2012	NA	Not sent	Not sent	-	53,489
	2011 - 2012	18,432	30 October 2013	Not sent	NA	Not sent	Not sent	-	18,432
		<u>71,921</u>							<u>71,921</u>
Employer 6	2011	36,441	Not sent	Not sent	NA	Not sent	Not sent	-	36,441
	2012	27,320	15 March 2013	Not sent	NA	Not sent	Not sent	-	27,320
		<u>63,761</u>							<u>63,761</u>
Employer 7	2010	1,624	7 December 2011	Not sent	NA	Not sent	Not sent	-	1,624
	2011 - 2012	100,744	Not sent	Not sent	NA	Not sent	Not sent	40,039	60,705
		<u>102,368</u>						<u>40,039</u>	<u>62,329</u>
Employer 8	2010 - 2011	37,965	30 October 2013	Not sent	NA	Not sent	Not sent	-	37,965
	2012	22,286	15 March 2013, 30 October 2013	Not sent	31 May 2013	Not sent	Not sent	-	22,286
		<u>60,251</u>							<u>60,251</u>

Table 3: Class One – Lack of Enforcement Action cont./

Employer	Basis Year(s)	SSC Due	Default Notice	Demand Notice	Warning Letter	Judicial Letter	Garnishee Order/Writ of Summons	Payments	SSC Balance as per date of testing
		€						€	€
Employer 9	2010	7,662	7 December 2011	15 February 2012	NA	Not sent	Not sent	5,844	1,818
	2011 - 2012	54,886	30 October 2013	Not sent	NA	Not sent	Not sent	-	54,886
		<u>62,548</u>						<u>5,844</u>	<u>56,704</u>
Employer 10	2006 - 2008	31,218	7 December 2011	15 February 2012	NA	12 March 2010	Not sent	-	31,218
	2010	3,471	7 December 2011	15 February 2012	NA	Not sent	Not sent	-	3,471
	2011	18,153	30 October 2013	Not sent	NA	Not sent	Not sent	-	18,153
		<u>52,842</u>						-	<u>52,842</u>
<b>Totals</b>		<b><u>5,154,382</u></b>						<b><u>62,791</u></b>	<b><u>5,091,591</u></b>

# St. Vincent de Paul Residence

## Overtime and Allowances

### Background

St. Vincent de Paul Residence (SVPR) is Malta's largest state-funded residence for the elderly. It is a hybrid between a nursing home and a hospital with a total population of over 1,100 residents. Such residents benefit from various services including medical, dental, pharmaceutical, podiatry, occupational therapy, physiotherapy, speech therapy and social work. The recently set up Active Ageing Unit also aims to enhance the quality of life of residents by providing both group activities and personalised services.

The average number of SVPR employees in 2013 was 1,106. The Financial Estimates Recurrent Vote 28 Cost Centre 03 show that the budgetary allocation, with respect to Personal Emoluments for this year, stood at €23,622,400. Of this amount, €4,740,800 (20%) and €1,218,000 (5.1%) were allocated to Allowances and Overtime respectively, which were both substantially exceeded during the year under review.

According to the Residence's Paylist, €6,885,059 was incurred on allowances while €2,187,144 was spent on overtime. Although Departmental

Accounting System records failed to reflect these amounts as at audit date, the Elderly and Community Care Department confirmed these figures. An additional €220,000 was disbursed for Continuous Medical Education and Continuous Professional Development, also considered as allowances, thus increasing the respective amount to an aggregate of €7,105,059.

### Audit Scope and Methodology

The objectives of the audit were to determine whether adequate controls were in place in relation to allowances and overtime, as well as to confirm that the applicable collective agreements and regulations were adhered to, for the award and payment thereof.

Testing focused on allowances and overtime paid to SVPR employees in 2013 as these were deemed substantial. From a review of payroll information it transpired that the highest allowance, amounting to €58,748, was paid to a Consultant. During the same year, the average annual allowance per employee stood at €6,225. *Table 1* gives some statistics on allowances paid during 2013.

**Table 1: Allowances paid to Employees during 2013**

Amount received in Allowances	No. of Employees
Between €50,000 and €58,748	7
Between €40,000 and €49,999	5
Between €30,000 and €39,999	5
Between €20,000 and €29,999	4
Between €10,000 and €19,999	184
Between €5,000 and €9,999	312
Between €1,000 and €4,999	484
Between €33 and €999	143
<b>Total</b>	<b>1,144</b>

On the other hand, the highest overtime payments, amounting to over €21,000 each, were received by two Nursing Officers, whilst overtime paid to another 28 employees individually ranged from €10,000 to €16,600. Additionally, others had high accumulation of balances of Time Off *in Lieu* (TOIL) running into thousands of hours.

Various meetings were held with Management and Administrative Officers during the course of the audit, in order to gain knowledge about internal controls and adopted procedures. A sample of 10 employees, spread out amongst the classes of Doctors, Nurses, Nursing Support Services and Hotel Services, was selected for testing, based on materiality of the amounts involved. A review of the policies and procedures for the administration of Sick Leave (SL) and for additions and deductions to TOIL balances and the relative records maintained was also performed.

### **Limitations on Scope of Audit**

The objectives and the completeness of the audit examination were hindered as adequate information was not presented as mentioned below:

#### **Incomplete Time Off *in Lieu* Records**

On 20 January 2014, the National Audit Office (NAO) requested SVPR to provide spreadsheets recording TOIL for the year 2013 and testing was performed accordingly. However, in mid-

February 2014, this Office was made aware that the Leave Section was still receiving TOIL documents pertaining to the previous year. As a result, the audit testing had to be performed on incomplete information made available.

#### **Vacation Leave Module not in operation**

Audit testing on Vacation Leave (VL) could not be performed. SVPR claimed that the respective module within the Payroll System was not operating properly due to a system overload.

#### **Attendance Records**

##### **Conflicting information**

During the introductory meeting, NAO was informed that, after October 2013, employees stopped using the punch clock to record their attendances as this attendance recording system was replaced by the use of attendance sheets. However, testing revealed that even before and until October 2013, a number of officers were simply noting their attendance manually on the punching cards, with no actual punching being made. Upon enquiry, Management confirmed that the punch clocks were in fact not being used following Union directives.

Although NAO was informed that both punch clocks installed in the Administration Building are obsolete, Management was not aware when such punch clocks stopped operating.



## Unreliable Evidence made available

NAO requested information about the officers who were previously using the punch cards. However, the list provided was deemed unreliable as it did not even comprise the three officers out of 10 included in the audit sample who, testing revealed, noted their attendance on punch cards throughout the period sampled for testing.

## Key Issues

### Consistent use of Overtime

Public Service Management Code (PSMC) Section 3.2.1.1, which requires that overtime work is resorted to only in exceptional circumstances, was not duly followed. As already noted in this Report, the actual overtime expenditure amounted to €2,187,144, thus exceeding the allocated budget of €1,218,000 by 80%. This expenditure confirms that, with an average monthly overtime cost of €182,262, overtime is being resorted to consistently by SVPR.

Management maintained that overtime cannot be resorted to only in exceptional circumstances due to the reasons hereafter:

### Staff Ratios

The caring staff complement depends on established ratios<sup>1</sup>, based on the number of residents in each ward. SVPR claimed that, besides the fact that any absences have to be compensated by overtime work to ensure that the elderly residents are provided with the necessary care, there is also a substantial shortage of 165 Carers.

### Union Agreements

According to SVPR, early in 2013, Union agreement with the Department for the Elderly was reached, resulting in the removal of the previous monthly capping of 70 overtime hours per employee. Restriction over the approval of

VL was also removed through the same agreement with the result that all VL requested is now authorised, provided that this is compensated for by other staff working overtime.

The above claims, however, could not be confirmed by NAO since they were not substantiated with documented evidence.

Additionally, the audit revealed that two out of 10 officers in the sample, who were also among the highest overtime income earners, availed themselves of SL immediately after the performance of overtime<sup>2</sup> in a number of instances. Thus, the possibility that SL was being abused, to the detriment of higher overtime expenditure, cannot be excluded.

### Attendance Verification

#### Attendance Verification Systems and Devices not introduced

Article 8.4 of the previous Collective Agreement for Employees in the Public Service, which was valid until the year 2010, stated that *“The Employer and the Unions agree to introduce modern mechanical and/or electronic systems for the purpose of security, recording attendance, salary computation and audit trails”*. Although the current Collective Agreement does not make reference to this requirement, PSMC still stipulates that the Government was bound to introduce Attendance Verification Devices in all its places of work by not later than December 2010.

However, NAO noted that staff attendance, with the exception of those above Scale 5 who are not required to sign for their attendance, was still being recorded manually during the year. A number of employees<sup>3</sup> were manually noting their attendance on punch clock cards up till the end of October 2013, but all employees were using attendance sheets thereafter.

<sup>1</sup> More detail on ratios is given in a separate observation entitled ‘Staff Complement Ratios’ included under ‘Control Issues’ within this Report.

<sup>2</sup> More detail is given in a separate finding entitled ‘Performance of Overtime before/after Sick Leave’ under ‘Control Issues’.

<sup>3</sup> Reliable information regarding the exact number of employees noting their attendance on punch clock cards was not made available to NAO. This fact was also noted as a ‘Limitation on Scope of Audit’.

### Lack of Control over Attendance Records

The audit revealed a lack of control over the record-keeping of hours worked as follows:

- a. Unlike the Medical Staff's attendance sheets, those pertaining to the Nursing and Carers Section and the Hospital Services Section were not certified correct by an authorised officer, in compliance with PSMC Section 3.1.2.1. Manual punch clock cards<sup>4</sup> were also not endorsed. Following NAO audit enquiries, an attendance policy incorporating this procedure was drawn up and issued by SVPR Management through an Internal Memo.
- b. No evidence was made available to confirm that checks/reconciliations were made by SVPR to ensure that extra hours worked were not compensated through the payment for overtime and added to TOIL balance at the same time.
- c. A return is sent daily from each ward/section to inform the Punching Section whether the respective officers reported for work, or to justify the reason for absence. However, checking of such records was not evidenced to confirm that officers' absences were duly documented and authorised.

### *Overtime Approval not sought from the Permanent Secretary*

The responsibility for regulating overtime work is vested within the respective Permanent Secretary (PS) as per PSMC Section 3.2.1.2 and this authority cannot be delegated. Notwithstanding such provision, PS approval to cover overtime performed within SVPR was not sought.

Upon enquiry, Management stated that the fact that SVPR is a hospital, and not a Department, has to be taken into consideration. Nevertheless, officially documented policies or procedures specifically regulating overtime at SVPR, if any, were not made available to NAO upon request.

During the introductory meeting held on 20 November 2013, Management claimed that the Manager Nursing Services authorised the overtime performed by the Care and Nursing Staff, whilst the Hospital Planning Manager authorised that performed by the Domestic Staff. All other overtime was authorised by the Chief Executive Officer (CEO). These claims, however, could not be confirmed as the relevant documentation, containing the official request and authorisation for the performance of overtime for the sample of employees reviewed, was not presented for audit purposes.

### *Overtime paid not adequately substantiated*

Testing of documents made available by SVPR revealed that Overtime Returns are compiled, bearing the officers' identification and overtime hours worked, amongst others. Spreadsheets are then compiled on the basis of these Overtime Returns for the Payroll Section to issue the relative payments accordingly.

However, this Office has reservations regarding the records kept by SVPR. Besides the fact that Attendance Records, which also include overtime, were not certified correct, as highlighted in the audit observation entitled 'Attendance Verification' under 'Key Issues', it also transpired that the respective Overtime Returns were not always endorsed by the officer in charge. Moreover, the timings on these Overtime Returns and Attendance Records do not always reconcile. SVPR claimed that such discrepancies arise as overtime payment excludes breaks, besides the possibility that employees may record actual time of arrival, which very often is earlier than required.

An Internal Memo regulating the payment of overtime working hours was issued on 27 November 2013, *i.e.* in the initial stages of this audit. SVPR confirmed that written guidelines, regulating compensation for overtime duty hours, were not available prior to this date. Nevertheless, NAO still attempted to corroborate the overtime hours paid to the said Memo, but such attempts were not always satisfactory.

<sup>4</sup> As previously noted, these cards were simply used to note employees' attendance manually and not in conjunction with the punch clock(s).

## Officers certifying own Overtime

From an analysis of SVPR annual payroll data it transpired that during 2013, the top overtime earners were employees in the Nursing and Carers Category. Testing revealed that two Charge Nurses signed the Overtime Returns in which their own overtime was included, which amounted to €2,177 and €444 respectively during the four-weekly period selected for the purpose of this audit. It is relevant to note that in 2013 these officers received a compensation of €21,777 and €4,261 respectively for overtime performed.

## The Payroll System

### Potential of the Payroll System not exploited

Management claimed that the use of the Payroll System in place at SVPR is limited to that of a 'glorified typewriter', due to the fact that its overall information technology system is rudimentary and cannot support the Payroll System and installation of the relative updates. Personnel in charge of payroll still use spreadsheets to compute the various calculations, the results of which are inputted into the System.

### Administration of Vacation Leave

Employees' leave records were not being updated regularly to reflect actual leave balances during 2013. This situation made it possible for officers to make use of VL even when the respective entitlement was already exhausted.

## Control Issues

### Time Off in Lieu

#### Background

SVPR Memo dated 20 February 2007 regulates the procedure to be adopted for VL, SL and other absenteeism. Amongst others, this Memo states that approval is to be obtained prior to working the extra hours, which are eventually to be compensated with TOIL. The relative documentation should be forwarded to the Leave Section immediately after the performance of such work. Documents confirming the prior approval of absences taken

as TOIL should also reach the Leave Section as soon as possible, in order to facilitate the update of records on the payroll package. TOIL record cards were distributed to each employee to facilitate individual record keeping, whilst also enabling reconciliation of balances with the Leave Section.

The Memo further states that Heads of Sections and employees are to ensure that negative TOIL balances do not arise, since such situation may be rectified either by means of a deduction from the VL entitlement, or from salary.

NAO requested to review TOIL records and supporting documents of the 10 employees included in the original sample. However, only six were tested as one of the sampled employees never had any TOIL records, whilst TOIL balance of the other three remained unchanged from the previous year.

### Absence of Official Standard Guidelines

Although there was a widespread use of TOIL, official standard guidelines of the relevant procedures do not exist. Re-computation to confirm the balances for audit purposes had to be performed by NAO by trial and error, following various enquiries put forward to the officers in charge.

As already noted under 'Limitation on Scope of Audit', this also means that the information submitted to NAO for audit purposes as at end 2013 could not be considered as complete.

### Records kept on Spreadsheets

A record of TOIL, including additions, deductions, and the running balance, was kept on Excel spreadsheets, and not on the payroll package, as originally intended. This is not in line with SVPR's plans to maintain such records on the payroll package, in accordance with the above-mentioned Memo.

### Excessive Accumulation of Balances

An analysis of TOIL balances revealed excessive accumulation of the foregoing, which, by the end of the year, hours exceeded the one thousand mark each in the case of 11 employees. In one of these

instances, the maximum available TOIL balance stood at 4,946 hours. In aggregate, employees have accumulated an aggregate of 146,528 hours as TOIL.

### Negative Balances

Negative TOIL balances, which ranged between - 0.01 and - 212 hours, were also evidenced in the case of 71 employees.

### Inaccuracies in Records

Several inaccuracies in TOIL records were noted in the sampled employees tested, resulting in an incorrect balance.

### Sick Leave

#### Sick Leave not supported by Medical Certificates

SVPR 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 the SL taken during the year by the 10 sampled officers revealed instances which were not covered by the necessary medical certificates.

#### Performance of Overtime before/after Sick Leave

Two of the highest overtime income earners availed themselves of considerable SL. In the case of one of these employees, nine separate days SL, out of 16 in 2013, were taken immediately after the performance of overtime. In the case of the other, eight out of 21 days SL also followed overtime.

It transpired that such abuse had already been noted by Management earlier on. As a matter of fact, an Internal Memo, dated 11 October 2006, did restrict overtime as follows:

- When an employee who had worked on overtime on a particular day or night, and was duty by roster the following day or night, reported sick, this was considered as abuse of SL. In fact, those who reported sick following overtime duty, were excluded

from working overtime/TOIL for 10 days following the day in question.

- Reference was also made to the fact that the restriction preventing employees from performing overtime for seven days following each SL taken still applied.

However, in correspondence dated 21 January 2014 exchanged during the audit, the Manager Nursing Services indicated that the restriction preventing officers from performing overtime for a number of days after SL was lifted following agreement with the Union. Such restrictions may now only be exercised at Management's discretion should it be established that an employee was abusing the system. However, the highlighted observation does not indicate that such necessary action was taken, at least in 2013.

### Doctors' Extra Duty Allowance

#### Background

Doctors are normally expected to work 40 hours per week but, as medical presence is required around the clock, extra hours are included in Doctors' weekly rosters. Compensation is effected through an Extra Duty Allowance<sup>5</sup> (EDA), which is paid at plain time rate for the first five extra hours, and at the rate of 1.5 when the aggregate 45 hours are exceeded in a particular week. Extra work on Sundays is paid at double rate, whilst that performed on Public Holidays is paid at the rate of 2.5.

Doctors record their attendance for work by signing the respective register and logging their arrival and departure times. The hours worked are manually calculated and inputted onto a spreadsheet in order to calculate EDA.

#### Inaccurate Extra Duty Allowance

The sample selected for audit purposes included two Resident Specialists, who are also required to perform 24-hour duties, and who during 2013 were paid EDA, amounting to €34,252 and €40,420 respectively. A total of four payments pertaining to such allowance, in aggregate amounting to

<sup>5</sup> Source: Article 23 of the Memorandum of Understanding between the Government of Malta and the Medical Association of Malta dated 27 February 2013.

€12,475, were tested. The discrepancies noted by NAO were brought to the attention of the Payroll Section and had to be adjusted for in the following payroll.

### Staff Complement Ratios

#### Background

Although not substantiated, Management stated that the caring staff complement at SVPR is pre-determined by ratios which are based on United Kingdom high dependency benchmarks. These ratios are as follows:

- One Health Care Worker for every five residents in the morning (07:00 to 13:00 hours).
- One Health Care Worker for every seven residents in the afternoon (13:00 to 19:00 hours).
- Three Health Care Workers in every ward at night, reduced to two in wards containing fewer than 30 residents.

The above staff complement is adjusted depending on the presence of patients under constant watch, or to accompany residents outside SVPR, as necessary. This staff complement must always comprise two Nursing or Deputy Nursing Officers, whilst usually the rest are Carers.

#### Absence of Supporting Documentation

As indicated by way of background, the agreement substantiating the said ratios was not available. As a result, claims that the relative agreement to cover an established staff complement was reached, between the three Unions involved and the Director for Elderly and Community Care, could not be corroborated.

Additionally, the fact that Management was not aware whether there was a related official file or not, raises questions about the basis of these ratios, in particular, whether a professional study specifically commissioned to cater for SVPR's operations was performed, or otherwise.

### Inconsistent Information

In a communication dated 17 January 2014, NAO was informed that during the night, it was agreed with the Unions that wards with less than 35 patients should have two Health Care Workers, wards with 35 to 40 patients should have three Health Care Workers, while wards with more than 40 patients are expected to have four. This conflicts with information received from the same source through another communication dated 18 December 2013, where it was stated that there should be three Health Care Workers in every ward at night, but only two in wards containing less than 30 residents.

### Medical Staff deployed at other Hospitals

#### Background

During 2013, the Department for the Elderly and Community Care issued invoices, in aggregate amounting to €705,247, to recharge for 15 employees' salaries who were on SVPR's payroll but deployed elsewhere. This consisted of a full recovery in respect of eight employees working at Rehabilitation Hospital Karin Grech (RHKG) and a proportionate charge in respect of seven employees working on rotation at SVPR, Mater Dei Hospital and RHKG.

### Incorrect Recharge of Doctor's Salary

The selected sample included a Resident Specialist, whose salary paid during 2013, amounting to €77,258, was recharged to RHKG. Initially, testing indicated an undercharge of €2,715 for the period 10 September to 7 October 2013. However, following audit queries, the Medical Superintendent confirmed that the same Officer reported for work at SVPR and was only deployed to RHKG in mid-December 2013. Thus, it transpired that almost the entire salary was incorrectly recharged.

### Slow Recovery of Amounts Due

A list of receivables and payables with respect to salaries for officers paid by SVPR but deployed elsewhere and *vice versa* was not made available

for audit purposes. Following enquiries regarding the recovery of the amounts due, the Financial Controller, Department for the Elderly and Community Care claimed that *“Payments are slow (if non-existent)”*.

### **Working Schedules**

#### **Background**

Numbered rosters for employees working full-time, as well as on reduced hours, are kept on a spreadsheet. Forms indicating the current rosters worked by employees are retained in their personal files and a new form has to be filed every time an employee changes his/her roster. During the introductory meeting, NAO was informed that the Director is required to approve new rosters.

#### **Approval of Roster Schedules not evidenced**

The following shortcomings were noted with respect to Roster Schedules' approval:

- a. A *“... schedule of approved rosters ...”* dated 11 November 2008, provided by one of the Managers, consisted of a total of 179 different rosters. Upon enquiry, the latter claimed that the schedule contained rosters which were approved by *“... the Director within the Health Department”*. However, no source document substantiating this statement was traced.

Subsequently, the Payroll Section provided a different schedule of rosters assigned to SVPR employees which, as at audit date, amounted to 127. It was further noted that in 57 cases, only one employee was working on each of the respective rosters. Approval of applicable rosters prevailing as at audit date, by the then Director, Department for the Elderly and Community Care, was also not evidenced.

- b. Although one particular roster, namely number '12A', was included in both schedules mentioned above, the details of the shift were different. It was noted that the break was reduced by an hour, with the result that arrival and departure times of the same shift had been altered. SVPR

alleged that this change was subject to Management and employee agreement, with the acknowledgement of the Union. However, evidence of such approval was not made available.

- c. During the course of the audit, NAO was provided with a 'Flexitime Policy' dated 6 October 2013 which, amongst others, incorporated roster arrangements. However, this policy document was also not signed by Management to indicate approval, thus it could not be considered as official.

#### **Change of Roster Forms submitted at Short Notice**

During 2013 there was a Roster Form, each completed in respect of five employees included in the selected sample. In two of the foregoing, the time span between the date the Form was completed and the date the roster-change came into effect, which was of three and four days respectively, was considered to be rather short.

Moreover, the Form template included a section addressed to the Director, Elderly, requesting approval of the allowance relative to the roster. NAO noted that this was endorsed in only one of the five cases mentioned above.

#### **Monitoring of Overtime not evidenced**

Following a marked increase in overtime, in a report drawn up on 28 September 2013, CEO analysed various issues with respect to overtime. The concluding remark stated that the situation will continue to be monitored, with the following review scheduled for end November 2013. Although it was claimed that such review was carried out, no supporting evidence was made available.

