CAYMAN ISLANDS

REPORT OF
THE AUDITOR GENERAL

on the

Financial Statements of the
Government of the Cayman Islands
for the year ended 31 December 1996

Cayman Islands Audit Office, 31 July 1997

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CAYMAN ISLANDS

REPORT OF THE AUDITOR GENERAL FOR THE YEAR ENDED 31 DECEMBER 1996

Introduction

In accordance with the provisions of Section 43 (1)(b) of the Public Finance and Audit Law (1997 Revision), this Report is submitted to the Presiding Officer of the Legislative Assembly of the Cayman Islands. This report concerns my examination and certification of the financial statements of the Government of the Cayman Islands for the year ended 31 December 1996, and other such matters which relate to the performance of my duties and the exercise of my powers under the Public Finance and Audit Law (1997 Revision). The Report has been agreed with the appropriate Government authorities to be a fair summary of all relevant facts concerned with the various issues raised. This Report, together with the financial statements of the Government, will now be considered by the Public Accounts Committee of the Legislative Assembly in accordance with Standing Orders (Revised). After the deliberations of the Public Accounts Committee, this Report, the certified financial statements and the Report of the Public Accounts Committee shall then be laid before the Legislative Assembly and submitted to the Secretary of State in accordance with Section 43 (2) of the Public Finance and Audit Law (1997 Revision).

PART I

Financial Statements of the Cayman Islands Government for the Year Ended 31 December 1996

1.1 The Government's financial statements comprising:

the Statement of Receipts and Payments
the Surplus and Deficit Account
the Statement of Movement of the General Reserve
the Statement of Assets and Liabilities
the Statement of Public Debt; and
the accompanying Notes and Appendices

were transmitted to me duly signed and approved by the Accountant General on 30 April 1997. I completed my audit and certified the financial statements and accompanying notes and appendices on 31 July 1997. The certified financial statements were then transmitted to the Presiding Officer of the Legislative Assembly of the Cayman Islands, together with this Report in respect of my examination of the financial statements and on other matters relating to my duties and the exercise of my statutory powers in accordance with the requirements of Section 43 (1)(b) of the Public Finance and Audit Law (1997 Revision).

Audit Opinion

Overseas Medical Expenses

1.2 I have qualified my audit opinion on the 1996 financial statements because I consider the accounting policy for overseas medical advances is inappropriate. Overseas medical expenditure is not brought to account at the date of payment, but is classified as a recoverable advance. Amounts accumulated in the advance account tend to be brought to account infrequently, usually accompanied by conversion of individual debts to long term loans. The effect of this accounting policy, which has been followed for many years, is to defer recognition of expenditure to future periods. In my opinion, the accounting treatment understates recurrent expenditure and materially overstates both the assets and the accumulated surplus reported in the annual Statement of Assets and Liabilities. At 31 December 1996 42% of the total assets reported in the financial statements consisted of overseas medical advances. I drew attention to this situation in both my 1993 and 1994 Reports and warned that the annual financial statements were being distorted. I qualified my opinion on Government's 1995 financial statements because accumulated overseas medical expenses charged to advances had reached $7,721,834. During 1996 seven advances amounting to $161,043 were expensed and were subsequently written off, as part of a write off totaling $614,363 authorised by the Legislative Assembly in December 1996. New medical advances increased by $2,271,789 during 1996 and the balance outstanding amounted to $9,832,580 at 31 December 1996:

	$
Balance 1 January 1996	7,721,834
Less: Expensed and written off	(161,043)
Plus: New advances (net)	2,271,789
Balance 31 December 1996	9,832,580

In the opinion of the Audit Office, many of these medical advances will prove to be irrecoverable in the long term.

1.3 With effect from 1997, responsibility for the management of all overseas medical accounts was transferred to the Director of Health Services. In May 1997 the Financial Secretary formed a small working group to address the accounting and debt recovery issues. It has been proposed that all advances classified as recoverable within one year will remain as advance accounts. The remainder will be expensed and either converted to long term loans, transferred to a dormant account or written off. At the date of preparing this report, management had not established the number and value of advances existing at 31 December 1996 which would be brought to account under the revised accounting treatment.

1.4 With the exception of the accounting policy issues disclosed in paragraph **1.2** and excess expenditure of $5,600, disclosed in paragraph **1.5** below, in my opinion the financial statements properly present the receipts and payments of the Cayman Islands Government for the year ended 31 December 1996.

Excess Expenditure

1.5 For fiscal 1996, only one excess and unauthorised expenditure was recorded. Prison overspent Head 07 by $5,600, some 0.14% of authorised budget.

	$	
Estimated:	3,969,345	
Actual:	3,974,945	
Excess:	5,600	(0.14%)

Explanation

Excess expenditure occurred under the personal emoluments ($20,704), travelling and subsistence ($4,039) and grants, contributions and subsidies ($20,866) sub-heads. The excesses were partially offset by savings in the supplies & materials and utilities subheads. The Department has pointed out that it requested a supplementary estimate of $50,000 for additional overtime to cover staff shortages, sick leave and hospitalisation of inmates. The request was reviewed by the Portfolio of Finance and Development, who decided that the Prison had sufficient funds to cover overtime up to 31 December. The supplementary request was therefore not placed on the agenda for Finance Committee. Two virement applications submitted by the Prison were also not approved by the Portfolio of Finance and Development.

Financial Highlights for Fiscal 1996

1.6 It will be seen from **Figure 1.1** that Government recorded a surplus of $11,902,298 on the Receipts and Payments Account for 1996, after crediting loan income of $22,381,287. This is significantly better than the original budget announced in November 1995 which proposed a deficit of $1,119,422. Highlights for fiscal 1996 are summarised below.

- The original budgeted expenditure of $202.702 million was increased by $23.669 million of supplementary approvals during the year ($7.533 million recurrent and $16.136 million capital). Despite the magnitude of supplementaries and an expanded capital budget, total expenditure was only $2.939 million (1.4%) above the original budget.

- Recurrent revenue totalled $195.162 million, some $10.584 million (5.7%) above the original estimate and $20.675 million (11.8%) more than 1995. Part of the strong revenue performance is in line with general economic conditions, but part is also attributable to greater efforts by Controlling Officers and to more effective debt collection by the Treasury. There were no revenue enhancement measures in 1996.

- With the exception of Prison Department, all Heads of expenditure remained within final approved estimate.

- New loans of US$33.820 million (CI$28.183 million) were arranged during the year, of which CI$22.930 million cash was drawn down to finance approved capital projects. Total loan proceeds

Figure 1.1: Budget Estimate and Out-turn for the Year Ended 31st December 1996

	Original Estimate 1996 $m	Approved Estimate 1996 $m	Actual 1996 $m	Actual 1995 $m	Increase 1996 %
RECURRENT REVENUE					
Local	**184.578**	**184.578**	**195.162**	**174.487**	11.8
EXPENDITURE					
Statutory	14.604	14.604	14.827	19.726	
Recurrent	160.045	167.578	156.723	138.430	13.2
Sub-total	174.649	182.182	171.550	158.156	
Capital	28.053	44.189	34.091	23.701	43.8
TOTAL EXPENDITURE	**202.702**	**226.371**	**205.641**	**181.857**	13.1
SURPLUS / (DEFICIT)	**(18.124)**	**(41.793)**	**(10.479)**	**(7.370)**	
FINANCED BY					
Local Loan	17.004	27.689	22.381	1.772	
ABOVE LINE CASH FLOW	**(1.120)**	**(14.104)**	**11.902**	**(5.598)**	
Cash Movements Below the Line					
(Increase)/ Decrease in Imprests			(0.019)	(0.116)	
Increase / (Decrease) in Deposits			1.635	(1.254)	
(Increase) / Decrease in Advances			(1.083)	(2.526)	
BELOW LINE CASH FLOW			**0.533**	**(3.896)**	
NET CASH FLOW FOR YEAR			**12.435**	**(9.494)**	
MOVEMENTS IN RESERVES					
General Reserve			(3.000)	-	
Housing Reserve			0.186	-	
CASH BALANCES					
Beginning of Year			(6.134)	3.360	
End of Year			**3.487**	**(6.134)**	
TOTAL ASSETS & LIABILITIES			23.178	16.744	

credited to Revenue amounted to CI$22.381 million, compared to a final approved estimate of CI$27.689 million.

