



Management Report for Financial Statements ended 30 June 2010 and 30 June 2011

Aid Management Division (AMD) Ministry of Finance & Economic Management

To:

Jim Armistead, Aid Manager

Distribution List:

Hon Henry Puna, Prime Minister
Hon Tom Marsters, Deputy Prime Minister
Hon Mark Brown, Minister for Finance and Audit
Richard Neves, Financial Secretary
Navy Epati, PSC Commissioner
Marie Francis, Chairperson of PERC

Date of Report: 14 December 2011

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1 Introduction

This report has been prepared to present to the management of the Aid Management Division. The report details the anomalies emerging from our audit procedures conducted on the systems and processes underlying the significant balances and transactions reported through the 30 June 2010 and 30 June 2011 financial statements. This report provides a summary of:

- our audit opinion, and
- the significant issues arising from the audit.

The matters raised in this report are only those which came to our attention during the course of our audit and are not necessarily a comprehensive statement of all the weaknesses that exist or all improvements that might be made.

You will appreciate that while our audit is carried out in accordance with New Zealand Auditing Standards, it cannot, and should not, be relied upon to detect every instance of misstatement, fraud, irregularity or inefficiency.

Management is responsible for implementing an internal control structure to maintain the reliability of the financial statements, safeguard assets and to mitigate risks in the entity. Because of the test nature and other limitations of an audit, it cannot provide an absolute assurance that there are no misstatements whether arising from fraud or error.

We must emphasise that:

- we did not examine internal controls other than to the extent necessary to determine the nature, extent and timing of our audit procedures;
- this report does not include all matters that came to our attention, but only those we regard as sufficiently important that they require management's attention;
- except as specifically stated, this report covers only the period of the financial statements and will not be updated to take into account any subsequent information or circumstances unless we are requested to do so.

AUDIT OPINION

We have issued an unqualified opinion on the Aid Management Division's financial statements for the 30 June 2010 financial year.

We have issued an unqualified opinion on the Aid Management Division's financial statements for the 30 June 2011 financial year.

2 Audit Findings

Following the recommendations contained in previous audit reports, AMD recruited the services of consultant Elizabeth Tommy in May 2011 to assist with the preparation of financial statements and improve the internal controls, financial records and financial reporting systems around donor aid funds managed by AMD.

The financial statements and supporting audit documentation submitted for audit of the 2010 and 2011 financial years continued the improvements highlighted in our 2009 management report.

We commend AMD for the initiative in implementing the improvement project which has successfully resulted in an unqualified audit opinion for the 2010 and 2011 financial years.

The Audit Office encourages AMD to ensure the improved internal controls and reporting processes are embedded in the division and that appropriate transfer of knowledge and skill has taken place to ensure that following the completion of the project, the current standard of financial reporting is maintained.

The Audit office would like to thank the division staff for the assistance provided during the course of the audit

2.1 Donor Confirmations

Audit Findings

To ensure that all Aid funds intended for the Cook Islands Government are actually received and accurately recorded in Cook Island Government financial statements, a comparison is made to an independent confirmation from the donor of actual amounts funded. This important control also verifies the completeness of donor revenue received.

The importance of regular reconciliation of funds received to donor confirmations was further highlighted by the discovery, by AMD, of a USD 22,251 deposit that was erroneously paid into an unknown bank account by the UNDP on 2 December 2008. The error was only discovered when AMD received a donor confirmation from UNDP in 2011. Although the funds were recovered on 5 October 2011 this highlights the importance of regular reconciliation to donor confirmations.

Risk Level	High
Recommendation	AMD ensures that Donor confirmations are received for all donors in future.
Ministry / Head of Ministry Response	

2.2 Cut off considerations - IPSAS 23 Revenue from Non-Exchange Transactions

Audit Findings

AMD receives the majority of its funding on a monthly basis from NZAID for specific projects that have been approved for completion. Currently, an asset and a corresponding liability is recognised when the cash is received and revenue is recognised when the funding is actually spent.

The subsequent release of the liability to revenue in accordance with IPSAS 23 should occur as the obligations under the funding agreement are fulfilled. AMD therefore correctly recognise revenue as the funding is spent on the project. However, consideration should be given to situations when spending does

not equate to the fulfilment of the obligations under the funding arrangement. In which case, despite funds having been spent, the liability would not necessarily be extinguished.

Conversely, AMD should consider if at year end a project has been completed (i.e. obligations under the funding agreement have been fulfilled) but all suppliers have not yet been paid. In terms of the current accounting treatment, the project liability will remain until all suppliers have been paid. However, if at year end the project is complete as envisaged by the funding agreement, AMD has no aid liability but rather normal accounts payable to the suppliers.