### **Compliance Issues**

#### **Bi-annual Return of Allowances not prepared and submitted**

In accordance with PSMC Section 2.4.1.2, Directors responsible for Corporate Services should submit, twice yearly to the Ministry for Finance, on behalf of all the Departments

within their Ministry, a return providing detailed information regarding the payment of allowances in the respective departments, as on 30 June and 31 December.

However, although allowances paid by SVPR are substantial, and MFEA Circular No. 4/2003 – ‘Payment of Allowances’ as well as Section 2.4 of the Manual on Allowances Payable to Public Officers also spell out this requirement, the bi-annual returns for 2013 were still not prepared by mid-January 2014. Despite NAO’s request to SVPR, to submit such returns when available, the relative documentation was still not received by the time this Report was drafted.

### Care Workers’ Allowance

#### Background

The Agreement on the Payment of an Allowance to Care Workers, dated 19 July 2007, stipulates three types of weekly allowances, *i.e.* €2.33, €5.24 and €8.74, depending on the area where the officer is assigned to work.

#### Unauthorised Allowance Payments

Testing of a sampled Care Worker revealed that the actual allowance<sup>6</sup> of €1,150 paid to the latter in 2013 was equivalent to that payable to Nursing Aides and Health Assistants in accordance with the Interim Agreement on the Nursing and Paramedical Class – (Nursing Support Services Grades), dated 6 March 2008. This agreement stipulates that Nursing Aides, Health Assistants, Care Workers and Assistant Care Workers were to be assimilated into a single Caring Stream, thus SVPR paid the revised allowances accordingly.

However, no evidence was provided indicating that this assimilation was actually undertaken. In the absence of any provision specifically stipulating that Care Workers are entitled to an allowance equivalent to what is due to Nursing Aides and Health Assistants, the respective payments cannot be considered as authorised. The annual overpayment of €696 per Care Worker in receipt of Category ‘A’ allowance results in an aggregate

annual overpayment of €25,056 when all 36 Care Workers falling under this Category are taken into consideration.

#### Minimum Daily Rest Period not taken

As from 25 March 2013, one of the officers started working 13.5-hour night shifts at a stretch, as it was claimed that he was unable to take the break due to the nature of his duty. He was granted three TOIL hours monthly as compensation.

NAO noted that this does not seem to be an isolated case. Evidence made available by SVPR to support TOIL additions<sup>7</sup> contained documentation titled ‘Breaks – Extra Time’, thus indicating that, at times, staff are also compensated with TOIL for working during the break period.

Working during the break period contravenes Article 7(1) of the Hospitals and Clinics Wages Council Wage Regulation Order, S.L. 452.54, which stipulates that “*Whole-time employees in any hospital shall be allowed intervals for meals and rest of not more nor less in the aggregate than one hour on any one day*”. Upon enquiry, the Department for Industrial and Employment Relations confirmed that unless there is a collective agreement which provides better conditions of employment, the relevant Wage Regulation Order applies in the case of both public and private sector employees.

## Recommendations

### Key Issues

#### Consistent use of Overtime

A long-term solution is required to address the issue of overtime, bearing in mind the recurrent expense involved. In this regard, Management is to conduct a holistic review of SVPR operations with the aim of identifying the realistic staff complement required in order to establish whether cost savings can be effected, preferably through redeployment.

<sup>6</sup> Category ‘A’ Allowance equivalent to €1,150 *per annum*.

<sup>7</sup> From information made available, NAO could not establish what portion of TOIL hours added relates to breaks and which part relates to extra time.

## Attendance Verification

Management is encouraged to install Attendance Verification Systems, instead of the manual system currently in use, to manage effectively time-keeping and staff movement. Until such time that these devices are installed, it is to be ascertained that all attendance registers are verified and certified correct on a weekly basis by Directors or senior officers authorised by them. As per PSMC Section 3.1.2, it is to be ensured that the previous week's record of attendance is complete in every detail. The verification of records in relation to overtime, TOIL, and absence from work, is to be entrusted to responsible officer(s). Such verification is also to be evidenced.

## Overtime Approval not sought from the Permanent Secretary

Requests for the approval of overtime are to be invariably submitted to PS in the established form. Amongst other details, such requests are expected to comprise justification for the performance of overtime, total number of overtime hours requested, number and grades/positions of employees in respect of whom overtime is requested, and the period<sup>8</sup> during which such overtime will be performed.

Such authorisation is to be granted prior to commencement of the respective work. Disbursements for the payment of overtime should not be effected unless the necessary authorisations are duly obtained.

## Overtime paid not adequately substantiated

Besides ensuring that overtime is properly approved, SVPR is to implement an adequate control system to ascertain that proper records are kept, thus substantiating the performance of overtime prior to the respective payment.

## Officers certifying own Overtime

Management is to address this concern by segregating duties in order to prohibit employees endorsing their own overtime.

<sup>8</sup> The period for which approval is requested cannot exceed three months.

## The Payroll System

### *Potential of the Payroll System not exploited*

Besides the introduction of the Attendance Verification Systems mentioned in the previous recommendation, Management is encouraged to overhaul the current procedure in order to exploit all the advantages of a modern automated payroll system. This will simplify the payroll process by drastically reducing the manual work, thus decreasing the possibility of error.

### *Administration of Vacation Leave*

The entitlement to VL comes at a cost, and thus should be adequately controlled. In this respect, Management is to ensure that VL records are kept updated at all times and provide for contingent plans of action in the event that the usual recording processes fail.

### *Control Issues*

#### *Time Off in Lieu*

Management is to be reminded that TOIL also comes at a considerable cost to Government, and thus is to be adequately controlled. The introduction of Official Standard Guidelines is encouraged to ensure that the maintenance of records is harmonised across all the officers entrusted to maintain TOIL records. Additionally, it is recommended that Management endeavours to overhaul the entire TOIL process and adopt a robust recording system at its earliest, thus reducing inaccuracies. Besides ensuring that the TOIL records within such system are updated regularly, a review of balances is to be carried out periodically to ensure that they are reasonable. Negative TOIL balances should not be permitted. Controls are to be implemented to ensure that such balances are not created.

#### *Sick Leave*

Considerable overtime in excess of the official working hours may trigger exhaustion, thus increasing the possibility of resorting to SL.



Management is thus recommended to consider the option of re-introducing and enforcing restrictions similar to those in the mentioned Memo. This would also partly mitigate the risk of abuse.

#### Doctors' Extra Duty Allowance

Thorough checks are to be made to confirm that information from attendance sheets is inputted correctly on the spreadsheets. EDA calculations are also to be properly verified prior to effecting payment in order to prevent incorrect payments.

#### Staff Complement Ratios

Management is to ensure that there is an adequate audit trail for all the significant issues surrounding SVPR's operations. In particular, the source of the ratios in question, the related communication between the parties concerned, and a copy of the prevailing agreement, should be filed appropriately for ease of reference, business continuity, as well as for audit purposes.

#### Medical Staff deployed at other Hospitals

##### *Incorrect Recharge of Doctor's Salary*

The Payroll Section is to ensure that it has official notification from the Medical Superintendent defining deployment details, which are also to be filed in the employees' personal files. Moreover, sufficient verification of invoices, drawn up to recoup salaries from other entities, against deployment details, is to be carried out to ensure accuracy.

##### *Slow Recovery of Amounts Due*

NAO acknowledges that the Department has no control over the implementation of Government policies and procedures. However, the cost involved in the administration of these amounts cannot be ignored. In this regard, it is suggested that discussions are held at Ministry level, for the parties involved to be able to voice their concerns and identify possibilities of settling these amounts.

#### Working Schedules

##### *Approval of Roster Schedules not evidenced*

The administration of effective and efficient staff rosters is fundamental to ensure that good quality care is delivered to residents, whilst ensuring that staff has appropriate rest periods from work. Furthermore, although flexible work schedules and family friendly measures are encouraged, considerable diversity in working schedules may render the system too difficult to monitor effectively, since some rosters may be created to accommodate employees rather than to cater for SVPR's operational requirements. Thus, in order to strengthen controls over roster changes, the approval of the present work schedules and variations thereafter are to be invariably obtained from CEO.

It is also to be ensured that official policies and procedures are duly followed and together with the endorsed work schedules are retained in the relevant file for future reference and audit purposes.

##### *Change of Roster Forms submitted at Short Notice*

It is to be ensured that the change of Roster Forms are, in all instances, forwarded to CEO for approval. Additionally, the Forms are to be dated and submitted within a reasonable period prior to the effective date, in order to allow the necessary time for the required arrangements to be implemented.

##### *Monitoring of Overtime not evidenced*

Documented evidence supporting discussions held and decisions taken by Management is essential to monitor developments and ensure that remedial action is in line with the latter's objectives. This is also to be adequately filed for future reference.

## Compliance Issues

### Bi-annual Return of Allowances not prepared and submitted

It is to be ensured that all allowances are reviewed periodically in order to ascertain that the conditions under which they were granted still prevail. Additionally, the relevant information is to be collated and the Return submitted regularly.

### Care Workers' Allowance

Management is to ensure that disbursements are in accordance with established agreements, duly endorsed by the parties concerned, particularly Government and Union representatives. Copies of such agreements are to be adequately filed for ease of reference.

### Minimum Daily Rest Period not taken

NAO acknowledges that due to potential staff shortages, pressures from the workload may accumulate. However, individuals will benefit when taking assigned breaks since they allow a person to recover from fatigue and return to work more refreshed. Therefore, it is advisable that the regulations outlined in the specific Wage Regulation Order are adhered to.

## Management Comments

Management's reply made reference to the fact that the audit commenced only three months after the CEO's office was set up, with the post of the Human Resources Manager still vacant at that time. Thus, the audit was perceived by SVPR as a '*golden opportunity*' given that during the audit, processes and procedures relating to Human Resources operations were evaluated in depth.

The shortcomings identified by NAO will assist Management in taking remedial action, especially in those cases related to operations. The importance of proper documentation needs to be addressed immediately.

It was admitted that personnel shortages in crucial sections transformed what was intended to be an emergency measure into daily practices. Overtime and TOIL were the only practical solution to address the inadequacy of SVPR's workforce, to provide the basic care services for a long time, since Management has no direct control in the recruitment of additional employees. However, discussions were underway to enhance the workforce through outsourcing contracts.

SVPR stated that several measures designed to manage overtime, TOIL and SL, effectively and efficiently, have already been adopted. Following internal notification, all overtime performed in wards is being endorsed by the respective Senior Nursing Manager, to ensure that officers do not certify their own overtime. When working extra time, employees have to distinguish between compensation through overtime or TOIL and the relevant documentation is to be forwarded immediately for processing. Office guidelines are being drafted in this respect. Though SL is now being verified, the concerns of possible abuse, of reporting sick following overtime duty, may only be properly addressed if the staff shortage problem is solved.

Although the Payroll System was upgraded in November 2013, it is still not operating at full capacity. In this regard, the payroll package is to be further exploited for maximum operability. The reply confirmed the need of a more robust information technology infrastructure in order to address flaws in documentation, as well as the upkeep of records and monitoring, amongst others. Training of personnel employed in the Human resources sections is also required.

The Bi-annual Return of Allowances was not available as, besides the fact that its compilation is time-consuming, it was not requested by the Financial Controller. However, the Return for the year 2013 was being prepared.

Attendance sheets are being duly checked and endorsed. SVPR is in full agreement with the recommendation concerning the attendance verification system but noted that the introduction of such devices was stalled by Union opposition.

New rosters may now only be approved by CEO if the request is justified. It was again claimed that the Officer who is on night duty is the only person responsible for the entire complex. As his shift duty necessitates constant availability, compensation through TOIL is given instead of the foregone break.

With reference to the weakness under 'Inconsistent Information', Management opined that there was no conflict between the two communications, but one simply provided additional detail. Initially

it was claimed that overtime authorisation by PS is impractical as SVPR is a hospital and not a department. However, during the exit meeting, it was verbally agreed that NAO's recommendation can be implemented.

Management also stated that certain shortcomings, which have been generating over the years and are common throughout the Health Care Sector, will be escalated to a higher authority of the Public Service for remedial action.

# St. Vincent de Paul Residence

## Expenditure

### Background

St. Vincent de Paul Residence (SVPR) within the Elderly and Community Care Department (ECCD), falls under the portfolio of the Ministry for the Family and Social Solidarity (MFSS). It is Malta's largest state-funded residence for the elderly, catering for more than 1,000 beds, with the residents contributing 80% of their retirement pension and 60% of their other income.

During the year 2013, SVPR was allocated a total estimate of €7,314,300 for Operational and Maintenance Expenses through the Elderly and Community Care Recurrent Vote. Out of this amount, the Residence was assigned €3,367,000 for Utilities, €1,717,900 for Materials and Supplies, and €123,400 for Repair and Upkeep.

At the time of the audit, procurement fell under the responsibility of the Residence's management. On the other hand, the finance function of SVPR was carried out by two different sections, one located at the Residence and the other one at ECCD in St. Venera.

### Audit Scope and Methodology

The main scope of the audit was to determine the level of existing internal controls over the procurement and payment of selected line items under Operational and Maintenance Expenditure incurred by SVPR during the year under review. This exercise 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.

Two introductory meetings were held, one with SVPR officials, and another with representatives from the Finance Section at ECCD, to discuss relevant issues pertaining to the controls in place. A systems overview was also carried out to obtain a general understanding of the procurement procedure adopted by the Residence.

Targeted accounts consisted mainly of Utilities, Materials and Supplies, as well as Repair and Upkeep. A sample of 37 transactions, amounting to €631,549, was selected, based on materiality and frequency of expenditure. Selected payments were traced to Local Purchase Orders/Letters of Acceptance (LPO/LAs), invoices, Payment Vouchers (PVs) and respective fiscal receipts/tax invoices. This was done to determine whether authorisation was obtained prior to the actual purchase and that related invoices were certified correct for payments to be effected. The selected sample was also vouched against the applicable contract agreements. Reference was made to the Public Procurement Regulations (PPR) to assess whether standing procedures were followed.

### Limitation on Scope of Audit

During the course of the audit, the kitchen facility at SVPR was closed down. To this effect, the National Audit Office (NAO) did not carry out an audit of the Provisions Store, which provided food supplies to the kitchen on a daily basis.

## Key Issues

### *Repetitive Quotations requested instead of Public Calls*

Testing revealed that in seven instances from the sample reviewed, regular monthly<sup>1</sup> calls for quotes to a number of selected suppliers were issued throughout the year, through electronic mail by SVPR for the procurement of various food items. Payments made during the year 2013 to the suppliers in question totalled €487,956. The costs involved entailed that a call for tenders ought to have been published in line with PPR.

Similarly, various repetitive monthly quotations were requested for the procurement of thin fuel oil between January and October 2013, until a public call for quotations was adjudicated in November 2013, for up to a limit of €153,400. In this regard, payments made to the supplier during the year under review amounted in aggregate to €876,841<sup>2</sup>. Upon enquiry, SVPR officials maintained that this service provider has been the only bidder for such monthly quotations since June 2011, including for the above-mentioned call.

Thus, besides the issue of unfair competition, there exists the risk that SVPR may not have obtained the best market prices.

### *Purchases from Suppliers with Expired Contracts*

A tender was issued in September 2010 by ECCD for the supply and delivery of a number of food items to SVPR. As indicated in LA dated 8 July 2011, the tender was awarded to a supplier at an aggregate value of €73,869, with a period contract valid for 12 months, up to 7 July 2012, with the possibility of two successive months' extension up till 7 September 2012.

However, a new tender was not issued upon expiry, and a payment amounting to €11,571 was still effected to the supplier during March 2013, relating to an invoice dated October 2012.

### *Procurement from the Open Market instead of utilising prevailing Period Contract*

The Department of Contracts, on behalf of the Health Division, issued a tender in November 2010, for the supply of mixed vegetable soup to SVPR. As stated in the respective Evaluation Report, the one year period contract was valid up till 31 December 2012.

However, in one instance in the audit sample, 56 boxes of this item were purchased from another supplier during December 2012, directly from the open market, at a cost which was more than double that agreed in the period contract. No explanation was provided by SVPR for this direct purchase at a higher price.

### *Procurement from the Open Market without Appropriate Approval*

Testing also revealed that repetitive procurement of a number of utilities, supplies and repairs, were not carried out in accordance with procurement regulations. Such items which exceeded PPR thresholds, were procured directly from the open market, without a public call for tenders or quotations, and lacking the necessary approval from the Ministry for Finance (MFIN) or any other delegated official, as applicable. All four instances also lacked a written agreement between the particular supplier and SVPR. Total payments in this regard, made to four different suppliers, amounted to €441,748. Details of these instances follow:

- a. Total payments made to a supplier, for the purchases of various fresh dairy products at retail prices during the year 2013, amounted to €187,827. SVPR confirmed that all such procurement was made through various direct orders on the basis that this is the only supplier for fresh dairy products.
- b. Likewise, aggregate payments made during the year under review to a service provider for telephone services, amounted to €111,023. It was verbally declared

<sup>1</sup> In one case related to the procurement of bread, the call for quotations covered supplies for a three month period.

<sup>2</sup> SVPR did not confirm whether the total amount paid to this supplier was in its entirety in respect of thin fuel oil.

that such services were procured directly from the open market, due to the existing infrastructure at the Residence.

- c. SVPR did not provide information on the procurement method adopted for the purchase of 8,450 litres of heating gas oil in January 2013, at a cost of €7,487. Thus, in the absence of any documentation showing otherwise, it was concluded that such utility was also procured through a direct order. Moreover, total payments made to the supplier in question during 2013, prior to the adjudication of a public call for quotes in April 2013, amounted to €114,985. However, it could not be established whether this total pertained to the supply of heating gas oil only, since SVPR failed to provide the relevant explanations to this Office.
- d. Departmental Accounting System entries show that total payments made to a service provider throughout 2013 for lift repairs amounted to €27,913.

### ***Considerable Accrued Expenses defrayed out of 2013 Vote***

During testing, it was noted that payments for Operational and Maintenance Expenses made in 2013, in respect of 21 different suppliers and amounting to €1,011,426, related to invoices outstanding from the previous year. These payments were expensed from all three line items tested, the majority of which pertained to food items and fuel.

In this regard, it was verbally maintained that substantial claims are repeatedly spilled over from one year to the next, since most of the allocated budgets are utilised by mid-year, and thus payments fall in arrears.

### ***Lack of Communication between the two Finance Sections***

As already mentioned in the introductory part of this write-up, the accounting function of SVPR was performed by two different Finance Sections, one located at the Residence and another located at ECCD in St. Venera. LPOs and PVs are raised by the latter, whilst purchase requisitions and

procurement procedures, including checking of prices quoted in the invoices received against the applicable documentation, are carried out by SVPR.

This audit revealed that there is lack of communication between the two Finance Sections. Furthermore, responsibilities for both Finance personnel are not formalised. This resulted in time-lag between the purchase request raised by SVPR and the respective LPO issued by ECCD. As mentioned in further detail under 'Control Issues', the majority of LPOs are also issued after the suppliers' invoices are received.

Moreover, it was very time consuming for NAO to clearly identify the internal controls over procurement by SVPR, leading to the relative payments effected by ECCD.

## **Control Issues**

### ***Local Purchase Orders/Letters of Acceptance dated after Suppliers' Invoices***

In 22 payments tested, representing 69% of the sampled transactions, and amounting to €151,804, the respective LPO or LA was only issued just before the payment was effected, which in most instances was well after receipt of invoice. This may be indicative that sufficient authority was not obtained prior to the purchase and that adequate funds were not committed to cover the expense.

### ***No Contract signed for Awarded Tenders***

SVPR failed to provide a signed copy of a formal contract between the latter and two suppliers, who were awarded a tender for oxygen cylinders and gas oil, during 2012 and 2013, respectively. In aggregate, the awarded tenders amounted to €314,015. Only LAs issued to these suppliers were presented, the terms of which were not agreed upon by same.

### ***No Clear Evidence of Certification of Delivered Goods***

NAO was informed that upon delivery, officers at the Stores are responsible to check and confirm delivery of items received. Audit testing revealed that the signature of the Stores Officers in charge

to certify such receipts was not evident on eight invoices, with an aggregate value of €97,358, even though these were certified correct by the Finance Section. Up to the writing of this Report, the respective bin cards of the items in question could not be traced for verification purposes.

### ***Unverified Invoices resulting in Overpayments***

Whilst examining payments in relation to food supplies, NAO verified two PVs issued to the same supplier, amounting in aggregate to €23,118. It resulted that on three separate invoices, the rate charged for certain items was overstated, when compared to that originally agreed upon by the supplier in the submitted quotations. SVPR failed to provide any explanation for the encountered discrepancies.

## **Compliance Issues**

### ***Non-Submission of VAT Quarterly Returns***

In terms of MF Circular No. 5/2002 and MFEI Circular No. 2/2012 – ‘Submission of Fiscal Receipts to Government Departments’, suppliers/service providers who fail to provide the necessary fiscal documentation, should be reported to Value Added Tax (VAT) Department accordingly.

Such information is only submitted by ECCD annually to VAT Department, namely in June of the following year, and not quarterly as required by the said Circulars. Moreover, it was confirmed that such Return was not submitted at all to VAT Department for financial year 2012.

### ***Awarded Contracts not published***

No evidence was provided to NAO, to substantiate that SVPR complied with the standing Circular to publish in the Government Gazette, a full list of departmental contracts awarded, including those effected through the direct orders procedure. Such publication ought to have also included a list of cases involving variations, which exceed the original contract values by more than 5%.

## **Recommendations**

### ***Key Issues***

#### ***Repetitive Quotations requested instead of Public Calls***

Procurement is to be made, as much as possible, either through departmental calls for tenders, or by means of public calls for quotations that are published in the Government Gazette, as regulated by PPR. Besides ensuring better control, adherence to these requirements is intended to provide more transparency, value for money for the items purchased, as well as promote fair competition.

In view of the lengthy departmental tender procedures, better planning is to be made well in advance so as to publish public calls in time.

#### ***Purchases from Suppliers with Expired Contracts***

Management is to ensure that proper mechanisms are in place to monitor the expiry of contracts, in order to avoid similar occurrences in the future. SVPR is to issue a new departmental call for tenders for the procurement of materials and supplies in a timely manner.

#### ***Procurement from the Open Market instead of utilising prevailing Period Contract***

It is important that all purchases are made from those suppliers with whom period contracts are entered into and at the pre-agreed prices. Any deviation from contracts in place, which should be the exception and not the rule, have to be clearly justifiable and appropriately approved.

#### ***Procurement from the Open Market without Appropriate Approval***

SVPR is to invariably adhere to the requirements of PPR, to ensure fairness and provide equal opportunity to all interested parties in the provision of goods and supplies paid from public funds. Approvals from MFIN for direct orders should only be requested in exceptional cases, as spelled out in MFIN Circular No. 3/2013 – ‘Public Procurement Regulations – Direct Orders’, in

order to ensure accountability and a competitive procurement process.