- Bank accounts at 31 December 1996 amounted to $3.487 million net. The overdraft limit of $4.5 million was not exceeded during the year.

- An amount of $3 million was transferred from the Surplus and Deficit Account to the General Reserve, which stood at $7,576,587 at 31 December 1996. Total Reserves at 31 December 1996 increased from $1.245 million to $13.524 million, including a separate Housing Reserve Fund of $185,523.

Compliance Issues

1.7 The Public Finance and Audit Law requires the Auditor General to satisfy himself, that:

- all issues and payments of public moneys were made in accordance with proper authority; and
- public moneys appropriated by the Legislative Assembly for a specified purpose were expended in the due application of that purpose.

Several departures from these principles were noted during the course of the audit.

Head 39-110: Government Pension Contribution - $2,366,191

1.8 In July 1996 the Legislative Assembly approved an increase in the employer's contribution from 4% to 6% of salary (section 3(b), the Pensions (Amendment) Law, 1996). It was intended that the increased contribution would take effect in January 1996. The increase was implemented immediately. Arrears were collected from government ($387,822) and from statutory authorities ($33,959) covering the period January to June 1996 and were paid over to the Fund. Unfortunately there was a drafting error, which meant that the amending legislation took effect in July 1996 instead of January 1996. This issue is being actively pursued by the Portfolio of Finance and Economic Development and will be resolved imminently. The Audit Office therefore concluded that there was no proper authority covering payment of the additional 2% employer's contribution ($387,822) from subhead 39-110. The Audit Office considers this to be a minor infringement, which will be regularised during 1997.

Use of Contingency Warrants

1.9 The Financial Secretary may authorise the use of Contingency Warrants where he is satisfied that, due to exceptional circumstances, an urgent need has arisen for payment to meet expenditure, for which no provision or insufficient provision is shown in the approved estimates, and which cannot be deferred without detriment to the public interest. Consistent with our parliamentary system of government, the generally accepted convention is that use of the contingency warrants should always be regarded as exceptional, especially for a new service. It is always preferable to wait for prior legislative approval of the relevant supplementary estimate, since only the Legislative Assembly can authorise a new or additional appropriation of funds.

1.10 The use of Contingency Warrants increased noticeably during 1995 and 1996.

		Recurrent		*Capital*		*Total*
1995	47	$3,408,230	49	$4,447,818	96	$7,856,048
1996	67	$4,561,704	58	$6,079,413	125	$10,641,117

It appears to the Audit Office that many of the Contingency Warrants issued do not arise as a result of exceptional circumstances or an urgent need to make payments, which cannot be deferred without detriment to the public interest. Many contingencies are really requests for supplementary funds to cover new or additional operating expenses or capital projects, some of which are already in progress. Part of the problem is a lack of financial flexibility. As virement of funds is not permitted between capital and recurrent expenditure, or between personal emoluments and other recurrent expenditures, Controlling Officers are obligated to seek authority for comparatively minor variations in expenditure. In many cases, savings cover the cost of the variation and there is therefore no additional expenditure involved. Nevertheless, the Audit Office **recommends** that future use of Contingency Warrants should comply with the requirements of the Public Finance and Audit Law.

Uncleared Contingency Warrants

1.11 All appropriations and warrants issued under the Public Finance and Audit Law lapse at the end of the financial year. Three Contingency Warrants totalling $572,253 issued in 1996 were not cleared by the year-end **(Figure 1.2)**. The expenditure has not been brought to account and is included within the deferred expenditure total shown in Advance Accounts.

Figure 1.2: Contingency Warrants Outstanding

Reference	*Date Issued*	*Purpose*	*Balance at 31 Dec 1996* $	*Balance at 30 June 1997* $
CW 51/96	14 August 1996	Pedro Castle	567,647	Nil
CW15/96	29 March 1996	Purchase of Office Furniture	4,356	4,356
CW 77/96	14 October 1996	Purchase of a stool	250	250
			572,253	**4,606**

1.12 The accounting for Pedro Castle expenditure deserves some explanation. An amount of $1,000,000 was originally included for this project in the approved estimates for 1996. During 1996, the Government concluded a loan agreement for US$5.790 million with the Caribbean Development Bank to finance the major portion of this project. The Legislative Assembly passed a law authorising the new source of funds. In accordance with internal accounting conventions, it then became necessary to obtain legislative approval to create a new expenditure classification under Head 53 – External Loan. A Contingency Warrant was issued to enable the Ministry to make payments to suppliers and contractors, so that the project could proceed in an orderly manner. Due to an oversight, the expenditure classification variation was not included in the agenda for the December 1996 meeting of Finance Committee. As a result, expenditure of $567,647 and matching loan revenue of $557,311 were held below-the-line as at 31 December 1996. The transactions have since been brought to account in the 1997 year of account.

Misclassification of Expenditure

1.13 The exclusive right to authorise public expenditure is vested solely with the Legislative Assembly. Government proposes a detailed budget in the form of annual estimates, which are submitted to legislators for debate and approval. Controlling Officers are not allowed to vary or change the pattern of approved spending, or to incur expenditure which is not covered by the budget, without the prior approval of the legislature. It follows, therefore, that expenditure should be charged against the appropriate subhead. The Auditor General has a duty to ensure that public moneys appropriated by the Legislative Assembly for a specified purpose have been spent in the due application of that purpose. In order to allow some degree of flexibility the Financial Secretary has discretionary powers to vary budgets between subheads (“virement”). By convention, virement is not permitted between personal emoluments and other expenditure, nor between capital and recurrent expenditure. Virements should be ratified quarterly by Finance Committee.

1.14 In late 1996, the Audit Office became aware that certain expenditures had been misclassified and posted to inappropriate votes. It was decided to conduct a cross-departmental study to assess the extent of expenditure misclassification. Due to the volume of transactions and other commitments, we were able to examine only 25 out of the 35 Heads of recurrent expenditure and part of the capital programme. The results of the audit demonstrated that there appears to be quite widespread disregard of financial regulations. We concluded that, in certain departments, expenditure misclassifications are significant in terms of both number and value. Whilst misclassifications do not alter the annual surplus or deficit reported, legislators may well be misled because expenditure is not being reported accurately in the Receipts and Payments Account and in Appendices IV, V and VI of the annual accounts. Audit established that misclassifications had occurred in 19 of the 25 Heads examined. Some of the more noteworthy examples are summarised in Appendix A. Audit review and discussion with accounting staff established a number of reasons why misclassifications had occurred.