As discussed earlier, these scenarios relate specifically to cut-off procedures and would only need to be considered at year end. We identified certain instance at 30 June 2011 where payables to specific suppliers were incorrectly recorded as aid liabilities. These classification errors were subsequently corrected.

Risk Level	High
Recommendation	At year end AMD should consider the liabilities recognised and determine whether there is a performance obligation outstanding on the project to ensure the recognition of a liability is in accordance with IPSAS 23. If there is no further performance obligation then revenue should be recognised.
Ministry / Head of Ministry Response	

2.3 EU Bank Accounts

Audit Findings

Two new bank accounts, opened on the 27 August 2009 and on the 14 February 2011, were set up for administration of EU funded projects. We understand that when these projects were initiated, the Ministry of Foreign Affairs and Immigration was responsible for their administration and management and that AMD took over responsibility for these funds and related bank accounts as at 30 June 2010. It was only after the financial statements were submitted for audit that the consultant identified these bank accounts, related revenue and expenditure and liability balances had not been recorded in AMD consolidated financial records.

We question why the project manager did not report this project through the finance division and why overall financial management and control was maintained independent of the finance division. This matter, although identified and subsequently recorded in the financial statements, highlights a larger issue surrounding the overall financial management control environment within the AMD.

Risk Level	High
Recommendation	AMD management ensure that all bank accounts and funds that are administered through the division and for which they are responsible are submitted via the finance division and included in the consolidated financial statements.
Ministry / Head of Ministry Response	

2.4 Aid Expenditure

Audit Findings

Audit performed tests on a sample of expense vouchers from the general ledger and traced these payments to supporting documents to determine that;

- Payments were properly authorised;
- Appropriate and original supporting documentation was attached to each payment voucher;
- The payment was reasonable and the purchase was in relation to the nature of the project;
- Expenses were correctly classified and coded; and
- Payment vouchers were appropriately filed.

We found

- \$138,221 of expenditure tested in the 30 June 2011 financial year could not be verified to original supporting documentation and
- \$40,117 of expenditure tested in the 30 June 2011 financial year was not appropriately authorised. Payments should be appropriately authorised, evidenced by signature and date, by the AMD manager prior to payment.

Risk Level	Low
Recommendation	All payment vouchers should bear the original signature of the AMD Manager, or someone of an appropriate senior level, after being endorsed for payment by the respective project officers
Ministry / Head of Ministry Response	

3 Conclusion

I would like to thank you and your staff for the assistance received during the audit.

The Public Expenditure Review Committee and Audit (PERCA) Act 1995-96, Section 32, paragraph 2, requires you to reply in writing within **14 days** to report your planned action to implement the recommendations contained in this report. Accordingly, we look forward to receiving your comments by 28 December 2011. Forward all responses to:

The Director of Audit
PO Box 659
Avarua
Rarotonga
Fax: (682) 25 231
Email: perca@auditoffice.gov.ck

To conclude, the Cook Islands Audit Office is always looking at ways of improving our service and would appreciate any feedback you and your staff may wish to make. Please ensure that you complete and return the client survey questionnaire upon the completion of this audit.

Yours sincerely



Allen Parker
Director of Audit.

4 Definitions – Audit Opinion and Risk Rating

The definitions used to rate the risks of audit issues has been adopted from the Cook Islands Audit Office's risk criteria.

Risk Rating	Definition
High	Potential for unfavourable or noticeable negative impact on the organisation's objectives, income, expenditure, human resources and/or reputation. Management attention is required to ensure that the risk is managed in line with the organisation's objectives.
Medium	Potential for unfavourable or negative impact on the organisation's objectives, income, expenditure, human resources and/or reputation. Management needs to establish controls to address risk identified.
Low	Potential minor impact on the organisation's objectives, income, expenditure, human resources and/or reputation. Management needs to identify if there is a cost benefit in establishing increased controls.

Audit Opinion	Definition
Unqualified	An unqualified opinion is expressed when the auditor is satisfied in all material respects with the matters on which an overall conclusion is required to be drawn.
Qualified	<p>A qualified opinion is expressed when either of the following circumstances exists:</p> <p>(a) there is a limitation on the scope of the auditor's examination; or</p> <p>(b) the auditor disagrees with the treatment or disclosure of a matter in the written assertion or set of assertions; and, in the auditor's judgement, the effect of the matter is or may be material.</p> <p>In order of severity (most to least), qualified audit opinions may take the following form:</p> <ul style="list-style-type: none"> • Disclaimer – expressed when there is a limitation on the auditor's work as a result of the lack of audit evidence • Adverse – expressed when the results of a disagreement with management or a conflict between applicable financial reporting frameworks is significant and pervasive • Except For – expressed when an unqualified opinion is inappropriate because of a disagreement with management or a conflict between applicable financial reporting frameworks is not so significant and pervasive