Moreover, SVPR is expected to regularise the position of those suppliers and service providers not engaged according to standing procurement regulations.

### Considerable Accrued Expenses defrayed out of 2013 Vote

Invoices are not to be left to accumulate, but settled within the least possible time to avoid any negative implications. MF Circular No. 2/2007, issued by the same Ministry, also emphasises that deferred “... *claims spilling over from one year to the next are kept at the absolute minimum ...*”.

### Lack of Communication between the two Finance Sections

The entire process of procurement, and its accounting, is to be performed as one central unit.

### Control Issues

#### Local Purchase Orders/Letters of Acceptance dated after Suppliers' Invoices

SVPR is to ensure that officers observe the standard purchasing procedure, which is to issue an LPO or LA as applicable before placing an order for goods or services. This will ensure that proper authorisation for the purchase is obtained and adequate funds are committed to cover the expense.

#### No Contract signed for Awarded Tenders

The successful bidder's engagement is to be duly backed up by an agreement, signed by the parties involved, indicating the applicable terms and conditions. Alternatively, the service provider has to officially accept the conditions specified by tender, following receipt of LA.

#### No Clear Evidence of Certification of Delivered Goods

Invoices are to be properly endorsed by the Store Officer concerned, certifying that goods

and services were adequately received before payments are effected.

### Unverified Invoices resulting in Overpayments

All invoices, including any other supporting documentation on which payments are based, are to be vetted for correctness and properly certified as correct before processed for payment. Moreover, SVPR is to carry out a full exercise to identify the total amount overpaid to this supplier, following which, the Residence is to take the necessary steps to recoup the excess paid within the least possible time.

### Compliance Issues

#### Non-Submission of VAT Quarterly Returns

Quarterly Returns, highlighting those suppliers not complying with VAT regulations, are to be duly filled in and submitted to VAT Department in a timely manner for necessary follow-up.

#### Awarded Contracts not published

Officers entrusted with the responsibility of issuing Departmental tenders are to be fully aware of all relevant Circulars and to ensure compliance accordingly.

### Management Comments

In the Management Comments received as well as during an exit meeting held at NAO, SVPR agreed with NAO's recommendations and stated that necessary action is being taken to address issues highlighted in this Report. In fact, this audit confirmed concerns expressed by SVPR's Top Management.

To this effect, besides the engagement of a Financial Accounting Manager in January 2014, an Accounts Section is being set up at SVPR. Management stated that this new structure would address the problem of lack of communication, improve the monitoring of procedures, as well as increase efficiency. Furthermore, a request to engage additional staff was raised by SVPR. However, the latter is still to date awaiting approval from the Public Administration HR Office (PAHRO). It



was further remarked that PAHRO is withholding approvals across Government. A brief outline of the additional feedback received follows:

***Repetitive Quotations requested instead of Public Calls***

SVPR stated that as from 2014, all calls exceeding the threshold are being issued through eTenders and published in the Government Gazette, as regulated by PPR. Moreover, employees across the Ministry were given training on the eProcurement system.

***Procurement from the Open Market without Appropriate Approval***

Management commented that the procurement of dairy products was amalgamated with the contract of the outsourcing catering services that is being drafted. With regards to telephone services, Management reiterated that the same provider supplied this service for many years. However,

this matter will be discussed with MFIN in order to regularise its position. In the meantime, SVPR recently entered into a Maintenance Agreement with this telecommunications service provider, a copy of which was forwarded to this Office. With reference to the maintenance and upkeep of passenger lifts, SVPR declared that a tender in this respect was issued in May 2014.

***Considerable Accrued Expenses defrayed out of 2013 Vote***

Although at budget stage SVPR takes into consideration the arrears which already exist, plus the increase in costs for the coming year, it was remarked that budget allocations by MFIN are much lower than the Ministry's request. As a result, every year SVPR is ending in a negative financial position whereby approved funds are exhausted by mid-year. To this effect, efforts to reduce its expenditure are currently being made, while an increase of funds for the year 2015 was also requested.



Ministry for Home Affairs and  
National Security

# Police Department

## Personal Emoluments

### Background

The audit covered the Personal Emoluments of the Police Department for financial year 2013. The budgetary allocation under Vote 31 and actual expenditure in this regard was as depicted in *Table 1*.

The strength of the Malta Police Force (MPF) as at 31 December 2013 was 1,942 officials, a number of them related directly to community policing, based in their respective districts. The remaining members were posted in several sections of MPF.

During the same year, approximately another 120 civilians were employed with the Police Department, with roughly 50% being Immigration Officers posted at the Malta International Airport. The rest were allocated within the Finance and Administration Directorate, the Police Garage, *Ta' Kandja* Academy, Forensic Office and Gozo.

### Audit Scope and Methodology

The main scope of the audit was to verify that, during financial year 2013, salaries, as well as overtime and allowances paid to various employees, were correct. Other objectives were to determine the level of internal controls and to verify that the Conditions of Service for MPF, including other applicable regulations, were duly followed.

Various meetings were held with officers in charge, in order to obtain an understanding of the relevant policies and procedures adopted. A sample of 13 employees with different designations was selected for testing, whereby emoluments paid to them throughout 2013 were verified. Furthermore, the allowances paid to all the officers during 2013 were analysed and reviewed.

**Table 1: Personal Emoluments**

	Estimate	Actual	Difference
	€	€	€
Salaries and Wages	34,000,000	33,157,309	842,691
Bonus	560,000	543,741	16,259
Income Supplement	500,000	491,692	8,308
Social Security Contributions	3,230,000	3,282,096	(52,096)
Allowances	8,300,000	8,606,200	(306,200)
Overtime	900,000	1,362,761	(462,761)
<b>Totals</b>	<b>47,490,000</b>	<b>47,443,799</b>	<b>46,201</b>

## Limitations on Scope of Audit

Lack of supporting documentation limited the scope of audit in a number of areas, as illustrated in *Table 2*.

### Key Issues

#### *Lack of Internal Controls*

From verifications carried out on the payroll process of a sample of employees, it transpired that internal controls in various areas were lacking, indicating that little or no monitoring was in place to reduce the possibility of errors.

Despite that the Police Department engages over 2,000 public officers, there is no internal audit mechanism to ensure efficient use of resources. During the year under review, only an average of five officers were directly responsible for the payroll process of salaries of all employees.

A number of issues, as will be discussed separately further on in the Report, under the pertinent observations, could have been avoided if an internal control system was in place.

#### *Computation of Sunday Allowance not substantiated*

Payments for shifts falling on a Sunday, both for the Police officers and civilians, were still being computed in accordance with the General Headquarters (GHQ) Circular No. 63/1993, which was in actual fact superseded in 2012 with the Conditions of Service for MPF.

The National Audit Office (NAO) re-calculated the Sunday allowances paid in 2013, as specified in the Public Service Management Code (PSMC) section 3.2.6.2(b). This resulted in an overpayment of €144,203<sup>1</sup>, with respect to an aggregate difference of 20,523 hours.

**Table 2: Limitations on Scope of Audit**

Areas	Number of Officers	Aggregate Amounts received in 2013	Reasons
		€	
On-Call Allowance	83	88,768	No evidence was provided that a stand-by at home system was in place.
Salary in Arrears	2	11,913	No documentation could be traced.
Performance Bonus Rate	2	5,701	The auditee failed to provide a copy of the official document indicating the percentage rate awarded.
Board Members Allowance	11	1,090	Supporting documentation was not provided.
Collective Agreement Adjustments	3	500	The Department was not in a position to provide a justification for such payments.
Returns of Overtime	4	433	Returns were not provided.
Salary in Arrears Overpaid Salary	1	390 (843)	Supporting documentation was not provided.
Qualification Allowance	6	Paid above the norm	
Police Force Allowance	3		

<sup>1</sup> This does not include any overpayments made in cases when the Sunday duties were less than eight hours, since it was not possible to calculate the respective amounts.

### ***Weak Budgetary Control on Overtime***

As per PSMC section 3.2.1.2, the Director is to request approval from the relevant Permanent Secretary for the performance of overtime work not exceeding three months. However, Management within the Finance and Administration, confirmed that it was not aware of such approach. Hence, Permanent Secretary's approval to this effect was not sought, even though the budgeted figure of €900,000, that was planned to cover overtime for the year under review<sup>2</sup>, was exceeded by €462,761.

## **Control Issues**

### ***Incorrect Basic Salary***

Testing carried out on the basic salary, paid to the 13 employees falling in the audit sample, revealed that three of these employees were incorrectly paid. The following relate:

- a. A Superintendent did not receive the annual increments for two consecutive years.
- b. A Police Constable and Senior Clerk were paid incorrect salary steps.

### ***Divergences from the Conditions of Service not formally approved***

#### **a. Special Duty Allowance**

The document titled Conditions of Service for MPF was signed on 7 August 2012, by the Permanent Secretary of the then Ministry of Finance, the Economy and Investment (MFEI), and the then Permanent Secretary, Ministry for Home Affairs. Two days later, the former approved a further request submitted by the then Commissioner of Police, to grant the payment of special duty allowance to the Dog and Mounted Sections. The Permanent Secretary, MFEI, however remarked that no other similar requests would be considered. Subsequently, GHQ

Circular No. 50/2012 was issued in order to include the highlighted sections, but it was not signed by the Commissioner of Police. Furthermore, an addendum to this effect was not in place.

#### **b. Disturbance and Shift Allowance**

In an email correspondence dated 27 February 2013, the then Prime Minister's Head of Secretariat informed the Commissioner of Police that, after discussions held between the then Prime Minister and Minister of Finance, a revision of both the disturbance and shift allowance was approved. In March 2013, an undated draft addendum was prepared, whereby articles 5.3 and 5.7 of the Conditions of Service were updated to reflect this revision. However, the said addendum was not signed by the respective Permanent Secretaries.

### ***Shortcomings in the Returns of Overtime and Allowances***

#### **a. Incorrect Computation of Hours**

From the review of a number of returns, covering overtime and allowances for the 13 officers falling in the audit sample, several inaccuracies in the computation of hours were noted. These errors remained undetected, notwithstanding that officers in charge were endorsing the requests to be processed for payment. Thus, it is evident that no verification on the correctness of details therein was being carried out.

#### **b. Time In and Out not indicated**

Notwithstanding that returns were being endorsed by the officers in charge, the following were noted:

- All the Sundays and Public Holidays returns for 2013, compiled by an Inspector within MPF, failed to indicate

<sup>2</sup> Table 1: Personal Emoluments refers.

the time in and out. Only the total number of hours on the particular days, totalling 585 hours, were recorded.

- In another three instances, the compiling officers did not indicate the period of overtime on the related returns, and therefore, it could not be confirmed whether such overtime was carried out outside the tour of duty.

c. **Returns not endorsed**

- Two out of nine claims for payment of allowances, with respect to 80 hours performed on Sundays and Public Holidays by an Assistant Commissioner, were only endorsed by the official himself. Notwithstanding that approval from higher authority was not evidenced, the respective allowance was still processed for payment by the Salaries Section.
- Another instance was noted whereby the officer in charge of compiling the return for Sundays and Public Holidays failed to endorse and stamp the return for the month of December 2012. However, this was also processed for payment. This return covered three officers claiming 176 hours of overtime.

d. **Incorrect Rates of Overtime**

Three officers out of the nine individuals in the audit sample, eligible to be paid for overtime, were incorrectly paid at the rate of 2013 for overtime performed in 2012 or *vice versa*, resulting in inaccurate payments.

e. **Late submission of Returns for Overtime and Allowances**

Claims for payments for overtime and allowances were being submitted late for endorsement, at times even 10 months later, thus making it difficult to validate them.

f. **Double Payments**

An Inspector claimed twice for payment of allowance, covering the same hours of work performed on Sundays, during the month of April 2013. His Superintendent endorsed both returns; one was dated 3 June 2013 and paid in the same month, while the other return was dated 12 September 2013 and paid the following month.

***Overpayments made to a Retired Police Sergeant***

From a review of the allowances and overtime paid to a Police Sergeant in the audit sample, who commenced pre-retirement leave in October 2013, it transpired that during the year under review, his salary contained several errors resulting in a net overpayment of €707. The discrepancies included:

- an incorrect computation of Sunday allowance as indicated under Key Issues – ‘Computation of Sunday Allowance not substantiated’;
- a police force allowance paid during pre-retirement leave. This is in breach of the standing provisions of PSMC;
- an overtime return presented for payment twice for the same dates and time; and
- two overtime requests on a particular day overlapped by an hour and were still paid accordingly.

***Paid at Overtime Rates although not exceeding the Weekly Hours***

A Woman Police Constable, selected in the audit sample, worked on a reduced timetable of 35 hours per week. However, in two pay periods, she was remunerated for 34 extra hours claimed at overtime rates, rather than at the normal hourly rate. On both instances the respective total number of weekly hours worked did not exceed the full-time schedule of 46 hours required by PSMC section 5.4.1.7(d).

### ***Lack of Training to Staff***

The officers currently responsible for salaries verbally stated that they were neither given any training, nor an appropriate hand-over when they took over their new tasks of computing the salaries. It was also claimed that in the circumstances, documents and workings of previous salary payments, many of which were not backed up by any explanations, were the main reference.

### ***Good Honours Allowance***

During the year under review, eight officers received an aggregate amount of €4,484 with respect to good honours allowance, which payment relates to a qualification allowance amounting to €582 annually, as per section 3.4.1 of GHQ Circular No. 63/1993. However, the good honours allowance was not included in the new Conditions of Service for MPF, dated 7 August 2012.

An Honours qualification is equivalent to Level 6 - Bachelor's Degree (Honours), thus, payment to these eight officers should have been revised downwards to read €465.87 annually, to cover the qualification allowance. Furthermore, the terminology also required to be amended accordingly.

### ***Double Payment of a Special Duty Allowance***

A Police Constable eligible to receive a special duty allowance, has been incorrectly receiving this allowance of €96.76, twice every pay period, since 10 September 2012. The Police Department upheld this observation, also stating that this error was brought to the attention of the Salaries Section in May 2014. Together with the Gozo Central Salaries Section, they commenced working on the amounts needed to be recouped, which totalled €2,136. Deductions to recover the overpayment from the officer's salary were due to commence with effect from September 2014.

### ***Topping-up Allowance***

A Senior Clerk engaged as an Immigration Officer was receiving an incorrect overstated amount of topping-up allowance.

## **Compliance Issues**

### ***Incremental Dates disregarded***

During audit testing, it was noted that three out of the 13 employees falling in the audit sample did not receive their next increment on the dates stipulated in PSMC section 2.3.2.

### ***Return of Allowances not compiled***

A bi-annual return of allowances, in line with PSMC section 2.4.1.2, has not been prepared by the Police Department since June 2012.

### ***Attendance Verification System Devices not in place***

Article 8.4 of the Collective Agreement for Employees in the Public Service, covering years from 2005 to 2010, states that "*The Employer and the Unions agree to introduce modern mechanical and/or electronic systems for the purpose of security, recording attendance, salary computation and audit trails*". It further states that, "*The Employer shall endeavour to introduce these systems in all its places of work by 31st December, 2007 but not later than 31st December, 2010*".

Prior to 2008, a number of officers recorded their attendance through a finger-printer device system, installed at GHQ. However, the Police Department reverted to a manual attendance system when such device was not performing as expected.

## **Recommendations**

### ***Key Issues***

#### ***Lack of Internal Controls***

Strong internal controls are essential in assisting the Department to mitigate financial risks and achieve its objectives to manage public funds entrusted to it as efficiently as possible.

### Computation of Sunday Allowance not substantiated

Officers in charge are to ensure that the most recent official instructions are followed. In the case of Sunday allowances, PSMC provisions are to be complied with. Reference is to be made to the competent authorities for further guidance, if further clarification is deemed necessary.

### Weak Budgetary Control on Overtime

As far as possible, requests for overtime are to be raised in a timely manner to ensure that proper authorisation from the Permanent Secretary is granted prior to the commencement of the respective work. The requests are expected to include the total number of hours of overtime required, as well as justification and specific targets to be attained during overtime hours.

### Control Issues

#### Incorrect Basic Salary

A review of salaries paid is recommended in order to ensure that correct payments are made.

#### Divergences from the Conditions of Service not formally approved

Prior to implementing any instructions, officers are to ensure that addenda are in place and formally endorsed as applicable.

#### Shortcomings in the Returns of Overtime and Allowances

The Department is to ensure that internal controls are immediately strengthened. Returns for both overtime and allowances are to be duly endorsed as applicable, following proper verification and before any payments are issued.

Management is also encouraged to inform employees that unless relevant returns are compiled and submitted within a specified timeframe, these will not be processed for the respective payments.

### Overpayments made to a Retired Police Sergeant

Independent verification is to be carried out in order to strengthen internal controls. The Police Department is also expected to make an effort to recoup these overpaid amounts.

### Paid at Overtime Rates although not exceeding the Weekly Hours

It is to be ensured that officers working on reduced hours are only remunerated at overtime rates for those hours exceeding the 46 hours per week. Furthermore, officers in charge are to thoroughly review overtime paid to employees on a reduced timetable, in order to recover any ineligible payments.

### Lack of Training to Staff

Appropriate training from knowledgeable and experienced sources is expected to be given to the officers in charge of salaries.

### Good Honours Allowance

It is to be ensured that the rate paid complies with that stipulated. Any overpayments are to be recouped.

### Double Payment of a Special Duty Allowance

The Department is to exercise the necessary controls in order to ascertain that officers are paid what they are actually entitled to.

### Topping-up Allowance

An exhaustive exercise is to be carried out in order to re-calculate the amounts paid as topping-up allowance and carry out the respective adjustments accordingly.

### Compliance Issues

#### Incremental Dates disregarded

The Police Department is to carry out an intensive exercise, in order to ensure that incremental dates are as stipulated in PSMC.



### Return of Allowances not compiled

Management is to make sure that bi-annual returns, to report all allowances being paid out to employees, are compiled as required by PSMC, in an accurate and timely manner.

### Attendance Verification System Devices not in place

The introduction of attendance devices in all the locations, to be used by employees on sites, is recommended. This will increase controls over the actual hours worked, eliminate manual data entry, and simplify salary calculations as specified in PSMC section 3.1.6.1. In addition, officers in charge may easily ascertain that the 'detail of duties' is being followed.

### Management Comments

Management concurred with the majority of NAO's findings and stated that the respective recommendations are being implemented with immediate effect.

The Police Department also maintained that the shortage of civilian staff, particularly at the Salaries Section, has been a serious problem for several years. In fact, during 2013, talks were underway to transfer all work related to computation of overtime and other adjustments to Gozo Central Salaries Section, as present civilian staff were finding it impossible to cope. However, this never materialised.

Management further stated that following a request to the respective Ministry, to authorise the recruitment of an internal audit officer for the Directorate, the officer to be recruited will assist in implementing NAO's recommendations.

It was also indicated that:

- overpayments made to the retired Police Sergeant will be recouped by a letter of request;
- the issue of appropriate training will be taken up with the Centre for Development Research and Training;
- for the purpose of compiling the bi-annual returns, Management will make a recommendation to the respective Ministry in order to authorise the Department to recruit a clerk; and
- the matter of introduction of attendance verification system devices will be taken up with the Public Administration HR Office. However, the Directorate is under the impression that the implementation of these devices was to be a Public Service wide initiative and not to be taken up by departments individually.



Ministry for Finance

# Ministry for Finance

## Expenditure Audit

### Background

The Ministry for Finance's (MFIN) initial approved budget allocation for 2013, in respect of the Ministry and the Permanent Secretary's Office, was €6,315,000<sup>1</sup>. This allocation was made up of €4,456,500 for Personal Emoluments, and €1,858,500 for Operational and Maintenance Expenses.

This allocation was increased to a revised aggregate budget of €6,910,555, leading to substantial increases in various line items, such as, Incidental Expenses (€343,515), Professional Services (€155,700), Overtime (€42,000) and Equipment (€26,500).

Payments effected throughout 2013 in respect of the Ministry amounted to €758,361, whilst an amount of €5,819,890 was disbursed from the Permanent Secretary's Office Cost Centre. In total, MFIN paid €6,578,251 as against a revised budget of €6,910,555.

### Audit Scope and Methodology

The scope of the audit was to determine the level of internal controls over expenditure incurred by MFIN, and to ensure efficient administration of public funds, in line with standing laws, regulations, policies and procedures.

Audit work performed covered a sample of transactions charged to a number of accounts falling under Operational and Maintenance Expenses, from the Cost Centre pertaining to the Ministry and Permanent Secretary's Office.

A total of 62 transactions, in aggregate amounting to €1,053,265, were reviewed. Particular consideration was given to the materiality of amounts and nature of expense when selecting the audit sample. Testing was carried out to ascertain that procurement was approved by the appropriate authority levels and covered by the necessary documentation. A number of Ministerial files were also reviewed in order to assess the procurement process.

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<sup>1</sup> This includes an amount of €220,000 featuring in the Financial Estimates 2013 under the Ministry of Finance, the Economy and Investment for the period January – February 2013.

Throughout the audit, reference was made to the Public Procurement Regulations (PPR), namely, Legal Notice (LN) 296 of 2011, and the Public Service Management Code (PSMC), together with all amendments issued thereafter. Adherence to standing Finance Circulars was also verified.

## Key Issues

### *Retrospective Direct Orders to settle Outstanding Payments to a Consultancy Company*

- a. An aggregate of €404,982 worth of services was procured by direct order, from a company providing integrated marketing communications services. These covered purchases from January 2010 till January 2013. Ministerial correspondence revealed that the respective covering approval to support a total of 64 invoices, the majority<sup>2</sup> of which pertained to 2012, was only endorsed retrospectively on 8 March 2013 by the then Finance Minister.

Moreover, the approval in question was not supported with proper justification for not complying with the Public Contracts Regulations, notwithstanding the materiality of amounts involved.

Furthermore, no evidence was provided to cover approval for direct order amounting to another €11,800, in respect of consultancy services rendered during February 2013.

- b. It transpired that a total of 58 payments made in 2013, to cover €306,680 of the amount in question, mostly related to long outstanding invoices, dating back to 2010 up to 2012. Such arrear payments affect the allocated budget for the current year, as well as distort financial reporting.

### *Other Services procured by Direct Order*

Besides the previously mentioned services, additional payments totalling €127,077, were effected in respect of various other related services,

from five different service providers, through a direct order. The following shortcomings were noted:

#### No evidence of Approval for Direct Orders

The relative direct order approval for two payments, having an aggregate value of €36,022, could not be traced by the Ministry and were therefore not made available for review.

#### Retrospective Approvals for Direct Orders

Another approval for a direct order, issued on 21 August 2012 for €38,544, was granted retrospectively, since this covered legal services rendered between February 2011 and July 2012.