- Undetected error. These seem to be relatively few in number.

- Certain expenditure may be incurred legitimately, but the spending does not fit easily with the description of existing subheads.

- Insufficient funds are available in the correct vote. Management knowingly misclassifies expenditure to another underspent subhead.

- Expenditure classification is consistent with its underlying purpose. Some Controlling Officers feel there are justifiable circumstances when expenditure need not be classified by type. For example, a photocopier and computer equipment were charged to the Construction of Roads capital vote, because the equipment was intended to be used by the roads department. Another Department acquired computer equipment and charged it to collateral and photography. The Audit Office does not agree with this approach. Budgets are presented to, and approved by, legislators primarily on the basis of expenditure type. Legislators reasonably expect Controlling Officers to operate within the ambits of subheads. It is expected that expenditure reports are prepared on a basis consistent with the annual estimates. The causal factor approach seems to be a convenient way of dealing with situations which result from inadequate planning or disclosure to the Legislative Assembly.

- In some cases, there appears to be willful disregard of the ambit of the subhead. It is difficult to avoid reaching the conclusion that Controlling Officers incur expenditure which was never contemplated or approved by legislators. In some cases, there appear to be deliberate attempts to conceal the real nature of expenditure, especially in areas where legislators are known to have concerns (e.g. computer acquisition and travel).

1.15 Many Controlling Officers complain of a lack of flexibility in our financial system. This argument is valid. The existing system of Supply incorporates well established checks and balances which are designed to provide the Legislative Branch with oversight and control of how the Executive spends public money. Central to this are annual expenditure limits by both amount and purpose. Any plan to increase Controlling Officers' flexibility, or spending discretion, must be balanced with the need for an appropriate level of authorisation and control by legislators. Against this background, examples of expenditure misallocation are all the more worrying. One of the concerns of the Audit Office is that greater flexibility or financial freedom may increase the risk of misallocation, or even inappropriate or unnecessary expenditure. Other Controlling Officers may not agree with this view. Increased managerial flexibility should be accompanied by a greater awareness of accountability and improved reporting to the legislature.

Virements

1.16 In order to allow some degree of flexibility, the Financial Secretary has delegated powers to reallocate declared savings on one subhead to cover additional requirements on another subhead of the same Head. This procedure, known as virement, requires ratification by Finance Committee on a quarterly basis. During the audit of the 1996 accounts the Audit Office noted a number of differences between the "Approved Estimate" figures in the published accounts and the final revised amounts authorised by Finance Committee. The differences may be classified into four categories (three relating to capital and one to recurrent). Most of the capital virements involve a change in the source of financing from local revenue to local loan.

- Virements were approved by the Financial Secretary and posted by Treasury, but were inadvertently omitted from the Finance Committee agenda.

		$
41-101	Computer Equipment	10,000
51-109	Agricultural Development	(198,117)
51-120	Purchase of Lands	(200,000)
52-109	Agricultural Development	188,117
52-120	Purchase of Lands	200,000

At a meeting between representatives of Treasury, Finance and Audit it was agreed that the virements should stand, as it would be unfair to penalise Departments who acted in good faith. The virements will be tabled at the next meeting of Finance Committee for ratification.

- The Budget and Management Unit notified Treasury of a classification error. The correction, outlined below, was posted by Treasury but Finance Committee was not informed of the adjustment.

		$
41-135	Medical Equipment	77,500
42-135	Medical Equipment	(77,500)

It was agreed that the adjustment would stand and that Finance Committee ratification would be obtained in 1997.

- Virement authorised by Finance Committee but insufficient funds in subhead

		$
41-101	Computer Equipment	(2,000)
41-126	Office Equipment	2,000
41-126	Office Equipment	(4,220)
41-101	Computer Equipment	4,220
51-123	Sports Centres and Parks	(30,000)
51-120	Purchase of Lands	30,000

It was agreed that these virements could not be processed and the Finance Committee ratification would be ignored.

- Recurrent virements approved by the Financial Secretary but not included on the Finance Committee agenda and therefore not approved by Finance Committee. The Heads involved are: 08 Personnel ($10); 13 Portfolio of Finance and Development ($161,487 – 3 virements); 16 General Registry and Shipping ($1,600); 21 Tourism ($45,000 – 2 virements); 23 Social Services ($35,757 – 2 virements); 26 Health Services ($5,000); 30 Lands & Survey ($5,354) and 35 Education ($1,600 – 3 virements). Following internal discussions, it was agreed that the virements would stand for the 1996 accounts and that Finance Committee's ratification would be obtained during 1997. The transactions in question do not affect the net surplus or the overall final approved estimate figure for each Head in the annual accounts.

All "Approved Estimate" figures for each Head are correctly stated and comply with total expenditure authorised by the Legislative Assembly. Variations exist between subheads of certain Heads in Appendices IV and VI of the financial statements. Subject to these foregoing remarks, the Receipts and

Payments Account and Appendices II to VI accurately reflect the amounts approved by the Legislative Assembly.

General Reserve

1.17 The General Reserve amounted to $7,576,587 as at 31 December 1996, an increase of $3,190,753 on year-end 1995. Finance Committee authorised transfer of $3 million to General Reserve in September 1996.

Housing Reserve

1.18 In June 1994 Finance Committee approved the creation of a Housing Reserve Fund for a maximum of approximately $1.1 million. The purpose of the Fund is to cover any default which may arise out of government guarantees provided under the Low Income Housing Scheme. It is estimated that Government exposure through the issue of guarantees over the life of the scheme will be approximately $7.6 million. The Reserve Fund has been established at 15% of the exposure outstanding and will be adjusted at the end of each financial year. At 31 December 1996 government guarantees amounted to $1,236,821. A reserve of 15% of this amount ($185,523) has been transferred from subhead 17 Repayments and Reserves to a Treasury deposit account. The Audit Office **recommends** that the Fund be segregated in a separate bank account. To date, there have been no known claims under the guarantee scheme.

Public Debt

General Guidance on Definition and Disclosure of Public Debt

1.19 Regular disclosure of public debt can reveal whether debt levels have been kept within a country's ability to support them and can help ensure that potential problems are visible. Disclosure may also provide the impetus to address problems before they become crises. One of the most challenging issues is how to make public debt more understandable, and thus relevant to the reasonably informed, but non-expert, reader. The Public Debt Committee of the International Organisation of Supreme Audit

Institutions (INTOSAI) has recently provided guidance on this issue[1]. The Committee has recommended that national audit offices should encourage the use of generally accepted ways of bringing these large numbers to life for taxpayers.

1.20 INTOSAI recognises that the scope of financial reports on public debt and the nature or type of liabilities shown will vary according to the purposes for which reports are prepared. Different definitions of public debt are used for different purposes, and there are many variations in scope between the resulting types of reports. By convention, in the financial statements of the Cayman Islands Government, public debt is defined as loans borrowed by government and applied to central government sponsored projects. Debt incurred by government and on lent to Statutory Authorities is defined as self-financing loans, on the basis that recipients service the debt from their own internally generated funds. There are at least two other categories of public debt, which ought to be recognised as public debt: these are additional borrowing by statutory authorities and state owned enterprises. This type of debt is often guaranteed by Government and is disclosed as a contingent liability in the annual financial statements. In the opinion of the Audit Office, these categories should be recognised within the wider definition of public debt as they are relevant in formulating any debt limitation policy. Ignoring these latter debt categories can result in short term distortions of public debt. For example, in 1995 the Water Authority refinanced part of a Caribbean Development Bank loan in order to eliminate exchange rate risk. This involved replacing a self-financing loan with a government guaranteed loan, which, by convention, is disclosed as a contingent liability in government's financial statements. Government can also create new non-departmental public bodies to manage specific investments or development projects. In these instances, the debt is usually classed as a self-financing loan. Recent examples include the former Health Services Authority and the Tourist Attractions Board.