## Control Issues

### *Payments for Cleaning Services*

#### Background

Following a call for tender, a service provider was engaged to carry out cleaning services at three locations pertaining to the then Ministry of Finance, the Economy and Investment (MFEI), for a period of one year, starting from 1 January 2011 and could be renewed for a further two-year period of 12 months each.

The total amount of the awarded tender was of €43,436 *per annum*, out of which €42,224 (implying a total of 145 hours per week), related to cleaning services performed on a daily basis by five janitors at the rate of €5.60 per hour. The remaining €1,212 pertained to window cleaning to be carried out every four months at the same hourly rate. Any overtime required to be performed was to be charged at the rate of €6.80 per hour.

The Ministry for Finance paid a total of €56,391 in respect of cleaning services performed by the service provider in question, during the period January to December 2013.

<sup>2</sup> A total of 60 invoices, amounting to €383,330, were raised during 2012.

### Number of Janitors not as per Tender

As mentioned above, the cleaning services performed on a daily basis, as stipulated in the Tender document, were to be carried out by five janitors at three different locations for a total of 145 hours per week. However, upon verifying the respective documents attached to four Payment Vouchers (PVs), each relating to a different month, it transpired that only four janitors were performing the normal daily work, covering not more than an average of 130 hours per week. The monthly flat rate of €3,519 stipulated in the signed contract was still being charged in full.

### Non-adherence to Tender Rates and Terms

Besides the monthly charge of €3,519, it transpired that an additional cost was being invoiced for extra cleaners at one of the three locations covered by the agreement, as well as at another two premises not mentioned therein. In respect of these two premises, MFIN was being charged at the overtime rate of €6.80 an hour. To this effect, MFIN incurred additional costs, which in the four PVs tested amounted to €4,048, covering 595.50 hours. Following National Audit Office's (NAO) query, the Ministry confirmed that the service provider accepted the overcharging. This supports the fact that no verification was being performed by the Ministry before processing invoices for payment.

If extrapolated over a 12-month period, the amount overpaid by MFIN could reach approximately €12,144.

### Lack of Verification before processed for Payment

Testing of job chits/sheets supporting cleaning services, covering the sampled period, revealed that six of these, comprising 30 hours, also lacked endorsement by MFIN, thus not certifying that the service provided was satisfactory. However, although this again implies that no checking was carried out, full payment was still effected.

### Non-submission of Bank Guarantee

The service provider was obliged to submit the Bank Guarantee within seven days from the date of the Letter of Acceptance (LA), but the Bond amount was not quantified. Moreover, the former failed to submit any Bank Guarantee, thus breaching Clause 32 of the 'General Conditions of Contract for the Execution of Works in Malta'. No action was taken by the Ministry in chasing the service provider to comply.

### Contract not officially extended

Even though the same rates were maintained during the year under review, no official correspondence was issued by MFIN to the service provider, confirming the extension of the contract at the same rates, terms and conditions for the financial year 2013.

### *Proper Authority to purchase not evidenced*

In 17 payments tested, representing 27% of the sampled transactions, and amounting to €707,170, the respective Local Purchase Order (LPO) or LA was issued following receipt of invoice, which is indicative that sufficient authority was not obtained prior to the purchase.

To this effect, in 11 cases, the Officer processing the relative payments did not even endorse the LPOs in question, but only certified that the goods/services were adequately received.

### *Signatures not clearly identifiable*

In various instances, officers verifying invoices could not be identified since the signature was neither accompanied by a rubber stamp, nor was the name and position of the officer clearly written on the document. This renders it impossible to hold officers accountable, especially when it comes to ascertaining that goods and services were received as ordered.

### ***Lack of Control on the use of Government owned Vehicles and Fuel Consumption***

Audit testing revealed lack of control over Government-owned vehicles, resulting from non-adherence to the provisions specified in PSMC. Whilst reviewing whether the logbooks pertaining to five general-use cars selected for audit purposes were adequately kept, the following shortcomings were noted:

- a. During the months of January to March 2013, MFIN was making use of a hired car for general-use by the then Minister's Private Secretariat.

From a communication dated 15 May 2014, it was confirmed that this vehicle was hired from the open market, but no supporting documentation was available. Hence, it could not be ascertained whether an agreement was entered into with the supplier to establish the chargeable rates that were agreed upon.

- b. None of the five logbooks contained any evidence, confirming that these were being inspected periodically by a responsible officer, to monitor fuel consumption and to ensure that any irregular use of cars is duly reported.
- c. The logbooks pertaining to three vehicles lacked certain important information when re-fuelling. Even though the words 'petrol' or 'diesel' were written down, no details as regards the requisition number and the actual mileage were indicated. The amount of litres taken was only noted occasionally.
- d. The logbook of a vehicle in use by a Department within MFIN did not always indicate the mileage covered for every trip performed.
- e. Although according to the Fleet Management System, both vehicles were being regularly re-fuelled by MFIN, logbooks detailing trips for two vehicles for office use during particular months in 2012 and 2013 could not be traced.

- f. A number of Fuel Requisition Notes lacked the date of supply, thus it could not be ascertained when fuel was actually taken.

## **Compliance Issues**

### ***Shortcomings related to Inventory***

As indicated hereafter, inadequate control was encountered on inventory items held by MFIN.

#### **Lack of Physical Marking on Inventory Items**

At least eight<sup>3</sup> out of the 32 inventory items, selected for physical verification on-site, were not marked with the respective Asset Identification Number, in accordance with standing inventory regulations.

#### **Untraceable Assets**

An additional nine items consisting mostly of oil paintings, prints/portraits were also selected in the audit sample for physical verification, five of which were recorded as heritage assets in the Inventory Database.

However, three of these heritage assets were not found on-site. The remaining two were marked as being transferred to Heritage Malta, however, no documents were made available to substantiate the said transfer. Moreover, a catalogue for heritage assets was not maintained by the Officer in charge of inventory, as required by MF Circular No. 14/99. The remaining four sampled items not listed as heritage assets were also not physically traced on site.

#### **Assets not included in Inventory Database**

The purchase of 12 office chairs, some of which were purchased in May 2013, and a table purchased on 9 August 2013, having a total value of €1,518, were not traced to the Inventory Database forwarded to NAO for audit purposes. Even though these items were traced to a list compiled by the Officer in charge of inventory, no further information was available as to the

<sup>3</sup> This does not include those instances where items of inventory could not be physically verified, either due to their poor state or awkward position.

location of these chairs. A laser printer purchased in October 2013 and found on site was also not traced to the Inventory Database.

### Room Lists not in place or not updated

Five Room Lists were neither made available by the Officer in charge, nor hung in the respective rooms. Another Room List was not updated to reflect an item purchased in 2013.

### Mobile and Telephone Bills presented late for Payment

A number of outstanding mobile and telephone bills, pertaining to officers entitled to such facilities, were paid out of 2013 funds, even though a number of them related to previous years. This may distort the current year's budget, besides not adhering with MF Circular No. 2/2007.

### Missing Fiscal Receipt

A PV, for the amount of €21,202 in respect of legal services, was not supported with the respective fiscal receipt. This is in breach of MF Circular No. 5/2002, which besides other implications, could include undeclared fiscal revenue by the suppliers and/or service providers.

## Recommendations

### Key Issues

#### Retrospective Direct Orders to settle Outstanding Payments to a Consultancy Company

The Public Procurement Regulations are meant to ensure that the basic principles of transparency and accountability are adhered to. As emphasised in MFIN Circular No. 3/2013, direct orders should be limited to the barest minimum and provided adequate justification existed. Moreover, commitments are not to be entered into direct with the service provider before requesting the necessary approval from the Direct Orders Office, which instances are to be resorted to in exceptional circumstances only and upon proper justification.

Once procurement is made in line with standing regulations, invoices are not to be left to

accumulate, but settled within the least possible time to avoid any negative implications and additional costs. MF Circular No. 2/2007, issued by the same Ministry, also emphasises that “... it is to be ensured that claims spilling over from one year to the next are kept at the absolute minimum”.

### Other Services procured by Direct Order

As recommended under the previous ‘Key Issue’, direct orders are only to be resorted to in exceptional circumstances, as spelled out in MF Circular No. 2/2007, in order to ensure a level playingfield for all potential bidders and obtain the most competitive process for the acquisition of goods and services.

### Control Issues

#### Payments for Cleaning Services

The Ministry is to carry out a full exercise to identify the total amount overpaid to this company over the years, from commencement of service. Following this, MFIN is to take the necessary steps to recoup the excess paid within the least possible time. In order to avoid further overpayments, all invoices, including any other supporting documentation on which payments are based, are to be properly vetted for correctness and certified as correct before processed for payment.

Moreover, MFIN is to ensure that suppliers honour the terms and conditions specified in the relative tender, by issuing the required Bank Guarantee. Failure to do so, the bidder in question should be rejected.

The Ministry is to ascertain that any extended contract is covered by an official letter, informing the service provider of the same terms and conditions. This will eliminate any possible disputes.

### Proper Authority to purchase not evidenced

MFIN is to ascertain that officers observe the standard purchasing procedure, which is to issue a LPO or LA, as applicable, before placing an order for goods or services. This will ensure that proper authorisation for the purchase is obtained and, as

far as possible, adequate funds are committed to cover the expense.

### Signatures not clearly identifiable

The names of officers endorsing official documents are to be clearly identifiable. MFIN is encouraged to issue instructions, not just within the departments falling under its responsibility but, if possible, within all departments and other entities across Government, stipulating that all signatures have to be accompanied by a rubber stamp, clearly indicating the name and position of the said officers.

### Lack of Control on the use of Government owned Vehicles and Fuel Consumption

Any supporting documentation that authorises the hire of vehicles is to be appropriately maintained for future verification. As stipulated in MFIN Circular No. 6/2013, requests for the provision of vehicles are also to be forwarded to the Government Transport Policy Unit within MFIN.

Management is recommended to refer to PSMC, in particular Section 8.2.4 to regulate the use of vehicles. These guidelines stipulate that a logbook is to be kept for each vehicle to record the exact mileage covered and other journey details.

Moreover, full details regarding fuel intake are to be clearly recorded on every logbook as per Appendix 8.I of PSMC, as a means to monitor each vehicle's fuel consumption.

Section 8.2.5 of the same guidelines also requires each logbook to be certified by the Officer in charge transport at the end of each month, to ensure that the trips recorded in the logbook were made on official duty and fuel consumption is reasonable.

### Compliance Issues

#### 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.

Heritage assets are to be properly catalogued as per Circular guidelines, and any transfer of assets is to be duly recorded and supported by a proper Transfer Note, endorsed by the officer concerned.

In order to maintain control over all assets, these are to be recorded accurately within the Inventory Database. These are to be adequately identifiable and traced to the respective location. Room Inventory Lists are also to be updated to reflect latest movements.

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

#### Mobile and Telephone Bills presented late for Payment

MFIN is encouraged to issue instructions to those officers who are enjoying free telephone facilities, stipulating that their bills be presented for reimbursement in a timely manner and without any unnecessary delay, preferably within the same year when they fall due.

#### Missing Fiscal Receipt

The Ministry is to ensure that it is invariably issued with fiscal receipts from respective VAT registered suppliers.

### Management Comments

Management concurred with the majority of findings and will be taking the necessary corrective measures to address the shortcomings highlighted in this write-up.

The Ministry's calculation of the amount overpaid in respect of cleaning services, amounted to €3,564. However, NAO is of the opinion that this figure is understated. This was communicated to MFIN in a counter-reply dated 25 August 2014.



# Value Added Tax Department

## Eco-Contribution

### Background

The Eco-Contribution Act<sup>1</sup> (Chapter 473), brought into force on 1 September 2004, mainly provides for the imposition of an eco-contribution on products which result in waste. This contribution is charged and levied by the Value Added Tax (VAT) Department, at the rates established in the First Schedule of the Act. Products attracting eco-contribution include amongst others, containers made of plastic, glass or metal, plastic bags, white goods and electronics equipment.

The liability for the payment of eco-contribution lies with the producer, *i.e.* the person who manufactures or imports into Malta the items which attract the contribution payable. Eco-contribution becomes due at the time when the product is transferred from manufacturing stage, or is imported with the intention to be placed on the local market. This includes also those items for use in the trade or business of the person importing or manufacturing the product. The amount of contribution payable is reported in the Eco-Contribution Returns, submitted by the producers to VAT Department.

### ***Registration of Producers, Eco-Contribution Returns and Exemptions***

The Third Schedule of the Eco-Contribution Act requires every person to register with VAT

Department for eco-contribution purposes within 30 days from when the person becomes a producer in terms of the Act. Where the Department believes that a person placed on the market, products which attract eco-contribution, and has failed to register, the former will proceed to register the business itself. Once registered, the producer is required to report any eco-contribution due in the quarterly returns, which are submitted to VAT Department concurrently with the VAT Return. For each item, referred to by its Harmonised System (HS) Code, the producer is to include in the Eco-Contribution Return, the rate at which this tax is charged, the quantity of the products placed on the market, as well as the actual eco-contribution payable thereon.

Producers who participate in an approved waste recovery scheme, in accordance with Legal Notice (LN) 84 of 2010, may apply for an exemption from the payment of eco-contribution due on imported or produced items, as long as the packaging waste generated from these products will be recovered through such scheme. In these cases, during the exemption period, no eco-contribution will be paid by the producers on all the products on which the exemption was obtained, or part thereof. Nonetheless, producers are still required to duly fill in the Eco-Contribution Return and deduct the exempt amount from the total contribution due during that quarter.

<sup>1</sup> In its Budgetary measures for 2015, Government announced its commitment to reform the Eco-Contribution mechanism. The first phase will entail eliminating such tax from a number of electronic and white goods by September 2015.

### Penalties

An infringement of the provisions of the Eco-Contribution Act and other related regulations, as well as failure to comply with any request or decision given by VAT Department under the Act, may result in the imposition of administrative penalties up to a maximum of €11,645 for each infringement or failure to comply.

The VAT Department may waive administrative penalties if it is satisfied that there was adequate justification for the default. However, insufficiency of funds to pay eco-contribution, or reliance on other persons to meet the obligations relating to the contribution, do not constitute a reasonable excuse for such waiving of penalties.

### Investigations

If VAT Department believes that the producer is not compliant with the provisions of the Eco-Contribution Act, an investigation is initiated. In such cases, the taxpayer is required to make available all business records covering the years under investigation.

### Financial and Other Information

According to VAT Department's electronic data, in 2013, 881 producers paid eco-contributions in

aggregate amounting to €8,110,900. However, this does not tally with the Departmental Accounting System (DAS) records, whereby the end-of-year balance on the Eco-Contributions Account amounted to €7,966,364.

During the same year, 1,044 taxpayers submitted the Eco-Contributions Returns declaring a total of €15,221,780. Out of this amount, €8,077,303 were exempt from eco-tax as a result of the waste recovery scheme. Thus, only €7,144,477 was actually due from producers in eco-contribution during 2013. This compares well with the estimated budgeted figure of €7,000,000.

Furthermore, from the 7,464 Eco-Contribution Returns sent to producers during the year under review, only 6,343 (85%) were received by VAT Department by the end of the year.

The VAT Department records also indicate that the total arrears of revenue as at 31 December 2013 stood at €7,324,113, out of which €4,535,950 (*i.e.* almost 62%) were estimated as not collectible. During the year under review, newly accrued balances amounted to €1,369,947, while only €202,918 were collected from past arrears. *Table 1* refers.

**Table 1: Arrears of Revenue outstanding on 31 December 2013**

Details	Amount
	€
Gross arrears as at 31 December 2012	6,366,700 <sup>2</sup>
Past arrears collected	(202,918)
Downward revisions	(209,590)
Newly accrued arrears	1,369,947
Amounts written off during 2013	(26)
Estimated amount considered as not collectible	(4,535,950)
<b>Net collectible arrears as at 31 December 2013</b>	<b>2,788,163</b>

<sup>2</sup> Out of this amount, €4,048,664 was estimated as not collectible on 31 December 2012.

## Audit Scope and Methodology

The main scope of the audit was to evaluate the internal controls in place over the collection of eco-contributions due to Government, as well as to ensure that income received by VAT Department was duly recorded. The audit also assessed whether adequate procedures are in place for the collection of eco-contribution, which were still in arrears as at the end of December 2013.

Audit work performed mainly covered eco-contribution payments effected by a sample of producers, to ensure compliance with the relevant regulations, in particular the Eco-Contribution Act, 2004, together with any LNs issued thereafter. Reference was also made to the Policies and Procedures Manual compiled by VAT Department in April 2003, as well as other guidelines concerning the waiving of additional tax.

### *Eco-Contribution Payments*

The audit sample consisted of the nine payments effected by producers in 2013 which individually exceeded €200,000 in value, as well as a further six payments selected randomly. In total, 15 payments amounting to €2,718,734 were tested, *i.e.* almost 34% of the total amount collected during the year.

The Returns submitted by the producers in the sample were reviewed to confirm the mathematical accuracy of computations, and to ensure that the rates quoted by the producers were in agreement with those listed in the First Schedule of the Eco-Contribution Act.

### *New Registrants*

A random sample of 10 producers was selected out of the 150 new registrants for 2013. Testing included verifying whether the applicant registered on time, as well as ensuring that the correct penalty amounts were charged in respect of late registrations.

### *De-registrations*

During 2013, a total of 77 producers filed for de-registration from eco-contribution. Out of these,

25 cases were closed, while the remaining 52 were still pending as at year end. Testing was carried out on a random sample of five producers who were fully de-registered by December 2013. The respective files were obtained and reviewed, to ensure that VAT Department carried out all the necessary checks prior to actually de-registering these producers, and that no further investigation was necessary.

### *Waived Penalties*

According to records forwarded to the National Audit Office (NAO), there were 59 cases of waived penalties during the year under review, collectively amounting to €28,936. The audit sample, which was selected on materiality basis, consisted of seven cases, in which a total of €17,771 was waived, representing 61% of the population. Testing included reviewing the respective documentation to ensure that in all sampled cases, the waiving was duly approved. The reason provided by the producer in default was also examined, in order to establish whether the waiving of the penalty was justifiable.

### *Investigations*

During 2013, six investigations, relating to eco-contribution, were carried out by VAT Department. Five of these inspections were initiated following a de-registration filed by the respective producers. Two of these inspections started in 2012, while the remaining three were carried out in 2013. The other investigation was triggered by the Department, since the respective taxpayer had failed to submit Eco-Contribution Returns.

Documentation relating to all six investigations was reviewed by NAO, to ensure that the verification process effected by VAT Department was satisfactory. In the case of de-registered producers, it was further ascertained that the eco-contribution registration was not cancelled unless all pending balances were duly paid.

## Limitations on Scope of Audit

Producers are not required to submit any documentation in support of their Eco-Contribution Returns. Therefore, NAO had to place reliance on information as presented in the

same Returns, thus limiting the scope of audit to ensure the completeness and accuracy of amounts declared by producers.

## Key Issues

### *Minimal Action taken to recoup Outstanding Eco-Contribution*

As mentioned earlier on in this Report, newly accrued eco-contributions during 2013 amounted to €1,369,947, an increase of €375,035 over the previous year. However, in sharp contrast, past arrears collected, which totalled €202,918 in 2013 (*i.e.* only 15% of the amount newly accrued), remained in the same level as the reported figure for 2012.

Furthermore, according to information obtained during the audit, out of the 7,464 Eco-Contribution Quarterly Returns sent to producers, 1,121 (*i.e.* 15%) declarations failed to reach VAT Department by end 2013. To this effect, the latter confirmed that during the year under review, no statements to follow-up on such submission were sent to producers. Thus, it is highly unlikely that all producers were fully knowledgeable of the actual total amounts owing to the Department, in particular with respect to penalties incurred.

Moreover, except for eight producers in default, who were to appear for the first time in the eco-tax sitting held on 12 December 2013, no other legal proceedings against eco-contribution defaulters were initiated during the year under review.

The absence of regular chasing of outstanding amounts, as well as lacking timely information sent to defaulters of amounts due to Government, will also lead to exponential increase in arrears of revenue, augmenting the risk that such amounts are not collected.

### *Unreconciled Eco-Contribution Payments received*

Total eco-contributions paid by producers during 2013, as extracted from VAT Department's computerised system, amounted to €8,110,900. However, actual income received in this respect, as recorded in DAS, totalled €7,966,364, thus resulting in an adverse discrepancy of €144,536.

VAT Department officials stated that such a discrepancy could be due to the fact that, whilst receipts are recorded in the computerised system according to the process date, these are accounted for in DAS when they are actually deposited at the Central Bank of Malta. However, no reconciliation is being performed to ensure completeness of income, which may be indicative of lack of control over the actual revenue generated from eco-contribution payments. In the circumstances, completeness of revenue could not be ascertained.

## Control Issues

### *Lack of Verification on Eco-Contributions receivable by the VAT Department*

During the year under review, no periodic or random spot checks were carried out by VAT Department to verify the accuracy and completeness of amounts declared in the Eco-Contribution Returns submitted by producers, including the exemptions claimed. The only verifications performed were those necessary prior to de-registering producers from eco-contribution.

Unless random checks are carried out, whereby amounts declared by producers are verified against source documentation, cases of intentional or accidental underdeclaration will remain undetected, thus resulting in loss of revenue for Government. The lack of checks carried out on amounts claimed as exemptions could also have the same consequences.

### *Shortcomings in the Investigation Process*

#### Background

When producers cease to import or manufacture items which attract eco-contribution, they are required to file for de-registration with VAT Department. Prior to concluding such de-registration, VAT Department ensures that all outstanding contributions due by the producers are settled. Furthermore, the Department substantiates the producers' claims of ceased trading, against corroborative evidence obtained from the National Statistics Office (NSO). If inconsistencies are encountered during the de-registration process, these would trigger an investigation on the relative producers.

In fact, as indicated earlier on, during the year under review VAT Department carried out investigations on five producers who filed for de-registration, testing of which revealed the following shortcomings.

a. **Total Reliance of Accuracy placed on Third Parties**

NSO records relating to one of the producers who was investigated in 2013, and who filed for de-registration on 13 January of the same year, revealed that the latter imported a number of items attracting eco-contribution, but which were not declared in the Returns submitted. In a letter sent to the producer, a VAT official stated that, although the mentioned items were covered by an exemption certificate, these still should have been declared. However, instead of issuing a correction with the exact amount of tax due, VAT Department requested the producer to correct the Returns submitted.

Furthermore, in the same letter, the producer was requested to verify whether eco-contribution was due on three imports, which verification provided by same, was accepted by the Department and no further verification was carried out. This suggests that total reliance was placed by VAT Department on the producer's judgment and calculations in establishing the amount of eco-contribution due, thus defeating the scope of carrying out an investigation.

Moreover, an incorrect administrative penalty was charged by VAT Department, instead of the equivalent 10% of eco-contribution due, as per LN 395 of 2004, which led to an immaterial loss of revenue.

b. **Inaccurate Calculation of Amount due by Producer**

According to eco-contribution declarations submitted to VAT Department, another producer investigated by the former, imported 10,174 items and paid contributions thereon. This figure was different to that

shown in NSO records, which showed that imports by the producer under the same code totalled 11,973, thus resulting in an under declaration of 1,799 items.