1.21 The Audit Office considers that understanding of public debt could be improved if all relevant data was consolidated in Government's annual financial statements. This would help the non-expert reader gain a better overall view. Debt could be disclosed under four separate headings:

I: Debt incurred by government direct (comprising long term loans and vendor financing, but excluding overdrafts);
IIA: Debt incurred by government on behalf of Statutory Authorities (i.e. self-financing loans);
IIB: Debt incurred by statutory bodies direct, usually supported by a government guarantee;
III: Debt incurred by state owned enterprises (i.e. Cayman Airways Ltd) including capital leases.

[1] "Guidance on Definition and Disclosure of Public Debt", INTOSAI Public Debt Committee, 1997.

The Audit Office has provided this information at **Figure 1.3,** together with debt service costs for central Government direct borrowing and self-financing loans.

1.22 INTOSAI has recommended four simple indicators of a government's overall financial condition. These are:

- **The Debt to GDP Ratio** is the percentage of government debt to the country's Gross Domestic Product. If the percentage increases year after year, it means that debt is growing faster than the economy. If this trend were to continue over the long term, it could eventually lead to burdensome and perhaps unaffordable debt loads.

- **The Interest Bite** is the percentage of interest costs on borrowed funds to government revenues. It is somewhat comparable to a percentage used by mortgage lenders in determining whether or not an individual can afford to carry increased debt.

Figure 1.3: Public Debt

	1996	*1995*
	$	*$*
Debt Category		
IA: Central Government – long term loans	50,108,692	33,241,188
IB: Central Government – vendor financing	1,595,022	1,268,116
IIA: Statutory Bodies - self-financing loans	17,484,617	18,320,862
IIB: Statutory Bodies – direct borrowing	23,242,522	22,930,321
III: State Owned Enterprises	3,226,667	3,516,667
Total Public Debt	**95,657,520**	**79,277,154**
Central Government Debt Service Costs		
Principal	5,550,478	4,983,277
Interest	2,264,910	2,592,184
Total Debt Service Cost	**7,815,388**	**7,575,461**
New Loans Drawn Down		
Central Government	22,372,237	1,200,000
Self Financing		
Via General Revenue	557,311	Nil
Direct	92,842	292,132
Vendor Financing	653,323	Nil
Total New Loans	**23,675,713**	**1,492,132**

- **The Expenditure Ratio** is the percentage of total government spending to total government revenue. If this percentage is consistently greater than 100, the revenue shortfall is likely to be made up by additional borrowing which, over time, could lead to financial problems unless corrective action is taken.

- **The Tax Bite** is the percentage of tax revenues to gross domestic product (GDP). If the tax bite increases year after year, it means that more of a country's production is being diverted to government and away from reinvestment in the private sector. Note that only part of government revenues are defined as tax revenues by the International Monetary Fund. The balance is classified as charges.

1.23 The level of public debt and the purposes for which funds are borrowed are policy matters, which go well beyond the mandate of the Audit Office. The Audit Office has prepared the indicators recommended by INTOSAI for the years 1990 through 1996 at **Figures 1.4.1 to 1.4.4.** We hope that this information will help interested individuals understand more clearly the significance of government debt and how Cayman Islands compares with other countries. We **recommend** this information should be updated annually and published, preferably as part of government's annual financial statements.

New Loans

1.24 New loans drawn down in 1996 comprised:

Loans for Central Government	*CI$*
Capital Projects Law, 1993	472,237
Capital Projects Law, 1995	14,700,000
Capital Projects Law, 1996	7,200,000
Self Financing Loans Accounted for Through Government Budget	
Pedro St James Heritage Project	557,311

In addition, Government also bought lands under vendor financing arrangements at a cost of $653,323. Vendor financed purchases are disclosed as a footnote to the Statement of Public Debt. Installment payments are made on the dates specified in individual agreements. The annual Statement of Receipts and Payments reflects the cost of installments falling due within a particular year.

Advance Accounts

1.25 Advances represent payments made by Government which have not been brought to account and included in the Statement of Receipts and Payments. Provided the advances are brought to account or are recovered within a reasonable period of time, the accounting treatment is acceptable. Advance Account balances increased by $1,083,045 to $11,361,475 as at 31 December 1996. The major part of advances are for overseas medical treatment (1996: $9,832,580 –86%). The Audit Office has expressed disagreement with the accounting treatment for overseas medical expenses and has qualified the audit opinion on the 1996 accounts. Comments on other major components of advances are provided below.

Dishonoured Cheques - $141,552

1.26 Overall there was a reduction of $36,249 on the balance on this account between 1995 and 1996. Some of the balances have remained dormant in this account for several years. The Audit Office reviewed all 36 balances over $1,000 and carried out an ageing analysis. This indicated that no action had been taken to pursue many of the older accounts outstanding.

	31 December 1996		*30 June 1997*	
1994	20 cases	$48,882	20 cases	$48,882
1995	8 cases	$26,140	8 cases	$11,140
1996	8 cases	$12,491	7 cases	$ 9,735

- 23 of the 36 balances selected had not been passed to the Treasury debt collector for legal action;
- Six of the accounts totalling $16,403 are either time barred or the debtor has gone out of business;
- Two mispostings occurred in 1996 or earlier, involving $19,014 collected but not credited to the debtor's account. The Advances Accounts balance at 31 December 1996 is overstated by this amount. One item had been incorrectly credited to revenue. The other entry could not be located.
- During the first six months of 1996 collections had been made for only three of the 36 accounts. Legal action was in process for two other accounts.

In terms of total government revenue the amount of returned cheques is not considered significant. The position has improved since 1995 and two large cases have been successfully settled. However further action is needed to ensure that all debtors are contacted by the debt collector as a matter of priority and appropriate legal action is taken wherever practical to recover these debts.

Deposit Accounts

Immigration Security Deposits

1.27 The 1995 Report of the Auditor General highlighted that $2,210,362 of immigration security deposits had been appropriated to General Revenue in 1991 and 1995. The Audit Office concluded that government should have waited five years after persons had left the Islands before contemplating any appropriation of unclaimed deposits. It was considered highly probable that the refund liability had been understated by a material amount, but this could not be quantified due to systems deficiencies.

1.28 Treasury Department completed an analysis of the deposit account in late 1996 and subsequently transferred responsibility for management of the account to Immigration Department. The Department can now make all refunds of security deposit to employers without having the transaction processed through Finance or Treasury Departments. This will help to improve the quality and speed of service in providing refunds to clients.

1.29 Refunds of security deposits are normally made from the deposit account. In cases where the deposit has been transferred to General Revenue, the refund is made from the Refund of Revenue subhead (17-016). A visual examination of the general ledger indicated that at least $41,000 had been paid out from the refund of revenue subhead in the 18 months between January 1996 and June 1997. The total amount could not be determined because of incomplete transaction descriptions for part of the period. Neither the Immigration Department nor the Portfolio of Finance and Economic Development, who controlled the refund subhead during 1996, were able to confirm how much had been paid out of General Revenue for deposit refunds. These findings lend support to the conclusion that the security deposit refund liability was understated as at both December 1995 and 1996.

1.30 Having taken advice from Computer Services Department, the Audit Office has concluded that it is not possible to calculate a precise refund liability from the Immigration Department's existing computer based records. System enhancements will be needed to provide a history of security deposits and refunds. A manual system does not seem to be practicable given the data volumes. Even with an effective computer system, Immigration Department will face a mammoth task of reviewing and collating data from over 30,000 manual files. There seems to be little prospect of a solution to the problem of calculating refund liability in 1997. The planned new integrated financial system may help. The difficulty in calculating a precise amount for the refund liability will not affect depositors' rights to receive refunds. Government will continue to honour all valid claims for deposit refunds.

Grants from the United Nations Development Programme (UNDP)

1.31 The United Nations Development Programme (UNDP) provides technical assistance to the Cayman Island Government for certain educational, training and technical projects. Individual government departments are responsible for managing UNDP funds and are accountable for all UNDP resources allocated to a project. Quarterly financial reports should be submitted to UNDP within 30 days after the end of each quarter. A financial year-end report, the Combined Delivery Report (CDR), is prepared by UNDP and transmitted to project managers. The CDR is a consolidation of all expenditure incurred. Project managers should verify and certify the CDR, which forms the basis for financial review. UNDP requires an independent audit of the CDR attesting to the propriety of disbursements and to project balances held by government. Financial accounting and audit arrangements for these projects have not operated within the normal government framework and accountability problems are now emerging.

Financial Accounting

1.32 The Audit Office has not been able to determine how much money has been received from the UNDP. Enquiries have been made direct with UNDP Jamaica regional office. We were able to establish that four projects are being funded, but UNDP had not provided details of funds transferred to the Cayman Islands Government at the date of presenting this report. Project receipts and payments are administered through advance and deposit accounts. Total receipts and payments are not known because transactions are never brought to account above-the-line in the Statement of Receipts and Payments. As a result, there is no public record of these projects. Amounts held in Deposit and Advance Accounts as at 31 December 1996 amounted to $168,294 and $19,856 respectively. These accounting arrangements contravene Section 4 of the Public Finance and Audit Law (1997 Revision), which mandates that all moneys raised or received for the purpose of Government should form part of general revenue. Financial regulations call for a separate Head of revenue for the receipt of grants, loans or funds from other overseas sources. There is also an implied requirement for prior legislative approval of project expenditures. This has never been sought. This situation was brought to the attention of the Portfolio of Finance and Development in late 1995. The Financial Secretary agreed that these transactions should be brought to account above the line for 1996. This was subsequently suspended on the basis that current projects would be completed in 1996. So far as can be ascertained UNDP funded activities are continuing as below-the-line activities.

Accountability

1.33 It is believed that at least four projects are currently supported by the UNDP. The Audit Office is not informed of projects approved for financial assistance, nor of amounts received from the UNDP. Audit and accountability arrangements are therefore reliant on submission of project accounting reports by management. Regrettably, sponsor departments pay scant attention to UNDP audit requirements and tend not to submit CDRs for audit on a timely basis. At the date of preparing this report it is understood that 11 CDRs were in arrears and had not been submitted for audit.

Project Title	*Sponsor*	*CDRs Overdue*
Socio-Economic and Demographic Data Collection for Planning & Development	Economics and Statistics	1995 & 1996
Public Sector Multi-Disciplinary Training	Personnel	1994 - 1996
Education Planning and Management	Education	1994 -1996
Technical Advisory Programme	Economics & Statistics	1994 -1996

The Audit Office receives periodic complaints from the UNDP that certified accounts are outstanding and overdue. Although we have reminded sponsors of their obligations, no action has been taken. There are obvious risks involved when departments are permitted to operate outside the normal accounts and audit framework. Persistent failure to comply with UNDP rules may also prejudice future assistance.

Statement of Contingent Liabilities

Public Service Pensions Liability

1.34 In February 1997 the Government-appointed actuary completed a valuation of public service pensions as at 1 January 1996. The liability was calculated to be $157.116 million. The previous liability reported as at 1 January 1993 was $65.001 million. However, the 1993 valuation did not include any allowance for future pay increases. Assuming pay increases of 5.5% per annum, the restated 1993 liability would have been $99.357 million. The comparable increase between 1993 and 1996 is therefore $57.759 million (58%). International Accounting Standards now require actuarial assumptions to incorporate projected salary increases to the date of retirement. Accordingly, the pension liability disclosed in Government's 1996 financial statements complies with best practice. Details of the liability and annual pensions funding costs are provided at **Figure 1.5.**

Figure 1.5: Public Service Pensions Liability

	1 January 1993	1 January1996
Number of active participants	1,508	1,652
Pension liability - no pay increases	$65,001,000	$114,331,000
Normal cost for year (1)	$5,501,000	$8,544,000
Normal cost as a percentage of pay	15.10%	18.30%
Amortisation of deficiency (over 20 years)	$8,789,000	$13,251,000
Amortisation as a percentage of pay	24.13%	28.38%
Total annual cost of benefits (2)	$14,290,000	$21,795,000
Total annual cost as a percentage of pay	39.23%	46.68%

(1) Normal cost is the cost of benefits earned during the current year with allowances for future pay projections.
(2) Total annual cost is the sum of the normal cost plus the amortisation of the actuarial deficiency as at 1 January 1996. The amortisation period selected is 20 years but a different period could be used.

1.35 Total assets of the Public Service Pensions Fund as at 31 December 1995 were $16.735 million, leaving a net deficiency of $140.381 million (net deficiency 1993: $93.112 million). The actuary has reported that the Fund continues to be severely under-funded with respect to benefit obligations as currently structured. This is to be expected since the Fund was established in 1990, whereas pension obligations have been building up for many years. The deficiency has increased significantly from 1993 for a number of reasons.

- **Inadequate contribution level** is the main reason for the increased liability. The actuary's 1993 valuation indicated a normal cost of 15.1% of salary and total annual costs, including amortisation of the past service liability over a 20 year period, at 39.23% of salary. Taking into account future new entrants, the actuary concluded that the long-term costs would be around 25% of pay in order to meet projected liabilities. However only 8% was contributed to the Fund for the years 1993 to 1995. The funding shortfall of this period is assessed to be :

  Based on a contribution rate of 15.1% for the *normal cost of benefits* - $7.573 million

  Based on a contribution rate of 25% for the *normal cost of benefits plus amortisation of the past service liability over 20 years* - $18.133 million.

- **Additional employees** have been included in the 1996 valuation, including elected Members of the Legislative Assembly. MLAs' pension contributions have been credited to the Fund since 1991, similar to the treatment for other monthly paid employees. MLAs' defined benefits scheme is separate from the scheme for permanent and pensionable civil servants.

- **Group Employees** There has been a continuing failure to collect contributions from all weekly paid ("Group") employees between 1991 and 1995, which has obviously reduced the assets of the Fund. This was rectified in 1996.

- **Retirement Age** The 1993 valuation was based on retirement at age 60 whereas the 1996 valuation assumes retirement at age 55. Employees in service before July 1980 can earn a full pension after 400 months (33 1/3 years). Employees who joined the service after July 1980 need to work for 40 years to be entitled to full pension benefits.