Following an investigation, VAT Department issued a correction of eco-contribution due by the producer. However, this was based on 1,721 items rather than on 1,799. No documentation was traced to the producer's file, explaining the difference of 78 items not included in VAT Department's correction.

***Reason for waiving of Penalties not justifiable***

One of the seven producers falling within the audit sample incurred penalties, amounting to €1,485, for failing to submit the Eco-Contribution Return for January 2008. This penalty was eventually waived by the Department on the basis that the producer had filed for de-registration and the late return penalty was incurred on a 'Nil' Return. This goes against the Third Schedule to the Eco-Contribution Act, requiring all producers to submit to the competent authorities quarterly returns, without providing for exceptions in case of 'Nil' Returns.

***Untimely Recognition of Late Registration Penalties***

Testing carried out on the audit sample of 10 new registrants during 2013 revealed that in eight cases, producers failed to submit their application on time and therefore were liable to pay late registration penalties. However, in four of these cases, the amount payable did not feature in the respective accounts in VAT Department's database.

Department officials stated that the late registration penalty is automatically generated in the system only upon the submission of the first Eco-Contribution Return, whenever this is forwarded to VAT Department. This results in unrecognised income receivable by VAT Department at a given period, leading to understated arrears of revenue. Furthermore, if producers are not immediately aware of the full amounts due to VAT Department, the risk that such amounts are contested is increased.

## Recommendations

### Key Issues

#### Minimal Action taken to recoup Outstanding Eco-Contribution

The VAT Department is to increase its efforts in chasing defaulters and collect eco-contributions due to Government. Legal action is to be targeted at persistent defaulters, in particular those who have long outstanding balances, so as to minimise arrears of revenue. Ledger statements are also to be regularly sent to producers reminding them of their amounts due.

#### Unreconciled Eco-Contribution Payments received

Reconciliation between the eco-contributions received, deposits effected, and amounts accounted for in DAS, are to be carried out by VAT Department on a regular basis to ensure completeness. Any resulting discrepancies are to be dealt with in a timely manner and duly explained.

### Control Issues

#### Lack of Verification on Eco-Contributions receivable by VAT Department

As also stated in its Policies and Procedures Manual, VAT Department is expected to carry out “... *necessary checks to make sure that all producers charge and pay ECO Contribution*”. Periodic checks on high risk taxpayers could also deter producers from not complying with eco-contribution regulations, by submitting inaccurate declarations.

#### Shortcomings in the Investigation Process

The VAT Department is to ensure that thorough verifications are carried out during investigations, such as tallying Returns against other source

documentation issued by producers. The administrative penalties stipulated by law are also to be duly enforced.

More attention is to be placed by VAT Department when carrying out investigations, so as to avoid errors and collect the entire amount due.

#### Reason for waiving of Penalties not justifiable

Penalties are to be waived **only** in exceptional cases, and where the reason for default is truly justifiable and within the criteria established by law. Supporting documentation is also to be presented by the producer, where applicable.

#### Untimely Recognition of Late Registration Penalties

Penalties resulting from late registration are to be recorded as soon as the defaulter registers for eco-contribution, thus ensuring that all amounts due to Government are timely recognised.

## Management Comments

Management concurred with the majority of findings, but expressed reservation on the observation relating to the difference in revenue recorded in VAT Department’s computerised system *vis-à-vis* that recorded in DAS. In this respect, it was claimed that a technical solution needs to be pursued to explain this discrepancy.

The Department also stated that the shortcomings outlined in this Report may be attributable to constraints in human resources, in particular the reduction in number of VAT inspectors who were never replaced. To this effect, Management remarked that although every effort will be made to implement the recommendations put forward, such efforts will prove unsuccessful unless adequate resources are made available.





Ministry for Health



# Mater Dei Hospital

## Contractual & Professional Services

### Background

The total budget for financial year 2013, allocated to the Ministry for Health for Operational and Maintenance expenses, was €41,541,000. Of this amount, Mater Dei Hospital (MDH)'s budgetary allocation for Contractual Services and Professional Services totalled €18,702,000 (45%) and €635,000 (2%) respectively for the same period.

The actual expenditure incurred by the Hospital during the year stood at €22,126,791 for Contractual Services and €733,879 for Professional Services.

Funds allocated to MDH under Contractual and Professional Services were mainly utilised for hospital cleaning and catering, care-worker and security services, and car park management, amongst others.

### Audit Scope and Methodology

The primary scope of the audit was to ascertain the validity of expenses incurred. It was also checked whether procedures adopted for procurement of goods and services, as well as the management

of contract agreements, were adequate and in compliance with the Public Procurement S.L. 174.04, and any other relevant regulations, policies and procedures.

Based on information gathered, an outline systems overview was prepared, summarising areas of concern and other potential risks within the current system. A sample of 26 transactions, based mainly on materiality, but also taking into consideration the nature of the expense, were selected for testing. The sampled transactions, with a value of €2,433,848, amounted to 11% of total expenditure incurred by MDH during the period reviewed.

A report titled 'Direct Orders and Outsourcing at MDH' covering Clerical/Reception, Security, Car Park and Traffic Management Services, was published by the National Audit Office (NAO) in 2009. This Report commented on the implications of the service concession contract split and included weaknesses in contract management, which were subject to irregularities of a financial and compliance nature, whereby the contractor was the main beneficiary from the new arrangements. As part of this year's audit, the contract for its entire duration was reassessed. It was also verified whether the reported observations were addressed.

## Audit Disclaimer

In view of limitations encountered during the audit, testing was neither comprehensive nor exhaustive on internal statistical data provided by MDH, concerning total periodic amounts disbursed for the procurement of various items under review. This data was not tested and, where applicable, was quoted as given.

## Limitation on Scope of Audit

Documentation and information, relating to the proposals made by the concessionaire following the decision to reduce car park fees, and negotiations chaired by the Foundation for Medical Services (FMS) leading to the final terms and conditions, were not made available for review.

Correspondence and agreements between the relevant authorities and the concessionaire, concerning the inclusion of the remaining part of the parking site within Level -2, in exchange for the Area C parking site, were not available, except that covering the final decision.

Tender documents for the supply of printers, including bids submitted and Adjudication Reports in relation to one of the contracts, were not provided for testing.

## Key Issues

### *Budget Allocations Exceeded*

MDH's actual expenditure on Contractual Services, for the period under review, surpassed the original budget allocated by at least €3,424,791, representing an increase of over 18%. Meanwhile the planned budget for Professional Services was overrun by at least another €98,879, equivalent to an excess of over 15%.

### *Car Park and Traffic Management, and External Security Services*

#### Changes following the Original Contractual Agreement

Subsequent to instructions to reduce parking fees, FMS appointed an *ad hoc* Committee to initiate renegotiation of the contract with the same concessionaire and, following a detailed request, approval was granted by the General Contracts Committee to enter into a new contract with the concessionaire. Consent was given, in terms of Regulation 59 (d) of the Public Contracts Regulations.

On 21 February 2008, FMS and the concessionaire agreed to terminate the original contract and split it into two new and separate agreements, effective retrospectively from 1 January 2008. This decision was taken notwithstanding the advantageous possibility that FMS could have terminated the original contract, giving a 30 day notice with no contractual penalties being due, in line with Article 18.3 of the applicable contract.

Moreover, this decision was made even though the agreement for external security services at MDH was a public services contract, and thus subject to Public Contracts Regulations.

#### Significant Changes leading to considerable Loss of Revenue to Government

This split brought about various changes to the terms and conditions of the original contract, leading to financial implications on public funds as indicated in *Table 1*.

**Table 1 - Significant Changes to Contract**

	<b>Original Contract</b>	<b>New Contracts</b>	<b>Difference</b>
	<b>€/annum net of VAT<sup>1</sup></b>	<b>€/annum including VAT</b>	<b>€/annum including VAT</b>
Car Park Concession	326,112	-	(326,112)
External Security Service	-	(577,219)	(577,219)
Area C Parking management <sup>2</sup>	-	(74,214)	(74,214)
Disabled Parking management	-	(43,979)	(43,979)
<b>Total per annum</b>	<b>326,112</b>	<b>(695,412)</b>	<b>(1,021,524)</b>

The above implies that over the contracted 60-month period of execution, an amount of *circa* €4,681,985<sup>3</sup> has been forfeited by Government.

Moreover, this amount excludes car park equipment Maintenance Costs and other Operational Expenses, such as utilities, which are borne by MDH, as well as further potential revenue which could have been generated from the rental of advertising space. Both these matters are highlighted in more detail further down.

The changes to the terms and conditions can be summarised as follows:

- Parking rates were reduced for all durations with the exception of night-time rates. As stipulated in the original Contract, revenue collected from car park users would be retained by the concessionaire.
- The original €326,112 (VAT excl.) annual fee payable to Government for the car park concession was waived in favour of the concessionaire.
- An annual fee of €577,219 is now due by Government to the concessionaire for the provision of external security services.

- A fee of €74,214 *per annum* is payable by Government to the concessionaire for the management of an additional car park area (Area C). This area was not included in the original Contract, and was to be utilised by MDH staff. In return, revenue collected from this parking area, as detailed in the new agreement, was to be passed on to Government, until it was forfeited.
- A fee of €43,979 *per annum* is payable by Government to the concessionaire for the provision of a parking area for users with special needs. Again, this area was not included in the original contract, and was to be utilised by vehicles holding the relative permit issued by FMS/MDH, or a 'Disabled Blue Badge' provided by the Malta Transport Authority.
- A new clause allowed the concessionaire to utilise the parking areas within MDH for advertising, *albeit* this was to be in line with Hospital policy and guidelines. Any revenue received is now retained by the concessionaire with no income due to Government.

<sup>1</sup> Amount excludes VAT element, as it is assumed that this would have been reclaimed by the concessionaire as Input VAT.

<sup>2</sup> Amount excludes revenue generated from Area C, which was collected by the concessionaire and passed on to Government until February 2011, when free parking was granted to all Mater Dei Hospital staff.

<sup>3</sup> Applicable as annual cost for the period per new contracts January 2008 - July 2012 – €1,021,524 *per annum* x 55 months.

Moreover, with reference to the original contract, it was also agreed that the concession fee, payable by the concessionaire to FMS for the first five months up to 1 January 2008, *i.e.* before the start of the new agreements, would be waived as well. This fee, which should have been paid in November 2007, amounted to *circa* €135,880 (VAT excl.). However, the one-time payment of €30,282 (Lm13,000) payable by FMS to the concessionaire would still remain due.

Relevant calculations, correspondence or other documentation evidencing and substantiating the changes, made to attain the final endorsed terms and conditions summarised above, were not available.

### Revenue from Area C / Level -2 West parking

In July 2010, an alternative parking location in the car park, Level -2 West, was provided as a replacement for the Area C car park, previously utilised by MDH staff in possession of a yellow parking permit. This was provided at reduced rates. In February 2011, the then Ministry for Health, the Elderly and Community Care acceded to the Union's request, to provide this parking area for free to MDH staff in possession of the necessary permit.

As a result, revenue previously collected from employees using this parking, which was passed on to the Consolidated Fund, was now waived to the detriment of Government. This also meant that no revenue was even considered to be recouped by the latter from these two new contracts.

### Other Car Park Costs burdened on Government

Detailed review of the car park and traffic management contract terms and conditions, as well other related documentation, further showed that all the equipment that was to be utilised for the management of the car park, including barriers, cash machines, and control room, was procured and owned by Government rather than the concessionaire. As indicated earlier on, relevant maintenance on this equipment is also paid from public funds.

Furthermore, no reference was made to other major operational costs, such as utilities, in the contract. In fact, these are also being paid for from public funds and are not reimbursed by the concessionaire. To this effect, MDH Finance confirmed that they have never issued any invoices for utilities to the concessionaire.

The above circumstances again show that all major expenses, including both capital start-up costs as well as day to day running expenses, were and are still being burdened on Government and ultimately borne from public funds, compared to the fact that during 2013, the concessionaire had a turnover in excess of €1,000,000 from the car park.

### Delays on Way Forward – Car Park and Traffic Management Contract

The contract relating to car park and traffic management, as well as the one covering the external security services, expired on 31 July 2012.

From internal correspondence, it transpired that as early as March 2011, MDH were already taking the initiative to start working on a new tender for the car park and traffic management.

Analysis of documentation provided during the audit revealed that MDH had initially issued a new call for tenders for the car park and traffic management in August 2012. A new maintenance agreement with the supplier of the car park equipment was also negotiated during the same period. It also transpired that MDH cancelled this tender beginning November 2012, following a decision to manage the parking in house, as highlighted further down.

However, MDH confirmed that in fact, a decision was eventually taken in January 2014, where following discussions, “... *it was decided to proceed as per original plans, i.e. to issue a concession tender for such services ...*”. This new call for tenders was planned to be issued by end of February 2014. Notwithstanding, it later transpired that the tender, although published,

had been “...retrieved following direction that the structure and operational requirements of the tender are being revised ...”, subsequent to instructions issued by the Permanent Secretary’s Office of the Ministry for Health.

Thus, given that the initial preparations for this tender were undertaken in March 2011, conclusive action on a way forward was not yet taken more than three years later.

### Delays on Way Forward – External Security Services Contract

The first correspondence indicating action on the external security contract was dated 1 August 2012, *i.e.* one day after its expiry, and shows that MDH was planning to integrate this service with the internal security services and merge into one contract.

However, financial approval from MFIN to publish this new call for tenders was only obtained in the beginning of 2014, and the tender itself was planned to be issued by the end of March 2014.

In spite of this, it transpired that in view of Government’s efforts to eliminate precarious job situations, in May 2014, discussions were still underway, covering employees’ conditions as well as the salary pegging equivalent to similar positions in the public service. According to MDH, this “... resulted in further delays to have this tender published”.

### Repeated Extensions not covered by the Original Contracts

An extension clause was not specified in the terms and conditions of either contract. However, MDH repeatedly sought approval from the then Ministry of Finance, the Economy and Investment (MFEI) or Department of Contracts (DC) as applicable, to extend both the car park and traffic management agreement, as well as the one relating to the provision of external security services, following their expiry, covering a total of two years each, up to July 2014.

In total four requests were made to extend the car park and traffic management contract, whilst another three requests covered extensions for the external security services contract.

### Retrospective Approvals to extend Contracts

All requests to extend the contracts in question were approved retrospectively. Most notable were the latest approvals for each of the two contracts, both covering 1 August 2013 to 31 July 2014, which were granted by DC more than 23 and 19 weeks respectively in retrospect.

Moreover, three of the requests for extension were also submitted late to the respective authority; two were made over 12 weeks after the previous approval expired, whilst the other one was made more than seven weeks later.

### Security Guard Service Level Requirement – Hours paid but not utilised

According to the Technical Requirements annexed to the Contract for the provision of external security services at MDH, the contractor was to provide a security team with “... a minimum level of 23 personnel ...” (plus one supervisor), providing “... full cover ... on a 24-hour, 7-day week basis”. This is equivalent to a minimum of 184 hours daily, based on eight-hour shifts as detailed in the contract. Calculated on the annual fee of €577,219, this would work out at an hourly rate of €8.62. The contract also gave FMS/MDH the right to reallocate any of the security staff to areas other than those stipulated in the Contract.

### Scheduled Hours

Enquires carried out during testing revealed that the daily scheduled number of external security guards on site, as per MDH, amounted to eight officers, plus one supervisor. Based on the 12-hour shifts that was currently in place, this translated into a total of 96 hours per day. This is nearly half the minimum number required as per contract, notwithstanding that the full annual fee due was being paid to the contractor by MDH. This resulted in an hourly rate of €16.47 being charged.

Moreover, the latter did not even exercise its right to allocate the unused personnel hours to other sites.

Thus, to this effect, MDH were paying an annual amount of €276,061<sup>4</sup> with no return whatsoever.

#### *Rosters and Timesheet Records*

It was observed that duty hours for security guards were pre-printed on the sampled manual timesheets, rather than the employees themselves manually record the actual hours on duty. Additionally, the timesheets were not endorsed by MDH representatives, approving the duties carried out.

Further to the above, when examining these timesheets and security guard rosters provided by the contractor, for the sampled four-week period from 2 December to 29 December 2013, the average hours worked per day were found to be overstated, when compared to the daily scheduled hours provided by MDH as indicated earlier on.

A palm reading system was eventually introduced as from December 2013 for use by the security guards.

#### *Digital Patrol System Out of Order*

The Technical Requirements also stipulated that the contractor shall operate a system of patrolling, using designated clocking points, varied and planned over a 24-hour period. Such patrols are to be timed and supplemented by a Digital Patrol System.

However, MDH confirmed that the electronic punch gun system that had been in use since the signing of the original contract, was out of order from January 2013 up to early December 2013. A new system that had been commissioned by MDH, and financed by the concessionaire, was operational as from 8 December 2013.

In the interim, a manual procedure was in place to log records of patrols performed by security guards on duty. However, MDH admitted that this was “... *not reliable* ...”.

## **Control Issues**

### *Cleaning Services*

#### *Lack of Details in the Contractual Agreement*

##### *Hours and Contract Value not specified*

- a. The agreement entered into between the contractor and DC does not clearly specify the total or maximum cleaning hours to be provided by the contractor delivering the service, nor make any reference to the total contract value (cost), whether *per annum* or for the whole duration. This was also not clarified in the contract extension, as such information was omitted again.
- b. The only indication of the hours to be rendered was an estimate given in the contractor’s financial offer, endorsed as part of the contract. In this financial offer, the contractor stated that “*Our estimates indicate that the Hospital will require an annual cleaning capacity in the region of 611,000 man hours, of which 527,000 man hours would be operated by us (we are assuming in our calculations that the remaining hours would be worked by existing employees employed at Mater Dei)*”. The latter figure was used by the contractor, together with the total annual cost, as a basis for calculating the quoted rate of €8.99 per hour.
- c. Meanwhile, the contract only details the hospital floor area and the number of rooms and corridors that have to be cleaned.

<sup>4</sup> Annual Fee for security hours not rendered - €577,219 *per annum* ÷ 184 hours/day x (184 hours/day – 96 hours/day).

- d. Documentation dated 28 February 2007 indicated that the approved estimated cost as per original tender was €2,795,248 (Lm1,200,000) *per annum*, well below the actual costs which exceeded €5,100,000 annually between 2009 and 2013. In fact, invoices in respect of 2013 amounted to €5,874,364. The total amount invoiced by the contractor on this contract amounted to €29,540,753, as at audit date, *i.e.* 28 May 2014, covering period from commencement in November 2008 to end March 2014.

#### *Limited Details on Government Employed Cleaners*

- a. The endorsed description of the contract specifies that, at the time, there were approximately 80 Government employed cleaners who “... *may be assigned cleaning duties in designated parts of the hospital ...*”. However, an indication of the actual number of cleaning hours that these would be providing was not given.
- b. On the other hand, the contractor’s financial offer presumes that the difference of 84,000 man-hours *per annum*, identified above, would be performed by existing MDH cleaners. As already stated, these hours were not factored in the contractor’s basis of the quoted rate.

According to information provided by the Manager Hospitality at MDH, there were 43 Government cleaners on commencement of the contract on 1 November 2008. However, this number had been reduced to 15 as at February 2014, mainly due to retirements and transfers. This implies that these cleaners only provide an aggregate of *circa* 28,320<sup>5</sup> man hours *per annum*.

#### *Potential Savings not achieved*

The financial offer submitted indicated that potential efficiencies envisaged during this period could result in “... *the total annual cleaning capacity required gradually reduced by circa 43,000 (7%) by the fifth year of the contract ...*”.

To this effect, it was calculated that from the original 611,000 hours estimated to be required in year one, a total of 568,000 cleaning hours were being predicted for year five of the contract.

#### *Adverse Man-Hours Variance*

As indicated earlier, actual cleaning hours carried out by Government employees could not be established. However, utilising 28,320 cleaning hours that can be provided by Government employees would leave *circa* 539,680 cleaning hours to be provided by the contractor for year five of the contract.

This contrasts sharply with the actual cleaning hours invoiced by the latter, which amounted to 584,921 for 2013, resulting in an increase of *circa* 45,241 cleaning hours billed by the contractor for the period. Thus, using the hourly rate of €9.80 applied during 2013, implies an additional cost of around €443,361 for MDH in one year.

When clarifications were sought on this matter, the Manager Hospitality claimed that MDH occupancy levels remained high and that “*Additional areas and requests to increase cleaning, have occurred along the years, thus changing the amount of required total hours, as these were not included in the proposed amount in the contract*”.

#### *Controls over Attendance Records*

##### *Biometric Electronic Attendance System not in place*

The extension of the contract for cleaning services, endorsed by both parties in November 2013, binds the contractor’s employees to record their daily attendance by biometric electronic means, fully accessible by MDH, in addition to the existing (manual timesheet) attendance record system.

However, enquiries carried out by this Office during the audit in February 2014 revealed that such a system was not yet introduced by the contractor. It was stated that the palm reading system was operational as from beginning May 2014.

<sup>5</sup> Annual Man Hours provided by Government Cleaners (as at February 2014): [(40 hours x 52 weeks) - (8 hours x 24 days)] x 15 cleaners.

### Verification of Timesheets not frequent

During audit fieldwork it was confirmed that the majority of manual timesheets for cleaning services are not checked for correctness at least on a weekly basis, with the exceptions being those for Medical Imaging, Out Patients, corridors/common areas and scrubbers. It was stated that for the majority of the remaining areas, on average, one week is checked out of every three or four weeks. However, instances were encountered when there were intervals of five or even six weeks in between checks being carried out.

### Shortcomings in Timesheets

Testing of timesheets, for a sample of 12 wards covering two months, analysed in comparison with actual hours invoiced by the contractor, revealed the following frequent shortcomings.

- a. The most prevailing matter concerned the break-time not being recorded on timesheets, which led to instances where one cannot quantify the actual hours worked by the respective cleaners. This was observed in eight of the 12 wards/sections examined.
- b. Other areas of concern related to the lack of endorsements by Duty Officers on timesheets, pertaining to five wards. In contrast, such endorsements were included for blank records, observed in two other wards.

### Photocopier and Printing Services

#### Contract Value exceeded

As per information submitted by the Finance Department, amounts paid on this contract on a year-by-year basis were approximately €20,000, €35,000 and €25,000, for 2011, 2012 and 2013 respectively, *i.e.* a total of *circa* €80,000 over the duration of the contract. This implies that the pre-established maximum limit of €47,000 (VAT excl.) stipulated in the agreement signed with the contractor was substantially exceeded by the end of the 36-month period.

Moreover, MDH continued to use such agreement and, following the contract's expiry in September 2013, it even exercised the option to extend it by a further six months up to March 2014.