- **Investment Policy** When the Fund was established in 1991, the investment policy adopted was similar to that of the Cayman Islands Currency Board. For reasons of prudence, permissible investments were restricted to cash and government-issued or backed securities. Prior to 1996, all investments were held in fixed deposits. Therefore the Fund has achieved a risk free return of only 5% - 6% p.a. and has failed to benefit from the higher returns of the bond and equity markets in recent years. An investment manager was appointed in 1996. It is expected that changes to the law will be proposed to permit investments in a broader range of investments, which should provide a better long-term return. A higher rate of return on the Fund's assets will reduce the funding requirements needed to pay future benefits.

1.36 Both the 1993 and 1996 actuarial valuations demonstrate clearly that the Fund will be unable to meet the projected pension and benefit payments at the current rate of contribution, even if payments from the Fund were to be delayed for the foreseeable future. Under the existing Pensions Law, the Board cannot begin to pay pensions, gratuities and other allowances from the Pensions Fund until the actuary has certified that it is self-sustaining. Pension contributions were increased from 8% to 10% of salary with effect from January 1996. The actuary has assessed the normal cost of pensions at 18.3% of basic pay. After taking into account future new entrants, the actuary has also indicated that the long term costs should be around 30% of pay in order to meet the projected liabilities, including amortisation of the past service liability. The Audit Office concluded that the actuarial deficiency has increased considerably during the past 18 months.

1.37 In the longer term, the cost of pension benefits is expected to increase rapidly. By way of illustration, the actuary has reported that projected annual cost of pension benefits will be approaching $30 million (30% of payroll costs) by the year 2016 and almost $60 million (over 40% of payroll costs) by 2026. By contrast, pension payments are currently around 5% - 6% of relevant payroll costs. The funding of pension liabilities will therefore have a major long-term budgetary impact on public finances. Recognition of the pensions liability and creation of a separate Public Service Pensions Fund are important first steps. The Portfolio of Finance and Economic Development is in the process of developing a funding scheme and contribution levels so that the Fund will be self-sustaining by an early date.

Arrears of Revenue

1.38 The amount of revenue arrears at 31 December 1996 was $15,564,395. This is a noticeable improvement from the figure at 31 December 1995 ($18,359,308). The debt collection unit has played an important role in reducing revenue arrears. As an example, the threat of legal action by the unit is said to have increased the collection of hospital fees by approximately $100,000 per month.

1.39 Arrears of Company Fees at 31 December 1996 totalled $2,333,939. This amount has subsequently been reduced to $243,861 at 31 March 1997. The reduction is partly attributable to the removal of certain arrears from the schedule in respect of companies which the Registrar intends to strike off. As the fees were payable to government at the year end, the Audit Office **recommends** that they should be classified as claims abandoned and disclosed in the 1997 Losses Statement.

Write-Offs, Waivers and Losses

Control and Reporting of Losses and Special Payments

1.40 Losses and special payments are transactions which the Legislative Assembly cannot be supposed to have contemplated when an appropriation was approved. There are therefore strong grounds to report these transactions in the published accounts so that the legislative branch is able to exercise oversight and control of the Executive Branch. Effective public accountability and good governance is also facilitated through full disclosure. Losses and special payments may also point to weaknesses in systems or to managerial efficiency generally. Under section 55 of the Public Finance and Audit Law (1997 Revision), authority to write-off all abandoned claims and losses of public moneys (except through fraud or theft) and stores is vested with the Financial Secretary. Existing financial regulations require reports to be filed for all losses of cash, fixed fee receipts, stores and other public property.

1.41 The Audit Office is of the opinion that the definition of losses in financial regulations is somewhat vague and **recommends** that the definition of disclosable losses should be widened in keeping with reporting practice elsewhere. In the United Kingdom, for example, all defined losses must be brought to the attention of Parliament. Defined losses comprise:

A: Cash Losses

A1 Cash losses due to theft, fraud and arson, including stamps, tokens, postal orders, fixed fee receipts, physical assets, etc.

A2 Cash losses due to other causes, including bookkeeping losses, charges to clear inexplicable balances, overpayments of pay, pensions, and allowances not due to theft or fraud.

A3 Cash losses due to overpayments to contractors, grants, subsidies due to miscalculation, or misinterpretation.

A4 Losses due to failure to make adequate charges for the use of public property or services.

B: Stores Losses

B1 Losses of stores due to theft, fraud or arson.

B2 Stores losses due to other causes, e.g. over supply, time expiry, bookkeeping imbalances, physical discrepancies, etc.

C: Fruitless Payments and Constructive Losses

These are payments that are unavoidable because the recipient is entitled to it, although nothing useful is received in return. Examples include: forfeiture under contracts as a result of error or negligence; payment for travel tickets or hotel accommodation booked but not used; goods wrongly ordered and accepted; cost of rectifying design faults due to lack of diligence or defective professional practices; and extra costs due to failure to allow for foreseeable changes in circumstances.

D: Claims Waived or Abandoned

There are subtle distinctions between claims waived and abandoned. Abandonment includes claims made and reduced, or not pursued for policy reasons; claims which were never made because the whereabouts of those responsible could not be established; failure to pursue claims to finality, for example where they have become time barred by the Limitation Law; claims arising from actual contractual or other legal obligations which are not met, whether or not pursued, for example under default or liquidated damages clauses of contracts. A practical example of claims abandoned is statutory late filing fees payable under the Companies Law which are not imposed (paragraph **1.43**).

E: Special Payments

E1 Extra contractual or ex gratia payments to contractors.

E2 Other ex gratia payments.

E3 Compensation payments.

E4 Extra statutory or extra regulatory payments.

1.42 Losses in 1996 appear to have been minimal and only two cash losses amounting to $453 have been disclosed in the 1996 Statement of Losses, Write-Offs, Waivers and Losses. During the year several additional losses and special payments came to the attention of the Audit Office. These include:

- Time expired drugs valued at $44,938 written off.
- A camera and PC stolen (losses were covered by insurance).
- An ex gratia payment of $15,270 being three months salary to one overseas officer, following a period of extended sick leave from November 1994 to May 1996 (five months on full pay and the balance on half pay). The Controlling Officer has stated that the period of sick leave was well within compliance of what a public officer would have been eligible for under similar circumstances. According to General Orders, the maximum sick leave for officers on contract terms is 90 days. Normally, appointments should be terminated if they are unfit to resume duty after that date.

General Registry and Shipping – Failure to Levy Late Filing Fees

1.43 A recent report by the Internal Audit Unit revealed that late filing fees payable under sections 40 and 41 of the Companies Law (1995 Revision) are not being enforced. The Registrar of Companies has advised that it is not feasible to impose penalties because of the Registry's inability to process bulk receipt of such correspondence. There has also been an unwritten policy not to impose late filing fees, as this could adversely affect the Registry's competitiveness. Statutory returns and fees are payable in January of each year. Companies are not deemed to be in default until 12 months after the due date for filing. A late filing fee of $1 for each day after the last day of each January is payable under section 40(3) of the Law. This increases to $10 per day once the company is deemed to be in default. Company directors and managers who knowingly and wilfully authorise or permit such default also incur the penalty.