### Limited Control over Quantities invoiced by Supplier

The supplier was providing an invoice covering the use of various photocopiers, together with a detailed spreadsheet listing each machine and related cost. However, relevant information for each copier, such as, the starting and closing print count and resulting copies made (meter readings), the relevant period, and endorsement/certification by MDH user, were not provided. Thus, proper checking could not be performed to ensure accuracy of the amounts being charged.

### Spreadsheets and Invoices not tallying

In all three cases in the audit sample, the total value as per detailed supplier spreadsheets did not tally with the value of the supplier invoices. Notwithstanding, two of these invoices were certified correct and paid accordingly. The third invoice was not certified correct but was settled nonetheless. This implies that proper verification was not being carried out.

Following enquiries made by this Office, all three spreadsheets were eventually updated and amended to reflect the invoiced amounts.

### Complimentary Hotel Accommodation and Travelling Expenses

#### Lack of Documented Policies or Guidelines

- a. MDH does not have an official documented policy or guidelines to regularise the complimentary benefits offered to foreign consultants, engaged both on temporary and long-term basis.
- b. Specifically, in the case of reimbursement of travelling (flight) expenses to visit family members abroad when on long-term engagement, one cannot determine completely whether flight expenses for the



immediate family are reimbursed, whether there is a capping on the number of flights, or whether reimbursements are only made against the cheapest of a number of quotes, amongst others.

- c. Likewise, where complimentary accommodation services are provided, it cannot be clearly ascertained who is entitled, what type of accommodation is offered, and under what circumstances.
- d. By way of example, in one instance encountered during audit testing, the reimbursement of tourist class airfare, including return flight to Samara (Russia) for a specialist engaged on long-term basis, his wife and two children during 2013, amounted to €6,842. It was also confirmed that quotes are not requested by MDH, and thus it could not be ascertained that the cheapest tickets were selected by the consultant in question.

#### Procurement of Accommodation by Direct Request for Quotations

Notwithstanding the amount of €19,651, representing annual invoices incurred by MDH for 2012, testing revealed that the selection of hotel accommodation for this year was based on two separate direct requests for quotations to a number of hotels, rather than being based on one single departmental call for tenders or a call for quotations, published in the Government Gazette.

#### Neurosurgeon Services

#### Insufficient Verification before endorsing Invoices for Payment

This Office is concerned about the strength of internal controls, specifically with regards to invoices endorsed by the Department of Neuroscience. The following relate:

- a. Invoices for duties performed by a Consultant were paid as long as they were rubber stamped and signed by the Clinical Chairman at the Department of

Neuroscience. Moreover, it transpired that the Finance Department does not have any further evidence, such as job sheets or attendance/time records, to back up and support the hours worked as per invoices.

- b. Testing also revealed that a bill for services rendered by this Consultant during September 2012, was signed and rubber stamped, notwithstanding that this consultant had been hospitalised at MDH during half of this period, rendering him unable to provide such services. However, it transpired that the overcharging of €3,750<sup>6</sup> had been noted by the Director Human Resources beginning June 2013 and the payment was cancelled in time.
- c. MDH erroneously also paid for five nights hotel accommodation, covering the period during which the consultant was hospitalised at MDH. The Finance Department acknowledged this error when brought to its attention during the audit, and stated that the respective amount will be deducted from the balance due to this Consultant.

#### Obstetrics and Gynaecology Specialist

#### No Contract of Service

- a. Notwithstanding the engagement of an Obstetrics and Gynaecology Specialist with MDH since August 2011, the former was not issued with a contract of service and MDH confirmed that an agreement was never signed. Only a letter minute declaring his appointment was traced in the respective file.
- b. Testing also revealed that travelling expenses to the country of residence for the specialist and/or his family were reimbursed by MDH. These amounted to €3,003, €5,025 and €6,842, for 2011, 2012 and 2013 respectively. However, the appointment letter only specifies that complimentary passage to Malta and back to the country of residence would be provided to the specialist and his family upon engagement and termination of service.

<sup>6</sup> Consultant had been hospitalised for five days, which at the contracted rate of €750 per day would cost €3,750.

*Neurophysiology Technologist Services***Over-dependency on Sole Service Provider**

The Ministry for Health has continued to obtain the Neurophysiology Technologist services from the same individual for the past 21 years, *i.e.* since 1992, in spite of attempts made to recruit or engage an alternate service provider. This high dependency on one service provider is very risky.

**Job Sheets or Attendance/Time Records not held**

The Finance Department does not have access to documentation in support of the related work, such as job sheets or attendance/time records. MDH maintained that since this individual is the only person providing this service, work performed is evident and reflected in records of electromyographic studies performed at the Neurosurgery Department.

*Renewals of Bank Guarantees and Insurance Policies*

In a number of instances, Bank Guarantees and Insurance Policies were not renewed as follows:

- Performance bond related to the Car Park and Traffic Management was expired.
- Performance bond in respect of Cleaning Services was less than 5% of the contract value, instead of the 10% specified in such agreement. Copies of extensions were not made available.
- Bank guarantee related to the Photocopier Service was also found to be expired.
- Though the Contractual Agreement binded the Neurosurgeon to take out and maintain adequate insurance cover against liability, in two years, MDH never asked for a copy of such evidence.

**Recommendations****Key Issues****Budget Allocations Exceeded**

As far as possible, MDH is expected to limit its spending to the budgetary allocation provided by the relevant authorities, whilst ensuring that expenditure is adequately monitored and controlled.

**Car Park and Traffic Management, and External Security Services**

Management is to ensure that major projects are only undertaken following comprehensive planning and necessary research. Actions taken and commitments made are to be in line with relevant rules and regulations; thus approvals are to be invariably sought and obtained, prior to committing to the procurement of services.

When entering into such agreements with private contractors, Government's interests are to be duly safeguarded with the intent to maximise potential revenue to Government while minimising costs.

MDH is to prioritise long-term planning and ensure that action is taken prior to the expiry of existing agreements.

Agreements are not to be extended unless this is specifically provided for in the original tender to ensure rigorous compliance with applicable regulations.

Management is expected to exercise its right and utilise any idle security personnel by allocating them elsewhere at MDH as required, thus ascertaining hours being paid for are duly utilised. Referring to the new call for tenders, Management is also encouraged to negotiate and contract these services on an hourly basis, indicating the maximum hours required by MDH. It is also expected to properly monitor and certify the actual hours worked by the guards, prior to approving any payments to the contractor.

It is to be ensured that the electronic punch gun system is in operation at all times, and that services procured are up to the levels and specifications contracted, such that adequate monitoring and controls are in force.

### **Control Issues**

#### **Cleaning Services**

All agreements are to be clearly drawn up, providing relevant details and specifications, including any capping on the service or total cost, as may be applicable. This will assist it to contain costs in comparison to its original plans.

Management is expected to have sufficient information on the potential output that can be performed by its cleaners, in order to request only the required number of cleaning hours to be carried out by the service provider.

The service being provided is to be analysed to identify the possibility of potential reductions, on a year-by-year basis, as envisaged by the contractor's financial offer. The quality level of the cleaning service provided by the contractor is also to be assessed and monitored through MDH periodic reviews.

Management is to ensure that the biometric electronic attendance system is invariably used, as envisaged by the contract, so that adequate controls are in place to monitor the service provided by the contractor's cleaners. The respective records are to be used for billing purposes.

#### **Photocopier and Printing Services**

All relevant tender files and documentation, as well as any other pertinent information, are to be securely filed for future reference, and to ensure a complete audit trail is maintained.

Appropriate monitoring and control of available funds is essential, to ensure that spending remains in line with budget plans. Moreover, Public Procurement Regulations are to be followed and applied rigorously.

Management is encouraged to install the necessary software which would enable it to implement suitable controls over costs for photocopies and printing services.

The meter readings for each machine, along with the rate charged and the relevant period, are to be specified by the supplier and endorsed by the officer-in-charge accompanying the former when taking the reading. This will enable MDH to properly verify and reconcile the invoices prior to issuing the respective payment.

#### **Complimentary Hotel Accommodation and Travelling Expenses**

Formal documented policies and guidelines are to be drawn up in line with any legal or regulatory requirements, to cover engagements of foreign consultants and referred to in respective contracts. Moreover, reimbursement of airfare tickets is to be made against a request for quotes and included in the respective contracts. A *proviso* that the cheapest option is to be selected, is also recommended.

Management is to encourage better co-ordination and planning between the Finance Unit and other sections procuring the required service.

#### **Neurosurgeon Services**

Evidence, in the form of documentation backing up the invoice, is to be provided, so as to authenticate work performed by consultants. Invoices are to be properly verified with supporting documentation before approved for payment. Better communication between the Departments concerned is expected to ensure that Government does not bear unnecessary costs from taxpayers' money.

#### **Obstetrics and Gynaecology Specialist**

Recruitment of foreign Consultants/Specialists are to be invariably covered by a formal agreement, clearly specifying the terms and conditions of the engagement. Amongst others, these are to comprise job specifications, remuneration

rates, any complimentary benefits including the reimbursement of travelling expenses and the provision for adequate insurance cover.

### Neurophysiology Technologist Services

In addition to continuing with efforts to seek an alternate service provider, MDH is expected to exercise its right and plan to recruit prospective candidates, and give them the necessary training by the current service provider, as provided for in the present agreement with the latter.

Furthermore, invoices are to be invariably supported by evidence of work done. These are to be properly verified and certified correct, prior to making any payments.

### Renewals of Bank Guarantees and Insurance Policies

Adequate Bank Guarantees and Insurance Policies are to be in place, in line with the contractual requirements, and invariably cover MDH and the contractor throughout the whole duration of the contract.

## Management Comments

### Budgetary Allocations exceeded

Management claimed that the annual budget allocated to MDH is not sufficient to cover the expenditure during the year. MDH is doing its utmost to curtail expenditure on contractual services whereby Heads of Department and Contract Managers will be rationalising the services requested whilst guaranteeing that quality of service is not reduced.

### Car Park and Traffic Management, and External Security Services

It was stated that MDH Management had no jurisdiction to change any terms and conditions of the contract. However, significant changes to new contract have been suggested. Lack of direction between stakeholders delayed the process to get extension approval and though the contracts have

been prepared since 2011, the Tender documents are currently awaiting direction from higher authority.

Management claimed that, as from 1 March 2014, it managed to negotiate a *pro rata* decrease in the lump sum payable for the security services provided, and also obtained a monthly reduction of €8,300. Furthermore, the forthcoming external security contract will be issued on a 'pay per hour' basis, rather than lump sum, thus ensuring that MDH pays only for the hours that are actually performed.

### Cleaning Services

When the Tender was issued, MDH was not in a position to clearly know the exact number of hours required as this was subject to change according to the needs when the amount of allocated areas to the contractor was not yet established. The number of Hospital cleaners, totalling 80, was only given as an estimate. These cleaners were eventually allocated to areas that were not covered by the contract. Management has identified a suitable person that will be conducting regular audits on its behalf to ensure that the level of cleanliness is maintained.

With regards to timesheets, breaks are deducted even if they are not always marked. Endorsements by duty officers are being enforced and checked by supervisors on a weekly basis. MDH Finance will ensure that, where applicable, VAT receipts are collected following payments.

### Photocopier and Printing Services

MDH stated that retrospective approvals for the amounts exceeding the limit covered by the contract were later requested and granted. A new contract has been awarded and proper controls are now in place, with invoices certified correct through IM&T Department. Management has also installed the necessary software to implement suitable controls over the use of these services. The supplier is required to send breakdowns indicating the initial and final readings, and which are to be endorsed by the end users.

### Complimentary Hotel Accommodation and Travelling Expenses

Two calls for quotations were issued for hotel accommodation as there was an abnormal increase in demand following the engagement of a number of foreign consultants. Eventually this service was covered by a departmental tender as from December 2012. MDH Finance are requesting an insurance policy from Consultants prior to payment and the respective head is to endorse timesheets and related invoices.

### Neurosurgeon Services

MDH Finance is requesting timesheets verifying the attendance to cover the amount of hours charged, which are to be endorsed by the respective head.

### Renewals of Bank Guarantees and Insurance Policies

MDH Finance will ensure that all Bank Guarantees and Insurance Policies are in place and extended as required on an annual basis and that no payments are made unless they comply accordingly.

# Rehabilitation Hospital Karin Grech

## Personal Emoluments

### Background

When Mater Dei Hospital was opened in November 2007, some wards in the former Karin Grech Hospital were refurbished, in order to accommodate elderly patients. Two sites, namely the latter and Zammit Clapp Hospital (ZCH), were being used concurrently for the same purpose; that of rehabilitating elderly patients.

Subsequently, the Rehabilitation Hospital Karin Grech (RHKG) was earmarked to cater for needs of patients with various pathologies, both on an in-patient and out-patient basis, and from the age of 16 upwards, thus offering a wider service in this respect. In 2010, ZCH closed its doors and all its services were migrated to RHKG. Currently, the latter operates under the administration of a Working Hospital Committee and provides rehabilitation services to approximately 269 patients.

The unaudited accounts for the year ending 31 December 2013, show a total revenue of €15,058,823, 74% of which was derived from funds directly allocated by the Government, which amounted to €11,099,099. The main source of the remaining balance was reimbursement of salaries recharged to other Government entities, likewise allocated by Government in the annual budgetary Estimates. A total of €7,879,441 was used for Personal Emoluments.

### Audit Scope and Methodology

The main scope of the audit was to verify that, during financial year 2013, salaries paid to various employees, as well as overtime and allowances payments, were correct. The upkeep of attendance records was also assessed. Other objectives were to determine the level of internal controls, as well as to verify that applicable regulations and agreements were followed.

Audit procedures were planned and performed, in order to obtain reasonable assurance as to whether the internal control structure at the Hospital is adequate. Walk-through tests and detailed substantive testing were carried out to confirm the existence and the correct application of controls. Furthermore, various meetings were held with RHKG's Management and the Personnel Officer, in order to obtain an understanding of the relevant policies and procedures adopted.

The sample selected for audit purposes comprised 10 officers with different designations, whereby emoluments and allowances paid to them throughout 2013 were verified.

## Key Issues

### *Weak or Lack of Internal Controls*

Throughout the audit testing, it was evident that a number of internal control measures were habitually not being observed, showing clearly that effective monitoring by Management, to ensure that personal emoluments paid are correct, is lacking. Consequently, ineligible or incorrect amounts were paid to the respective officials. Internal control failures identified during testing are outlined separately further down in the Report, under the pertinent observations.

### *Statutory Bonuses not paid pro rata*

During testing, it was noted that 12 employees working on a reduced timetable were still receiving the full statutory bonuses. It also transpired that, as from employment dates, ranging between year 1991 and 2013, such bonuses were never paid *pro rata*, resulting in a total overpayment of €17,041. Following audit enquiries, RHKG alleged that, upon recruitment, six of these employees were promised the full bonuses even though working on reduced hours. Supporting documentation to substantiate this statement was not available.

### *Lack of Segregation of Duties*

During the audit, it was observed that the Personnel Officer is responsible for most of the payroll functions and is a 'key person'. Due to the lack of segregation of duties, effective internal controls are very limited.

## Control Issues

### *Overtime*

#### *Prior Requests to perform Overtime not made*

Six out of the 10 employees selected for testing, namely a Senior Principal Pharmacist, an Assistant Accounts Officer, a Nursing Aide, a Driver and/or Security, and two Staff Nurses, were paid overtime during the year under review, in aggregate amounting to €12,564. Thus, a number of related payrolls were selected for the verification of respective payments, comprising 242 instances.

Whilst the two Staff Nurses were sometimes being asked to perform overtime by means of written requests, it was not the same practice for the other highlighted Officers. RHKG confirmed that, apart from Nurses and Care Workers, Heads of Department verbally ask employees to perform overtime. Moreover, Management requests for approval of overtime to the Permanent Secretary, as required by the Public Service Management Code (PSMC) Section 3.2.1.2, were not even considered.

### *Irregular Payments paid to Principal Pharmacist for Ineligible Overtime approved by himself*

#### *a. Overtime paid to Ineligible Employee*

A Principal Pharmacist, in Salary Scale 6, was promoted to Senior Principal Pharmacist with effect from 30 May 2013, which grade is entitled for a Salary Scale 5 as per Schedule of Grades for 2013.

As specified in the Collective Agreement Section 2.5, pertaining to the Pharmacists employed within the Public Service, all employees are to abide by PSMC. However, although Section 3.2.1.3 of the regulations states that officers above Salary Scale 7 are not entitled to overtime pay, the incumbent received €754 in overtime payments during 2013, covering pay periods 1 to 9.

#### *b. Overtime not exceeding half an hour*

It was also noted that in 20 instances, the same Officer requested and subsequently got paid for overtime ranging from 12 to 30 minutes, notwithstanding that PSMC Section 3.2.2.1(b) stipulates that, "*Overtime attendances not exceeding half an hour are on no account to be paid for*".

#### *c. Approving his own Overtime and Leave*

In all 10 applications, covering 57 instances for a total of 57.17 hours, the signature approval and that of the applicant are the same. Therefore, it is evident that payment of overtime was approved by his good self. This employee was also authorising his own leave, since in the eight application forms

pertaining to 2013, covering 21 instances for a total of 135.75 hours, both signatures were identical.

In addition, an application form for payment of extra hours was endorsed by the incumbent on 5 March 2013, for overtime performed between 6 March and 22 March. Thus, certification of correctness for payment was irregularly carried out prior to performing such overtime.

## Allowances

### Clause in Agreement with respect to Meal Allowance open to subjective interpretation

Clause 5 of the Agreement entered into on 10 December 2012, between the Health Services Section of the *Union Haddiema Magħqudin (UHM)* and RHKG, on behalf of the Ministry for Health, the Elderly and Community Care states that “*All employees deployed at RHKG shall receive a daily meal allowance of €2.10*”.

- a. The above-mentioned Agreement does not include a deductions clause, or at least mention, when the employer can deduct from the employee’s allowance, for example, a provision stating that if the employee is on a day’s leave or part thereof, the respective deductions are to be carried out.

Furthermore, it is not clear if shift workers are entitled to such allowance when they perform overtime on their off-duty, or when non-shift officers perform overtime on weekends.

- b. Following a re-computation of the meal allowance paid for the year under review, to the 10 employees in sample, this Office observed that the meal allowance is not paid when:

- officers avail themselves of hours of leave, even when the employee working on a 12-hour shift avail himself of just three hours leave after break time; and

- officers attend for work to perform overtime.

On the other hand, it was noted that when officers change a day duty (12-hour shift) to two half-day shifts on their off-duty, the allowance is paid for both instances.

### Payment of Weekend Allowance

During 2013, a Radiographer received a weekend allowance amounting to €3,536. Letter correspondence dated 20 March 2005 revealed that the then Hospital Management Committee decided that, instead of an hourly basis remuneration, the services rendered by this Officer during the weekend are to be paid as a fixed sum of €66 per weekend. This was calculated as ‘Annual Salary/281 plus €4.19’.

Whilst scrutinising the source document provided by RHKG, the following was noted:

- a. It is not clear whether the rate of allowance increases annually, since the rate granted was based on the annual salary at the time, presuming that paid for the year 2005.

It also transpired that the aggregate amount of €3,536, *i.e.* an average of €68 per week, paid during 2013, was not in accordance with the weekly rate of €66 as mentioned in the letter.

- b. It is also not clear whether such allowance is to be paid for every weekend, even if the Officer’s services are not requested by the Hospital, and if he is to attend, what are the expected minimum hours, if any, of attendance.

During the year under review, the Officer attended for only 76.75 hours at work on a Saturday and/or Sunday, *i.e.* an average of 1.47<sup>1</sup> hours per weekend. Moreover, on the weekend dated 22-23 December 2012, according to the attendance records, the Officer attended at the place of work for only one minute.

<sup>1</sup> Average is equal to 76.75 hours divided by 52 weekends.



Furthermore, since the payment of a weekend allowance is neither covered by PSMC nor by the Sectoral Agreements, the National Audit Office (NAO) requested RHKG to provide the relevant authorisation from the Public Administration HR Office (PAHRO) and the Ministry for Finance (MFIN), as required by PSMC Section 2.4.1.3. However, such approval was not provided.

### Justification of Allowances not provided

#### a. Supervision Allowance

An Assistant Principal Occupational Therapist received a supervision allowance of €1,541 during the year under review<sup>2</sup>. Correspondence provided by RHKG indicates that this allowance was granted on 19 February 1993<sup>3</sup> by the then Hospital Manager at ZCH, following a request for compensation by the Officer for running the Occupational Therapy Clinic. Initially, such allowance was approved for €70 per month. On 1 June 1993, by means of a handwritten memo, the same Hospital Manager informed the Officer that the allowance was increased to €165 monthly, adding that this allowance could be stopped or revised by the Hospital according to revisions in the salary of the employee in question.

During the year under review, instead of the monthly allowance of €165, this Officer was paid €128 per month. However, no documentation substantiating this amount was forwarded to this Office, to evidence this revision. Furthermore, since the approval was given by the then Manager way-back in 1993, and the payment of this allowance neither emanates from PSMC nor from the Public Service Reform Agreements, it cannot be ascertained whether the incumbent is still entitled to such payment.

#### b. On-Call Allowance

On 25 November 1992, a Senior Nursing Manager requested the then Hospital Manager, for payment of an on-call

allowance for that particular year. It was noted that during 2013 this Officer received such allowance, amounting to €395. However, proof of Management's specific request for this Senior Nursing Manager to be on-call was not provided. Furthermore, although requested by NAO, the auditee failed to provide the calculations of this allowance, which has been paid for over 20 years.

### Incorrect Allowance paid to Social Workers resulting in Overpayments

As per Clause 1 of the Memorandum of Understanding covering the Social Work Class, dated February 2008, a non-pensionable allowance of €1,000 *per annum*, effective from 1 June 2007, was to be awarded to officers in the respective grades falling under the Social Class and who have a warrant to practice as Social Workers.

However, it was noted that, at least in 2013, instead of €1,000 *per annum*, 10 Social Workers engaged with RHKG received the amount of €1,864, or *pro rata* thereof if working on a reduced time-table. Subsequent to queries raised by this Office, it transpired that the latter amount was incorrectly derived from Annex A to the Memorandum of Understanding between Government and UHM, covering Paramedics, Health Inspectors, ECG Technicians and Pharmacy Technicians.

### Deputising Allowance paid even though the Stipulated Conditions were not abided with

During 2013, nine employees employed by RHKG were in receipt of a deputising allowance for carrying out higher duties than their position entails. However, not all the conditions stipulated in PSMC Section 2.4.6.4 were met. Thus, they were not eligible to such allowance.

### Internal Controls

#### Personal Files not updated

The personal files of the employees included within the audit sample were not being properly

<sup>2</sup> From the payrolls issued during 2013, it was noted that this Officer was not receiving any salary from RHKG, but was only being paid this allowance.

<sup>3</sup> At the time, the employee was a Senior Occupational Therapist.

updated. Various related documents that were expected to be filed, mainly covering contracts and approvals, were only made available following an enquiry during the audit. Moreover, one of the employment contracts requested was still not provided for audit purposes as this could not be traced.

### Palm Readers not being used

From a sample of 10 employees, three of them, namely a Driver and/or Security, a Medical Secretary and a Nursing Aide, record their attendance manually rather than make use of any of the three palm readers installed at RHKG. Management claimed that due to Union(s) directives, employees cannot be enforced to use them. However, the actual directive provided by RHKG for audit purposes, is dated 18 August 2009 and refers only to Nurses and Nursing Officers employed with ZCH.

### Application Forms not endorsed

As stated by RHKG, *“All forms, prior to being accepted and processed by payroll office, have to be signed by the applicant, his/her direct supervisor, by the departmental manager, and head of department. Once said forms are processed by payroll office, said forms are countered signed ...”*. This was applicable for application forms covering overtime, paid leave, change of duty and Time Off *In Lieu* (TOIL).

However, this procedure was not always being enforced. By way of example, from the audit sample, it transpired that two applications for payment of extra hours were not signed by the Personnel Office. Likewise, four applications for paid leave were neither endorsed by the Head of Section nor by the Head of Department.

### Other Shortcomings

#### Salaries stipulated in the Collective Agreement not in line with Letters and/or Contracts

##### a. Contract not updated

A Medical Secretary was being paid a salary in line with Scale 9 Pay Point 7 (2013: €20,437), as stipulated in Appendix B to the

Collective Agreement entered into between ZCH and *UHM*, dated 20 September 2010. However, on the same date, a side letter to the said Agreement indicated that the incumbent was entitled to Salary Scale 10 Pay Point 5 (2013: €18,298), up to the maximum of the said Scale (2013: €19,113). Furthermore, the latest contract available in the personal file, was a contract of service dated 1 June 1995 for an indefinite period, stipulating a maximum annual salary of €11,083 after two years, which amount is much less than that specified in the highlighted salary scales.

##### b. Missing Contract

The only document available in the personal file of the Hotel Services Officer was a letter of appointment dated 22 August 2000, stating that the Officer was to be upgraded to Scale 12 after five years and Scale 11 after another five years. However, at least during 2013, this Officer was remunerated an annual higher salary as per Scale 10 Pay Point 7. According to RHKG, the respective contract could not be found.

#### Contract of Service not in place

On 28 October 2009, the then General Manager informed a Nursing Aide, that her contract of service, signed prior to 7 December 2007, was converted to an indefinite one. However, the only contract of service available in the personal file was effective from 10 March 2008, for a definite period of three years.

#### Lack of Control over Time Off *In Lieu*

##### a. Balances not readily available

Whilst application forms for accumulation of TOIL hours and/or hours to be availed of were provided, these forms were not properly designed to record the opening and closing balances. Thus, correct balances at any point in time could not be determined, since the outstanding balance was not always indicated, and in certain cases an incorrect balance was recorded when compared to the stipulated balance in the prior and/or subsequent forms. Therefore, authorising

officers are approving requests without having an indication whether the officers concerned have sufficient outstanding balance, if any.

Furthermore, during November 2013, *i.e.* at commencement of the audit, and on 23 January 2014, all documents related to TOIL were requested by NAO. However, records indicating the outstanding balances were only provided on 28 February 2014, *i.e.* over three months following the first request. In the circumstances, the possibility that balances of TOIL were compiled subsequent to audit queries cannot be excluded.

**b. No Policies for the Accumulation of Time Off in Lieu**

On five instances, an officer worked less than the required number of hours and any differences were recorded as TOIL. The Hospital alleged that TOIL was accumulated in 1997 and claimed that no forms were requested to be filled in.

**Change of Duty**

Whilst reviewing the applications for change of duty of the six employees falling in the audit sample who work on a shift time-table, the following shortcomings were noted:

- a. On certain instances, the application was raised on the same day, or long after the officers refrained from duty, sometimes even more than a month later, implying that no prior written notice was given.
- b. In a number of instances, approval from higher authority was sought after the change of duty actually occurred.

**Working Long Hours at a stretch**

As per S.L. 452.87 Article 5(1), “*Every worker shall be entitled to a rest break where the working day is longer than six hours*”. However, from the 10 employees selected for testing, three of them did not have any break deductions, even though their working day consisted of seven or eight hours.

Furthermore, overtime performed by a Senior Principal Pharmacist ranged from 0.12 to 6 hours, over and above the normal eight hour working day. Since this employee does not stop for a break, this implied that he ended up working long hours at a stretch. In one instance in the sample period, he worked six hours overtime after an eight hour day’s work. An Assistant Accounts Officer, falling in the audit sample, was also entitled to a break during his eight hour working day. However, no break was deducted when working overtime of eight hour or more on Saturday in the sampled period.

**Compliance Issues**

***Relevant Approvals to enter in Contracts of Service not sought***

As per PSMC Section 1.4.1.2 and OPM Circular No. 20/2006, contracts of service are subject to clearance from the Office of the Prime Minister (OPM). Although three out of the 10 employees selected for testing had a contract of service dated subsequent to 2006, relevant approvals were not sought in two of these cases. Moreover, one of these contracts was signed for an indefinite period.

***Return of Allowances not compiled***

A bi-annual return of allowances, in line with PSMC Section 2.4.1.2 and MFEA Circular No. 4/2003, providing updated information regarding allowances paid by RHKG, is not being prepared. The latter claimed that it is not regulated by PSMC.

***Prior Authority for Payment of New Allowances not provided***

As per PSMC Section 2.4.1.3, authority for the creation of new allowances must in all cases be sought from PAHRO and MFIN. As indicated in the Manual of Allowances payable to Public Officers, the request for a new allowance is to include the amount of allowance to be paid, a justification and the estimated number of employees who will receive the allowance.

As already highlighted under ‘Control Issues’, the relevant approval for the creation of a weekend

allowance was not provided by RHKG. Similarly, as per contract of service entered into on 15 February 2010, with effect from 1 January 2009, between the Hospital Management Committee of ZCH and a Hospital Nursing Manager, the latter is to receive an all-inclusive allowance of €6,202 *per annum*. Although such allowance was neither covered by PSMC nor by the sectoral agreements, requests and relevant approvals from PAHRO and MFIN were not provided for audit purposes.

## Recommendations

### Key Issues

#### Weak or Lack of Internal Controls

Effective internal control measures need to be strengthened, to address risk management. These are fundamental to the successful operation and day-to-day running of the Hospital. It is also recommended that ongoing monitoring activities, to evaluate and improve on the effectiveness of internal controls, are carried out. Spot-checking transactions or basic sampling techniques can provide a reasonable level of confidence that the controls are functioning as intended.

#### Statutory Bonuses not paid *pro rata*

RHKG is to ensure that it pays bonuses *pro rata* to employees on reduced hours, in line with Chapter 452, Article 24(d) – ‘Employment and Industrial Relations Act’.

#### Lack of Segregation of Duties

RHKG is expected to step up internal controls and address the issue of lack of segregation of duties. Continuation of the key process is thus to be ensured at all times.

### Control Issues

#### Overtime

##### *Prior Requests to perform Overtime not made*

Whilst acknowledging that the requirements of a Hospital are different from those of other departments, the need for overtime, especially that

which is required on an ongoing basis, is to be well defined. Requests for overtime are to be raised in a timely manner to ensure that proper authorisation by the Permanent Secretary is granted prior to the commencement of the respective work, including justification for the request, the total number of hours of overtime required and specific targets to be attained during overtime work. Disbursements for the payment of overtime are not to be effected unless the necessary authorisations are invariably obtained.

##### *Irregular Payments paid to Principal Pharmacist for Ineligible Overtime approved by himself*

An exercise is to be carried out by RHKG in order to identify all employees above Salary Scale 7 who are receiving ineligible overtime payments. Furthermore, positions covered by an agreement that stipulates that they are regulated by PSMC are not to be paid for overtime attendance of less than 30 minutes. Thus, any overpayments are to be immediately recouped. In addition, it is to be ensured that requests for payment of extra hours are invariably endorsed by their respective superiors.

#### Allowances

##### *Clause in Agreement with respect to Meal Allowance open to subjective interpretation*

Discussions are to be held with UHM and other related parties in order to establish whether deductions to the entitlement as per Clause 5 should be formally clarified. Eligibility to the meal allowance is to be clearly defined by means of a side letter, as well as in future agreements between the Government of Malta and the Union.

##### *Payment of Weekend Allowance*

Management is to ensure that the applicable rate and conditions of payment of the weekend allowance are formally clarified and endorsed by both the employer and the employee. Furthermore, relevant approvals are to be obtained.

##### *Justification of Allowances not provided*

If payment of the allowances in question is deemed justifiable, RHKG is encouraged to liaise with

the pertinent authorities to obtain the necessary approvals. The Hospital is also to exercise the necessary controls and ensure that the guidelines on payment of allowances are strictly adhered to. All authorised allowances are to be reviewed periodically, in order to ascertain whether the conditions under which they were granted are still relevant or not.

*Incorrect Allowance paid to Social Workers resulting in Overpayments*

Management is to ensure that stronger internal controls are in place, to manage public funds entrusted to it more effectively. Regular reconciliations are to be carried out, to ascertain that the allowances paid are in line with that stipulated in the respective sectoral agreements. Furthermore, RHKG is encouraged to carry out an exhaustive exercise, and rectify the amount of allowance to be paid, to avoid any further unjustified disbursements from public funds.

*Deputising Allowance paid even though the Stipulated Conditions were not abided with*

RHKG is to regularise its position prior to continuing with the payments of the deputising allowance. The necessary approvals and/or endorsements are to be obtained, and any discrepancies in the payments already made are to be rectified.

**Internal Controls**

*Personal Files not updated*

All supporting documents are to be retained in the relevant file, in order to ensure that the requested information is always available in a timely manner, to enable verification by third parties.

*Palm Readers not being used*

All employees at RHKG are expected to start using the palm readers already installed on-site. As also specified in PSMC Section 3.1.6.1, this will increase controls over the actual hours worked, eliminate manual data entry and simplify salary calculations.

*Application Forms not endorsed*

RHKG is to ensure that application forms are duly endorsed as applicable.

**Other Shortcomings**

*Salaries stipulated in the Collective Agreement not in line with Letters and/or Contracts*

RHKG is to ensure that all employees are covered by valid contracts in line with the collective agreement, in order to regulate the salary and conditions of their employment.

*Contract of Service not in place*

Considering that in November 2007, OPM approved the recruitment of 74 Nursing Aides, NAO recommends RHKG to check that all the contracts in place are still applicable, including the Officer in the audit sample.

*Lack of Control over Time Off In Lieu*

Controls over recording of TOIL are expected to be strengthened. Officers in charge are also to ensure that records are appropriately updated. A policy is to be drawn up, clearly stipulating the maximum total hours which may be accumulated and the period during which these hours can be availed of.

*Change of Duty*

Ideally, requests for change of duty are to be presented well in advance, to enable Management to plan and allocate staff effectively. In addition, employees requesting change of duty are to include the name of the replacing officer for control purposes. Officers authorising these requests are to ensure that such consent will not negatively affect the level of service, or give rise to additional costs to maintain the expected standard. Should this be the case, requests are to be declined. Moreover, for practical reasons, change of duty is to occur between similar shifts.

### *Working Long Hours at a stretch*

In order to avoid any possible inconsistencies with other employees and non-compliance with employment regulations, it is being recommended that break is invariably deducted when working more than six hours. As per S.L. 452.87 Article 5(2), collective agreements or any other agreements entered into between the employers and employees, should also stipulate the entitled rest break, including its duration and the terms on which it is granted.

### *Compliance Issues*

#### *Relevant Approvals to enter in Contracts of Service not sought*

Relevant approvals are to be obtained as per OPM Circular No. 20/2006, before entering a contract of service.

#### *Return of Allowances not compiled*

Management is to ensure that an officer within RHKG is entrusted with the responsibility of compiling such return in an accurate and timely manner.

#### *Prior Authority for Payment of New Allowances not provided*

In line with standing regulations, proper authority is to be obtained in writing prior to granting new allowances.

### **Management Comments**

Management concurred with most of NAO's findings. Remedial action has already been taken in particular areas. During an exit meeting held between NAO and Management, the latter also stated that it intends to take further corrective action in line with NAO's recommendations. The following comments and reservations were also submitted:

- To address the issue regarding the weak and/or lack of internal controls, Management claimed that a request was made for the

engagement of a Finance Manager and Accounts Clerks.

- RHKG declared that any payments for overtime not approved by Management will be recouped over the next few months.
- The Occupational Therapist agreed that the supervision allowance should not have been paid and therefore the money will be recouped.
- Up to the audit visit, RHKG was still acting according to previous methods when staff was working at ZCH, *i.e.* in an autonomous way.
- RHKG had a meeting with Unions to discuss the use of palm readers, but the latter refused to accept such suggestion.
- Since in most instances, a change of duty is requested by Management and initiated on the same day, applications are done after the initial change.

Furthermore, the following issue was not properly addressed:

- Although NAO pointed out that the statutory bonuses are to be paid *pro rata* in line with the Employment and Industrial Relations Act, RHKG stated that, "... *unless proof of contracts or agreements is provided, statutory bonuses will be paid pro rata*".

Management comments made no reference to the following recommendations:

- The carrying out of an exercise, in order to identify and recoup ineligible overtime payments made to the respective employees, including those to officers above Salary Scale 7 and those who performed less than 30 minutes overtime.
- Clarification from MFIN, whether the retrospective payment of the disturbance allowance was justified and duly approved.
- Ascertaining that the social workers allowance is paid in line with that stipulated in the respective sectoral agreement.

- To delve into the issue of unreconciled payroll amounts, in order to provide NAO with an explanation for the noted variances.
- Explaining the concept of flexi time to the officers concerned.
- Deducting break in line with employment regulations when working more than six hours.

# Rehabilitation Hospital Karin Grech

## Expenditure

### Background

Financial Estimates 2013, Recurrent Vote 47, provided a budgetary allocation of €11.1 million for the Rehabilitation Hospital Karin Grech (RHKG) under Contributions to Government Entities. However, the actual expenditure for the year amounted to €13,228,056<sup>1</sup>. Apart from the Personal Emoluments, a substantial portion of this expenditure, totalling €2,518,248, was utilised for the procurement of cleaning and upkeep services, support services and food.

### Audit Scope and Methodology

The audit scope was to determine the level of internal controls over expenditure, and to ensure efficient administration of public funds, in line with standing laws, regulations, policies and procedures, also making recommendations, where warranted.

For the expenditure items selected for testing, the National Audit Office (NAO) requested files, including the related Purchase Orders, invoices, Value Added Tax (VAT) fiscal receipts and any other relevant documentation. The sample selected was analysed and examined mainly to ensure that payments were backed up by the necessary documentation, and that Public Procurement Regulations (PPR), in particular, were adhered to.

### Limitations on Scope of Audit

Following a request for the timesheets covering cleaning and food handling services for the year under review, NAO were only provided with the attendance records for the months of June to December 2013. Management claimed that the other timesheets could not be traced. This limited this Office to carry out the necessary verifications on just two invoices falling within the sampled period.

Testing of clerical services was also limited, since the related file could not be traced.

### Key Issues

#### *Public Procurement Regulations continuously by-passed*

Throughout the audit testing, comprising a sample of transactions from various accounts, it was noted that the majority of procurement by RHKG was not made 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. Procurement of services directly from the open market without the issuance of a call for tenders and/or quotations, notwithstanding the materiality of the amounts involved, at times running into millions of euro.

<sup>1</sup> This amount excludes salaries, in aggregate amounting to €3,045,315, refunded by other Government entities.



- b. Expired contracts still in use without being renewed.

### ***Fundamental Internal Controls non-existent***

Whilst reviewing the invoices and payments included within the audit sample, it was noted that a total of 72 invoices out of a sample of 233, in aggregate amounting to €533,218, were not signed as certified correct, but still processed for payment. Likewise, in 102 instances, amounting to €663,806, the approval for payment was not endorsed by the Financial Controller (FC) or any other Accounting Officer.

On the other hand, 119 invoices in the audit sample, amounting to €1,191,149, were still endorsed by an officer in charge, notwithstanding that supporting documentation indicating the rates and services to be charged were not available, and/or amounts invoiced were incorrect. It was also observed that at times, the same person was both certifying the invoice as correct and approving the respective payment, resulting in lack of segregation of duties. A number of shortcomings noted, very often resulting in overpayments, are reported upon in detail under 'Control Issues'.

## **Control Issues**

### ***Cleaning and Food Handling Services***

#### ***Procurement direct from the Open Market***

A call for tender for cleaning and food handling services was never issued by RHKG, notwithstanding that over €3.6 million were paid for such services rendered between 2007 and 2013<sup>2</sup>.

The procurement of these services was made directly from the open market and the only source of documentation, provided for audit purposes by RHKG in this respect, was an invalid and expired contract for service agreement, which indicated that:

- a. The service provider was engaged by Zammit Clapp Hospital (and not by RHKG).

- b. It was effective from 15 July 2007 for a definite period of one year, renewable for a further year following a written consent by both parties.

- c. It only covered cleaning services (hence the food handling services were not included).

Furthermore, no official renewals of the contract were provided to NAO, following requests.

### ***No Contract for Service Agreement in place***

Since there was no valid contract in place to cover the services rendered, the rates, as well as the respective terms and conditions agreed upon by both parties, were nowhere indicated. These were expected to include the following:

- a. The daily personnel requirement.
- b. The minimum and maximum number of working hours the employees have to work daily.
- c. Break entitlement.
- d. The rates charged for the different services offered.
- e. The rate that is to be charged when extra hours are required over and above the normal working timetable, and/or when the services are entailed on Sundays and Public Holidays.

The cleaning of the public areas and the manual duties, which include the food handling services, were actually being charged at an hourly rate of €7.13 (VAT excl.). On the other hand, the rate of the cleaning services of the rest of the Hospital was €4.16 (VAT excl.) per hour. However, RHKG confirmed that no supporting documentation was available to substantiate the rates charged.

### ***Hours claimed for Payment not corroborated to the Timesheets***

Throughout 2013, the employees engaged by the respective service provider used to sign and record their time in and/or out on two manual attendance

<sup>2</sup> The last invoice paid by the Hospital in 2013 covered services carried out until 11 August 2013.

records, one pertaining to the Hospital and one to their employer. Subsequently, the latter submits invoices detailing the man-hours performed by his employees for every four weeks of service.

This Office attempted to reconcile the number of hours claimed for payment over a 12-week period<sup>3</sup>, against the total number of working hours recorded by the employees on the attendances pertaining to the Hospital. However, this proved futile as a material difference of 2,945 hours remained unreconciled; thus none of the payments could be validated.

As already indicated, the services provided entailed two different hourly rates, that of €4.16 and €7.13 (both VAT excl.). However, the timesheets compiled by the respective employees failed to indicate the area and/or type of service they performed. Thus, the exact amount overpaid cannot be determined, ranging from €12,251<sup>4</sup> to €20,998<sup>5</sup>.

#### Discrepancies between Attendance Records

Up to end December 2013, personnel were still making use of manually filled timesheets to log the hours performed at the Hospital. An automated attendance recording system was later installed at RHKG in 2014.

- a. Whilst reviewing the attendance records for cleaning and food handling services made available for the necessary audit verifications, it was noted that these were not being verified by the officers responsible for the Hospital's housekeeping, namely the Hotel Services Officer and/or his Assistant, to ensure the accuracy of the hours and details recorded therein. Various anomalies in the time recording were noted by this Office, such as time out overwritten, or not included. These shortcomings, made it difficult to quantify the number of hours that were actually performed.

- b. As part of the audit testing, NAO also attempted to reconcile the hours recorded on the attendances for a particular month, namely August 2013, pertaining to records kept by the service provider and those maintained by RHKG. Various discrepancies between the time in and/or out recorded on the timesheets were noted.
- c. Despite that no checking whatsoever was being carried out, on several instances, the Hotel Services Officer, or the Assistant, endorsed the number of hours claimed on the invoices, and eventually payments were effected in full.
- d. During a meeting held at RHKG, the Hotel Services Officer verbally stated that the foregoing timesheets were kept at the service provider's Supervisor office, which is located at the Hospital, rather than kept by RHKG for control purposes.

#### Excessive Number of Hours performed by the Service Provider's Employees

Notwithstanding that Government has been striving to ensure that any contracts awarded by Government departments or public sector organisations do not lead to precarious employment conditions, no action whatsoever was taken by RHKG with respect to the excessive number of hours performed weekly by the employees.

By way of example, from week 25 to week 40 of 2013, 43% of the employees recorded more than 50 hours in a week. Two instances were also noted whereby, in each case, an employee recorded 91 hours in a week.

According to FC, the contracted employees are entitled for a break, however the invoices submitted by the service provider do not reflect this.

<sup>3</sup> This period includes four weeks of service, which were paid in 2014, since testing on 2013 payment was limited on just two invoices of four weeks each.

<sup>4</sup> The hourly rate of €4.16 (VAT excl.) charged for the cleaning of wards, administration area, stores *etc.*, multiplied by 2,945 hours.

<sup>5</sup> The hourly rate of €7.13 (VAT excl.) charged for the cleaning of public areas and the manual duties, including food handling services, multiplied by 2,945 hours.

### ***Procurement of Services not in line with Pertinent Regulations and Other Shortcomings***

As highlighted under ‘Key Issues’, the majority of services were being directly procured from the open market. Moreover, these were not even covered by approvals from the Ministry for Finance (MFIN) or Department of Contracts, as applicable.

Furthermore, as per Public Service Management Code and OPM Circular No. 20/2006, contracts for service are subject to clearance from the Budgetary Operations Division within MFIN. However, the approvals to outsource the following services were not provided in line with the applicable standing regulations.

#### **Provision of Meals to In-Patients**

More than €4 million were paid by RHKG for the provision of meals, covering the period from April 2007 up to end December 2013. Management confirmed that, so far, RHKG did not enter into a formal agreement with the contractor, but it was using the contract for the provision of catering services to in-patients at Mater Dei Hospital, St. Luke’s Hospital and Sir Paul Boffa Hospital.

#### **Care Worker Services**

As from June 2011 up to end December 2013, RHKG paid over €1 million for care worker services. However, the only document made available was an expired contract, covering services to Mater Dei Hospital and Primary Health Care up to September 2012.

#### **Clerical Services**

a. As from January 2008, clerical services started being provided to the Hospital, the latter paying at least €480,000 to a particular service provider up to end December 2013. Notwithstanding this, neither a tender was issued, nor a formal agreement was ever entered into.