1.44 The Audit Office reviewed 1996 revenue collections and established that most companies do not file and pay by the due date:

Percentage of Company Registration Fees Received by:	*Companies on Register As at January 1996*
31 January (the due date)	19%
31 March	55%
30 June	78%
30 September	90%

A similar collection pattern was observed for 1997. The above figures exclude companies on the Register at 31 January 1996 with fees still unpaid as at 31 December 1996. It is not possible to quantify accurately the value of late filing fees not enforced and uncollected. Based on cash collections, the revenue loss for 1996 is estimated to exceed $1.8 million. Consideration is being given to proposing a change to the Law whereby filing requirements and fees fall due on the anniversary of a company's incorporation, rather than the present fixed date of 31 January each year. The Registry believes that this will make its task of following up late filing and overdue fees much more manageable. Any other statutory fees or charges which are not imposed or collected from companies should be disclosed on the annual losses statement as Claims Abandoned.

PART II

Departmental Audits

H M Prison Northward

2.1 During September 1996 the Audit Office carried out an expenditure study at Northward Prison. The following areas were examined: purchasing and stock-recording procedures, the Priscraft operation, welfare funds, water usage, prisoner remuneration and overtime payments. Detailed recommendations have been made to the Director of Prisons on the following issues. The Director has agreed to the recommendations and many have been implemented during 1997. The main points arising are summarised in paragraphs **2.2** to **2.10**.

Purchasing and Stock-Recording Procedures

2.2 The procedures in existence at the Prison for purchasing and stock-recording require improvement. This conclusion is based on a number of findings, which are outlined below. The head of each section at the Prison submits purchase requisitions for items required. Administrative staff issue Purchase Orders (POs) to buy the required items from suppliers. The purpose of purchase requisitions and POs is to ensure that limited resources are only used to acquire authorised inputs.

2.3 Auditors investigated numerous cases in which the description on POs and suppliers' invoices was a bland 'goods' or 'merchandise'. We were able to obtain copies of cash register receipts from suppliers in respect of some of these invoices. Our findings were disturbing:

- Many of the items bought were surprising. The purchases ranged from cat food, personal hygiene and hair-care products, grocery items, laundry detergents and softeners, sodas, Easter eggs, chocolates and cakes to vitamin/mineral supplements. From late 1992 to June 1996 the Audit Office identified purchases of similar household or personal items totalling $13,403. The total involved may be more. Payments were charged to the Dietary/Food Supplies expenditure vote. Most of the items were purchased in 1995 or 1996 from the retail section of a local supermarket. This includes seven invoices totalling $2,788 issued in 1992-94 which were not paid until 1995-96.

- The storekeeper did not know of these purchases, which were not recorded in the stock records of the Prison's general stores area. The goods were apparently delivered to the administrative offices at the

Prison. Most of the items are believed to have been consumed by Prison employees. The Audit Office does not accept that these were legitimate purchases because they were not intended for the general population of the Prison. It is not appropriate to charge this expenditure to public funds.

2.4 The Director acknowledges and regrets that administrative staff made the purchases. The practice has ceased since the audit findings were reported. The Audit Office concluded that the circumstances surrounding the purchases are suspicious. There appears to have been misuse of public funds. The Director has confirmed that he will endeavour to identify who consumed the items and, if appropriate, make cost recoveries by salary deductions.

2.5 It is important to point out that the preceding should not taint the spending by the kitchen unit at the Prison. The total expenditure incurred in the Dietary/Food Supplies vote during 1996 was $294,260. With an average inmate population of 187 during 1996 this translates into a modest cost of $4.31 per prisoner per day, including the cost of meals provided to on-duty Prison officers.

Rehabilitative Activities - Operation of the Priscraft Account

2.6 Government and Prison officials have important roles to play in the rehabilitation of inmates at Northward. One instrument of inmate reform and training is the Priscraft operation. Participants receive instruction and work experience in tailoring, motor mechanics, ceramics and woodwork. Priscraft trading operations are supplemented and supported by public funds in two ways. Part of the Prisoners' Rehabilitation vote is used to purchase materials and other inputs. Between 1991 and 1996 a total of $459,223 was spent against authorised expenditures of $444,000. A further $103,000 has been voted for 1997. Participants do not receive wages directly from the Priscraft operation but are paid via the Indigent Prisoners' Remuneration vote (1996 expenditure: $137,660). It is not possible to quantify the proportion of expenditure attributable to the Priscraft operation. In 1989 the Director of Prisons opened a bank account for the Priscraft trading operation. The Legislative Assembly was unaware of Priscraft's existence and gave after-the-fact approval to the operation by passing Government Motion No. 2/91, subject to certain conditions and safeguards:

- records of goods and services produced should be maintained
- receipts and payments and supporting documents should be easily verifiable
- the Accountant General should be furnished with quarterly summaries of transactions through the bank account
- Priscraft may retain all income earned provided that the balance in the account does not exceed $20,000.

Regrettably, most of the conditions set out by the Legislative Assembly have not been complied with.

2.7 Auditors noted several areas of concern about Priscraft operation.

- Inadequate record-keeping is the greatest failure of the operation. Records of items produced, materials used in the operations and the sales therefrom are unsatisfactory or non-existent. There is substantial doubt as to whether all revenue earned, expenditure, receipts and receivables will ever be captured in the accounting records.

- Auditors examined the cashbook kept for Priscraft operations. There were no transactions for 1996 entered into the cashbook, as of October 1996. This was communicated to the Director on 22 October 1996. In July 1997 auditors were told that a new, separate and distinct cashbook has been opened for 1996 transactions. It is said to have been available at the time of the auditors' visit. The Audit Office does not agree with these statements. The cashbook has never been reconciled with the bank account. Quarterly summaries of transactions had not been furnished to the Accountant General as required.

- Part of Prisoner Rehabilitation expenditure (public funds) relates to purchase of raw materials and other inputs for the Priscraft trading operation. The precise amount applied for this purpose since 1991 cannot be determined but is considered to be substantial. It is not clear whether funds voted for Prisoner Rehabilitation are intended to be spent on this purpose. The lack of adequate stock and financial records and the absence of financial statements for the Priscraft operation make it impossible to give a proper account of how the materials have been utilised.

- There is some evidence of mismanagement and abuse of the operation. There have been substantial volumes of credit sales. As there were no proper financial records, the exact amount of receivables was not known. Management estimated receivables to be $40,000 - $50,000 in September 1996. Auditors were astonished to learn that Prison officers owed some $15,000 and several of these debts were over two years old. Some officers clear their accounts monthly whilst others are allowed to accumulate large balances without loss of credit. Other entities have been allowed to build up large balances owed to the Priscraft operation without suspension of credit. This indicates a lack of effective management of the operation.

2.8 The Internal Audit Department has reviewed systems and procedures, including pricing policy and revenue collection and has issued a draft report and recommendations. Following consultation with the Accountant General, the Director has instructed that all transactions will be processed through a

Treasury suspense account so that there is a basic record. In a post-audit discussion with audit personnel, the Director reported a number of improvements. Deductions have been made from Prison Officers' salaries to clear outstanding balances. There is evidence that debts are now being pursued and collected. At 31 December 1996 debtor balances totalled $36,446. By 31 March 1997 the amount had decreased by $14,363.

Welfare Fund

2.9 Since 1991 a total of $137,481 has been spent against the Prison Welfare Funds / Social Security vote. Of this amount, some $98,000 has been paid to the Prison Welfare Fund as a contribution towards insurance for Prison Officers. The Prison Welfare Fund is not subject to audit by the Audit Office. Auditors examined payments made from public funds for the period January 1995 to September 1996. Certain purchases are highlighted below:

- bedroom furniture - $1,550;
- a three piece living room set, one centre table and four dining room chairs - $1,248;
- a dining room table and four chairs - $495;
- other purchases of household items such as towels, bedspreads, pillows and drapes - $5,160.