NAO compared the clerical hours provided by the service provider as per attendance records, with the quantity of hours charged on invoices that were paid in 2013. An

aggregate amount of 956 hours was noted to be overstated on the claims for payment. Thus, one can conclude that internal controls were practically non-existent.

b. No contract was reached with another service provider for the provision of clerical services, although an aggregate amount of €46,683 was paid, from commencement date in July 2011 up to 31 December 2013. In addition, no supporting documentation was provided explaining the selection procedure of how this company was chosen, *i.e.* the original tender, biddings, evaluation report *etc.* No reason to justify why this service provider was selected directly from the open market was given.

c. Two individuals were chosen to provide further clerical services following interviews held by Management. Their contracts were for a period of six and 12 months respectively, one commencing on 1 February 2010 and the other on 1 May 2011.

Although the two contracts in question did not include the option of renewal on their expiry, these were extended for subsequent periods. As a result, up to end December 2013, aggregate amounts of €51,929 and €14,993 respectively, were not covered by the original contracts.

d. Clerical services were also provided by another company, who was paid *circa* €7,000, as from commencement date in June 2007 up to end December 2013. This procurement was also direct from the open market and again no contract was in place.

#### **Rental of Bed Mattresses**

Bed mattresses started being rented as from July 2008, amounting to over €200,000, from the said date up to end December 2013. Then again, no tender was issued, and no contract was in place.

#### **Childcare Services**

With effect from January 2006, RHKG’s employees started benefiting from childcare services. Up to 31 December 2013, the Hospital paid an amount of

€147,025 to this effect. It transpired that a tender was not issued and thus, this service provider was selected from the open market.

### Testing of Potable Water

The only document provided, with regard to the services rendered for testing of water, was a quote dated 5 November 2011, submitted by the supplier. Notwithstanding the date of the quote, it was noted that payments started being made as from November 2008, *i.e.* three years earlier. Since a signed contract was not provided, the amount of *circa* €27,000, which was paid as from 2008 up to end December 2013, could not be checked to source documentation.

### Information Technology Consultancy Services

During the audit, it transpired that as from the date an individual started providing Information Technology consultancy services, *i.e.* in September 2009, till end December 2013, total payments made amounted to €12,693. However, RHKG stated that a contract was not in place. Following a thorough analysis of the amounts paid in 2013, it was noted that the rate charged was €35 per hour.

### Accountancy Services

Up till 13 March 2013, an Assistant Accounts Officer was employed within the Finance Section at RHKG. Three days following his resignation, the foregoing officer started providing his accountancy services to RHKG at the hourly rate of €25, as against that of €7.92 he was receiving as a staff member.

Despite that RHKG paid the amount of €11,250 for this service in less than 10 months, *i.e.* from mid-March to end December 2013, there was no call for tenders or quotations published in the Government Gazette. The Financial Controller claimed that this individual was directly appointed by the Hospital to continue providing his services, due to shortage of staff within RHKG's Finance Section.

MFIN's covering approval for direct order was only requested by RHKG on 17 September 2013, *i.e.* six months later, and when RHKG had already

paid the total amount of €5,250. Moreover, FC confirmed that such approval was not given. Notwithstanding this, the foregoing individual was still providing his services up to the date of audit testing, *i.e.* May 2014, and had already received an aggregate amount of €15,300.

No contract for service, confirming the rates to be charged, the number of hours to be inputted per week, and the duration of the said engagement, was in place. As a result, it could not be ascertained that agreed terms and conditions, if any, were followed.

The job sheets, indicating the man-hours prepared and presented for payment by the individual giving accountancy services during 2013, were not being verified by an independent officer. Only FC was endorsing these documents prior to effecting payment, resulting in lack of segregation of duties and internal control.

### Sickness Absence Control Services

Services rendered by an entity, engaged since March 2006 to assist RHKG in controlling its employees' sickness absences, was also procured directly from the open market, and therefore neither a call for tenders, nor quotations were published in the Government Gazette.

Furthermore, an agreement was not entered into between RHKG and the service provider, confirming the rates to be charged by the latter and the duration of the said engagement. Since the date of commencement up to end December 2013, over €10,000 were paid to the foregoing entity.

### Repairs of Vehicles

During 2013, the aggregate amount of €7,081 was paid to an individual for parts and manual labour on the various vehicles held by RHKG. It was observed that no quotations were obtained prior to procurement of this service. The same mechanic was also entrusted with purchasing the parts needed, and then reimbursed accordingly. RHKG claimed that the services from this provider are procured by direct order since there is no qualified in-house personnel to assess the damage in vehicles. Furthermore, from documentation provided to this Office, it was noted that the

Purchase Requisition and actual Purchase Order were only raised after the respective vehicles had been repaired.

Following queries raised by this Office, it transpired that:

- a. Prior to the commencement of works, RHKG does not obtain clear and accurate details of the repairs required and parts needed to be replaced on a vehicle.
- b. RHKG does not ask the garage to provide in writing, the provisions on works required, costs and charges, guarantees if any, completion dates and payment terms.

### Physiological Services

Notwithstanding that during the contract period of one year, as from 3 February, a Physiologist was paid a total amount of €4,205 for the provision of physiological services, Management was not aware how this service provider was chosen.

### Secretarial Services

During 2010, an advert was published in a particular newspaper, requesting secretarial services to the Hospital Management Committee. An individual was selected following an interview and the respective contract was signed for a period of 12 months, commencing on 2 May 2011. Notwithstanding the latter date, RHKG confirmed that this Secretary started providing secretarial services in December 2010, receiving an aggregate amount of €2,207 not covered by the agreement.

Furthermore, although the contract in question did not include the option of renewal when it expires, this was extended for subsequent periods, resulting in an aggregate amount of €4,064 as from April 2012 up to end December 2013, *i.e.* the period not covered by the original contract.

### Transport – Shortcomings related to Logbooks

Following the review of all 10 logbooks, covering

different periods, various incorrect and unreliable information was noted, indicating weak internal controls over vehicle usage and fuel consumption. Moreover, in a number of cases, the pump attendant's signature was the same as that of the officer performing the journey. Such irregularities may remain unnoticed since the daily transport records were not always endorsed by the officer in charge.

### Meal Allowance to Doctors not validated

- a. The meal allowance paid to Doctors working on call for more than 24 hours at RHKG was not backed up with formal approval. Since this allowance started being paid in 2007, RHKG paid an aggregate amount of €15,239 till end December 2013, out of which €4,354 were paid in the year under review.
- b. On a number of instances, Doctors were incorrectly paid, mainly for days that they did not attend for work, or for days not exceeding a 24-hour schedule, notwithstanding the endorsements on the relevant claims.
- c. All 11 payments, randomly selected for testing, were endorsed by FC only retrospectively, *i.e.* following the actual payment.

### Compliance Issues

#### Service Providers not compliant with VAT Legislation

From verifications on the transactions falling in the audit sample, it transpired that:

- a. Two service providers registered for VAT under Article 10, did not issue either tax invoices<sup>6</sup> or fiscal receipts covering various payments, totalling €270,964 and €3,018 respectively.
- b. Four suppliers registered under Article 11 of the VAT Act failed to supply RHKG with

<sup>6</sup> The issuance of tax invoices in this case is considered valid since RHKG was inappropriately VAT registered under Article 10.

a fiscal receipt against payments made to them for services rendered, in aggregate amounting to €19,374.

- c. An individual was not requested to furnish a declaration form, confirming that the person is exempt from registering for VAT under Article 11 of the VAT Act, on the basis of Legal Notice (LN) 524 of 2010, as indicated on the respective invoices.

## Recommendations

### Key Issues

#### Public Procurement Regulations continuously bypassed

RHKG is to strive to ensure that the method of procurement is compliant with the applicable regulations, thus ascertaining transparency and fairness, as well as that the most competitive prices are obtained. As far as possible, all suppliers are to be given equal opportunity to submit their quote, *i.e.* a call for quotation or tender is at least to be published in the Government Gazette.

#### Fundamental Internal Controls non-existent

It is important to stress the obligation that all invoices are invariably verified and certified as correct by the officers in charge, in order to confirm their accuracy before processed for payment. Endorsing officers are to be held responsible for the correctness of the amounts and details quoted in the invoices. Subsequently, the actual payments are to be authorised by a different individual, thus enforcing internal controls.

### Control Issues

#### Cleaning and Food Handling Services

##### *Procurement direct from the Open Market*

For the sake of fairness and transparency, RHKG is to regularise its position in line with PPR without exception of fail when purchasing services. Thus,

a call for tenders for cleaning and food handling is to be issued without further delay, in accordance with standing regulations. Reference is also to be made to the relevant Contracts Circular issued in 2014, indicating that as from 2 June 2014, the company currently providing such services is to be excluded from the award of public contracts for a period of two years.

In the meantime, an approval for direct order is to be obtained from MFIN, until the new tender is adjudicated, limiting it to the barest minimum. It is also to be ensured that all ongoing services provided to RHKG are covered by valid contracts at all times.

##### *No Contract for Service Agreement in place*

All engagements are to be formally backed up by an agreement, signed by the parties involved. Applicable conditions of service, rates to be charged, and the duration of the agreement, are to be clearly spelled out.

Moreover, transparency in the management of public funds is an integral part of good governance and accountability. Thus, Management is to give priority to this issue in order to have a public contract in place, following a transparent procurement process without further delay.

##### *Hours claimed for Payment not corroborated to the Timesheets*

Requests for payment must be substantiated by adequate documentation, enabling full audit trail for independent verifications by third parties.

Furthermore, sound internal controls are to be implemented. Invoices are not to be paid prior to being thoroughly checked and certified correct by an authorised officer. Moreover, it is to be made clear to all officers that, when endorsing documents and/or certifying invoices, it is implied that one is assuming the responsibility that the data and/or amounts contained in those documents are correct. Thus, unless adequate checks are carried out to ensure that it is the case, no certification is to be endorsed, and more importantly no payments are to be effected.

Undue payments are to be recovered following a comprehensive exercise to identify the amount overpaid to the service provider in question.

#### *Discrepancies between Attendance Records*

Controls are to be put in place for the proper checking, ensuring that the computerised attendance reports tally with the hours charged on the respective invoices. As reiterated above, officers verifying and endorsing invoices are to be held accountable in case they fail to carry out their duties properly.

#### *Excessive Number of Hours performed by the Service Provider's Employees*

As stipulated in OPM Circular No. 12/2013, RHKG is obliged to ensure that employment conditions of the service providers' employees are safeguarded and guaranteed. Whilst RHKG is to abide by the various Circulars issued by Government in an effort to eradicate precarious work, it is also to ascertain that all service providers comply with the Employment and Industrial Relations Act, Employment and Training Services Act, as well as the Occupational Health and Safety Authority Act.

#### *Procurement of Services not in line with Pertinent Regulations and Other Shortcomings*

RHKG is to ensure that the provisions and thresholds imposed by PPR are invariably adhered to. Besides ascertaining that value for money is achieved, such procedures enable transparency and accountability. While the Hospital may in exceptional cases resort to direct orders, after obtaining the appropriate MFIN or the Department of Contracts approval as applicable, this is not to be considered as best practice.

Contracts endorsed by both parties are expected to be in place, to outline the terms and conditions binding the contractual agreement and to be referred to when verifying invoices before they are approved for payment. Extensions to existing contracts are only to be granted if a relative clause was already incorporated in the original Tender and the respective contracts.

Relevant approvals are also to be obtained as per OPM Circular No. 20/2006, before entering a contract for service.

#### *Transport – Shortcomings related to Logbooks*

The relative provisions of the Public Service Management Code covering logbooks are to be complied with, in order to monitor the use of vehicles and fuel consumption. Amongst other obligations, the officer in charge is to request the logbooks for proper examination at least on a monthly basis and include a certificate as required by standing regulations.

#### *Meal Allowance to Doctors not validated*

Unless duly justified and officially approved, meal reimbursements to Doctors are to be discontinued. Management is to ensure that stronger internal controls are in place, to manage public funds entrusted to it more effectively.

#### *Compliance Issues*

##### *Service Providers not compliant with VAT Legislation*

Accounting Officers are to ensure that all VAT registered suppliers, who received payments or part thereof for goods and services provided, adhere to VAT Regulations by being furnished with a tax invoice or a fiscal receipt as applicable. In cases where the supplier(s) lacks adherence to VAT Regulations, as per MF Circular No. 5/2002, the Hospital should immediately discontinue to purchase from such defaulter(s) until this situation is rectified.

#### *Management Comments*

Management confirmed that although attempts have been made through the years, to change the old practices to conform to Government regulations, much still needs to be done. It further stated that, whilst major issues reported upon by the Auditors had started to be tackled before the audit, efforts are being made to regulate matters and comply with NAO recommendations. The

following comments and reservations were also submitted:

- In 2011, RHKG submitted documents to the Central Procurement and Supplies Unit (CPSU), relating to the issue of a new tender for cleaning and food handling services. However, this tender was never issued.
  - Management confirmed that when checking the attendances of cleaning and food handling services, no reconciliation could be made because of the unorganised and undisciplined way these attendances were kept.
  - In order to eliminate precarious work, hours will be monitored and an allowance for break-time will be deducted accordingly.
  - RHKG is waiting for CPSU to issue a tender for clerical services to cover the whole Department. Furthermore, the Hospital confirmed that clockings for Clerks taken from RHKG Personnel Office are not reliable.
  - A tender is being issued by CPSU to purchase bed mattresses, childcare services, sickness absence control services and repair of vehicles.
  - Management stated that the individual providing Information Technology consultancy services was engaged because he was already well-versed with the system and thus could provide the most efficient service.
  - The provision of accountancy services was regularised following the issue and adjudication of a departmental call for tenders.
  - The shortcomings related to logbooks are all existent and measures will be taken to correct this.
- Management comments did not properly address or make any reference to shortcomings raised under the following titles:
- Public Procurement Regulations continuously by-passed.
  - Fundamental Internal Controls non-existent.
  - Cleaning and Food Handling Services
    - No Contract for Service Agreement in place.
    - Hours claimed for Payment not corroborated to the Timesheets.
  - Procurement of Services not in line with Pertinent Regulations and Other Shortcomings – Clerical Services (Sections b, c and d).
  - Meal Allowance to Doctors not validated.







Statutory NGOs

# Conservatorio Vincenzo Bugeja

## Background

The Conservatorio Vincenzo Bugeja (CVB) was instituted by virtue of the Deed made by the Marquis Vincenzo Bugeja on 4 December 1880. The main objective of the Trustees is to execute the Founder's will, primarily by managing the funds and contributing to the running of the residential homes, which provide therapeutic and education services to female adolescents, between the ages of 12 and 17, encountering behavioural problems.

## Audit Scope

The audit was conducted in accordance with generally accepted auditing standards. These standards require, planning and performing audit procedures in order to obtain reasonable assurance as to whether the internal control structure at the entity concerned is adequate. It was also ascertained whether the Foundation Deed, together with the policies set by the Accounting Policy Document, approved by the Board of Trustees (BOT) of CVB on 20 June 2011, have been followed.

The Management Letter for the year ended 31 December 2012, drawn up by the National Audit Office (NAO), contained comments and recommendations to provide constructive advice to the Board.

## Observations

### *Limited Funds used for Welfare Assistance*

The main objective of BOT is to execute the Founder's will, primarily by managing the funds and contributing to the running of *Fejda* Programme and Jeanne Antide Home. During the previous two years, it was observed that limited funds were used for Welfare Assistance compared to earlier years. The aggregate expenditure to this effect was only €4,798 in 2012, which is even less than the amounts paid in the previous two years, totalling €8,020 and €8,094 in 2011 and 2010 respectively. In view of the continuous substantial surpluses, the Board is expected to take a more proactive approach to the well being of the homes' residents, by increasing the financial allocation accordingly.

### *Lack of Transparency in Procurement*

It was noted that during 2012, CVB purchased items, with an aggregate value of €10,572, from three companies where its Chairman is the ultimate major shareholder. It also committed itself to a maintenance agreement, valued at €10,620, over a period of three years with one of these companies.

No evidence was provided that there was a call for quotations prior to the procurement in question, limiting the level of transparency and accountability, especially when dealing with funds belonging to a Charitable Trust.

### ***Presentation of Accounts not in line with International Accounting Standards***

#### **Fixed Assets**

CVB has maintained its policy of giving a notional value of €233 for each of its 48 properties, with the exception of two premises which are recognised at cost, as one was purchased and has been developed since recent years, whilst the other, which is on a short-term rental agreement, has been valued on the basis of costs for improvement. This valuation approach is not in compliance with International Accounting Standards (IASs) which require more disclosure on the actual valuation of the properties.

#### **Financial Assets**

The Conservatorio has also maintained its policy to recognise at cost, equity investments which do not have a maturity date. This is not in line with IAS 39 which states that “*The best evidence of fair value is quoted prices in an active market*”.

### ***Presentation of Accounts***

The same presentation of accounts as per previous years has been retained. This is not in accordance to the format required as per IAS and does not include the Cash Flow Statement and the Statement of Changes in Equity.

### **Management Comments**

#### ***Limited Funds used for Welfare Assistance***

Management strongly objected to NAO’s comments under this caption, contending that it was not the remit of the Auditors to go into the Board’s policy decisions on how to use its funds as well as its autonomous powers of acting for the well-being of the homes’ residents.

#### ***Lack of Transparency in Procurement***

Whilst the Board agreed to the recommendation to issue a call for quotations, it was alleged that the particular items were very urgently needed. Furthermore, it was maintained that CVB is not a government entity, bound to follow public sector procurement procedures. It was also fully within BOT’s discretion to consider and accept what was being offered. It was further stated that the Trustees are strongly independently minded persons of integrity, and their decision in those particular circumstances saved CVB valuable time and funds, besides gaining excellent operating systems.

### ***Presentation of Accounts not in line with International Accounting Standards***

Management reiterated that it is not obliged to present accounts in line with IASs, but in accordance to the Accounting Policy Document, approved by BOT on 20 June 2011.

## Co-operatives Board

### Audit for Financial Years 2011, 2012 and 2013

#### Background

The Co-operatives Board was established by Article 3 of the Co-operative Societies Act, Chapter 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 responsible for Co-operative Societies, whose functions 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, obliges 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.

Compared to allocated funds of €71,250 in 2010, Government provided the Board with amounts of €38,000, €100,000 and €93,500 during the years 2011, 2012 and 2013, respectively.

#### Audit Scope

The scope of the audit was to ensure that the Financial Statements for the years ended 2011, 2012 and 2013 show a true and fair view of the financial position of the Co-operatives Board as at 31 December of the respective years, and of its financial performance and cash flows for the years then ended. Compliance with the Co-operative Societies Act, 2001, as well as the existence of adequate internal controls, was also ascertained.

#### Control Issues

##### *Lack of Evidence on the Selection Process of Service Providers*

The Board issued expressions of interest for the provision of legal services on a retainer basis. Although various parties had expressed their interest, no details were provided in relation to the terms of reference of the post, projected hours and retainer fees quoted by the applicants. The same issues were noted in the case of the selection of an accountant/auditor to provide vetting services on Co-operatives' Financial Statements submitted to the Board.

Since the basis on which these two service providers were selected was not clear, it could not be ascertained whether the most favourable rates were actually chosen. This may lead to

inappropriate decisions being taken, as well as possible misuse of public funds.

### ***Payments for Periods not covered by Agreement***

Instances were encountered whereby payments, totalling €4,222, were made by the Board to its appointed legal advisor, in relation to periods that were not covered by a contract for service between the two parties. To this effect, the correctness of these particular payments could not be verified.

### ***Unauthorised Professional Fees***

A one-time payment of €4,000 was issued on 6 October 2011 to one of then Board members, for carrying out additional administration work for the Co-operatives Board, during the period September to November 2011.

Although the Board minutes stated that an approval of this payment was to be sought from the then Parliamentary Secretary, such approval was not made available for audit purposes. Hence, it could not be verified whether the latter had been informed of this payment and whether it was actually authorised. Moreover, since the entire payment was made in October 2011, a considerable portion thereof was affected prior to the work actually carried out. Furthermore, payment should have been supported by either a fiscal receipt or a declaration that the individual was exempt from Value Added Tax (VAT) registration, but none were provided.

## **Compliance Issue**

### ***Non-compliance with Public Service Regulations***

The Board paid for expenses in relation to telephony expenses incurred by two former Board members, during the three years that were audited. No documentation was made available to confirm that the two officers in question were duly authorised to make use of a mobile phone at Government's expense.

Moreover, the maximum entitlement as laid down in the Public Service Management Code (PSMC) was exceeded by these officers, during the years under review, by a total of €1,433. To this effect, neither were the excess amounts refunded by the officers in question, nor was a specific approval for higher telephone expenditure obtained from the Permanent Secretary.

## **Recommendations**

### ***Control Issues***

#### ***Lack of Evidence on the Selection Process of Service Providers***

The selection of particular service providers is to be as transparent as possible, clearly indicating all the specific details and terms of reference of the post, as well as details on the proposed fees to be charged to the Board. Evaluation reports, listing down all the relevant details of each service provider expressing an interest in the post, are to be prepared in order to support decisions taken by the Board in this regard. This would ascertain that the most cost-beneficial option is chosen.

#### ***Payments for Periods not covered by Agreement***

The Board is to ensure that formal contractual arrangements with its service providers are always in place, clearly disclosing the terms and conditions of the contractual relationship between the parties involved. Payments to service providers are to be issued in accordance with the respective provisions of the agreement in force.

#### ***Unauthorised Professional Fees***

All payments are to be properly authorised and only issued after ensuring that the service has been satisfactorily delivered. Moreover, all payments are to be adequately supported by the appropriate fiscal documentation, in accordance with VAT legislation.

## **Compliance Issue**

### **Non-compliance with Public Service Regulations**

The Board is to ensure that the use of mobile telephony at Government's expense is properly authorised and that the threshold laid out in PSMC is not exceeded. This would assist the Board in maintaining control over its telephone expenses. All payments made in excess of the limit imposed by PSMC are to be authorised by the respective Permanent Secretary if deemed justified; otherwise, they are to be refunded by the officer in question.

### **Management Comments**

*In its reply, the Board remarked that "... the present Board Members were appointed with effect from 16 June 2013 and therefore can only provide clarifications for any points raised which are the direct result of decisions taken from this date onwards. In relation to any other issues raised, the explanations provided hereunder are limited to information that could be sourced from documented minutes of the meetings of previous Board Members and any other available documents".*

The Board also provided the following comments:

### **Payments for Periods not covered by Agreement**

The Board alleged that one of the reasons for the absence of an agreement was that there was a break in service provided by the legal advisor. One particular payment of €874 was processed prior to the current Board members' appointment, thus could not be commented upon by the Board.

### **Non-compliance with Public Service Regulations**

With regards to telephony service, the Board stated that it was Management's decision to replace one of the landlines with a mobile line, as it was estimated to result in cheaper telephony calls. The Board also confirmed that it could not trace any approvals from the Permanent Secretary for the payment of the bills that exceeded the threshold specified in PSMC. Management is also committed not to exceed the stipulated threshold established for expenditure on mobile calls.

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