The items have been used to furnish officers' bungalows at Northward. This practice subsequently ceased in 1997. It is not clear to the Audit Office whether these payments reflect the wishes and intentions of the Legislative Assembly. Some of the items outlined above would only be legitimate purchases if provided in the capital expenditure budget approved by legislators.

Overtime Payments

2.10 Due to the nature of Prison operations, some overtime is inevitable at Northward. The Audit Office observed that there have been positive attempts to reduce overtime in recent years. Overtime costs have been reduced from $278,749 in 1995 to $100,000 budget for 1997. Auditors reviewed overtime payments during the first six months of 1996. The main findings were:

- An administrative staff member claimed overtime in respect of work performed during lunch hours. The amounts involved are not material. Whilst General Orders do not expressly prohibit payment for lunch break overtime, Personnel Department does not encourage this practice, which ceased in 1997.

- A member of the administrative staff made claims for overtime worked when the staff movement register indicates that the officer was not at work. The Director has investigated and has concluded that the staff movement register is not always entirely reliable. Auditors were told that administrative staff often leave their offices in the central Prison compound and perform overtime duties outside the general Prison area at the Director's office. In those instances the staff movement register, which is located at the Prison admission area, would indicate that administrative staff had finished work for the day. As a result of the auditors' findings an overtime log is now maintained. This is reviewed and signed by senior management as acknowledgement that the overtime was actually performed.

Department of Environmental Health

Recycling Programme

Background

2.11 Grand Cayman currently generates around 37,000 tons of garbage and solid waste each year. The Department of Environmental Health (DEH) is responsible for the collection, transportation and disposal of solid waste. The service provided includes extended kerbside refuse collection, commercial container service, community containers, public drop-off facility, litter collection, derelict vehicle removal, collection of dead animals and street sweeping in George Town. DEH operates a sanitary landfill, scale house and a medical waste incinerator in the heavy industrial zone. Two disposal areas are operated on the landfill. The garbage disposal area receives loads of mixed waste including putrescible materials. The trash area receives yard waste, construction and demolition debris and other non-putrescible materials, including scrapped vehicles and household appliances.

2.12 Prior to 1991, operations at the landfill were hampered by the lack of heavy equipment and the absence of a daily soil cover. During 1991 consultants were hired by DEH to examine solid waste management on Grand Cayman and to recommend ways of reducing the amount of waste placed in the landfill. The consultants estimated that 28% of the waste stream could be recycled, although only 50% of recyclable material would be recovered, for a total waste reduction of around 14% to 15%. This would require a second collection or handpicking to process recyclable materials. The consultants concluded that recycling would not be cost effective, mainly because of high transportation costs as there was no local market for recycled materials. Recycling costs were expected to exceed the landfill disposal costs. After reviewing several alternative disposal plans, DEH selected the air curtain incinerator option, supplemented by recycling glass, aluminium and ferrous metals. This method reduces the volume of waste by burning paper and other combustible material. In 1992, the United States Environmental

Protection Agency banned air curtain incineration as a means of solid waste disposal thus eliminating this alternative. Solid waste has therefore continued to be disposed at the George Town landfill, a 93 acre site operated by government since late 1970. In 1993/94, DEH embarked on a strategy to reduce dependence on landfill operations through a policy of recycling.

The Recycling Programme

2.13 Although recycling is not a new technology, it is experiencing increased attention and is gaining widespread acceptance as an alternative approach to solid waste management and disposal problems. Because recycling reduces the waste stream, it can be a viable way of expanding the life of the landfill and reducing future landfill requirements. Recycling can also help to reduce the harmful effects on the environment caused by hazardous materials. By the end of 1996, DEH had established recycling programmes for Christmas trees, automotive batteries, corrugated cardboard, aluminium cans and used motor oil. Additional programmes are being developed for office paper, glass bottles and tyres. The total recycling programme cost from 1993 to 1996 was $888,382, including $299,191 for capital equipment and facilities. Gross revenues received during the same period were only $70,408. Analysis of project revenues and costs indicates that recycling revenues do not cover shipping costs **(Figure 2.1)**.

Figure 2.1 Summary of Materials Recycled 1994-96

Material	*Tons Shipped*	*Revenue*	*Average Revenue*	*Direct Costs*	*Net Expense/ (Revenue)*	*Performance Measures Material Recycled*		
		$	*$/ton*	*$*	*$*	*Target (1996)*	*Achieved (1996)*	*Target (1997)*
Aluminium	16	11,920	745	4,371	(7,549)	42%	2-3%*	45%
Batteries	349	33,085	95	22,799	(10,286)	60%	70%	70%
Cardboard	461	25,403	55	47,935	22,532	60%	5-7%*	40%
Newspapers	0	0	0	0	0	25%	Nil	40%
	826	70,408		75,105	4,697			
Oil (gallons)	10,400	Nil	Nil	6,800	6,800	37%	10-15%*	20%
Sub total		**70,408**		**81,905**	**11,497**			
Other operating expenses					507,286			
Capital costs					299,191			
Total					**817,974**			

Notes

Direct costs comprise inland transportation, ocean freight, handling and other charges

* Audit Office estimates based on 1991 waste audit, DEH projections and actual quantities recycled.

Programme Performance

2.14 The Department has published several long term recycling goals in its annual budgets, which are subject to review and revision in light of experience. There are several inherent difficulties in reviewing the Department's recycling performance.

- Many of the initial assumptions included in the department's appraisal of recycling projects were based on established recycling programmes in the United States. The potential volume of recyclable materials was derived from a limited waste audit carried out in 1991. In hindsight, some of the forecasts were too optimistic. For example, an early estimate of 24 million recyclable aluminium cans now seems much too high.

- No data are readily available on the quantity of certain products imported and the recovery potential.

- Before 1996, the Department did not have reliable data on the volume of material deposited in the landfill. With the commissioning of the scale house, the Department is now able to record the weight of waste collected. The difficulty of estimating the composition of the waste stream and the potential for materials recycling remains.

2.15 Although the Department has accurate records of materials recovered and recycled, it has not been able to establish the percentage of materials recycled. However, only the battery programme appears to have achieved the targets set by the Department. Both the aluminium and cardboard programmes appear to have fallen well short of the initial volume targets published by DEH. Both programmes have been adversely affected by poor world prices, particularly the cardboard programme. The price for corrugated cardboard plummeted in 1996. Although no shipments of cardboard were made for a year, the Department and the private sector continued to collect and bale cardboard. Most of this was subsequently dumped in the public landfill, with some donated for private land reclamation purposes.

2.16 The Audit Office reviewed several project appraisals, which were prepared by the Department shortly after the recycling programme commenced. Each of these uses an estimate of $116 per ton as the cost of disposing solid waste, which was reportedly prepared by consultants. Reference to the consultants' report confirms that the figure of $116 relates to the total costs of collection, disposal and administration. The disposal cost calculated by the consultants was only $26 per ton at 1991 prices. The Department's current estimate is $48 per ton. Had the appropriate cost of disposal been used, it is likely that project appraisals would have shown recycling not to be cost effective. In the opinion of the Audit Office, thorough project design and appraisal should have been carried out before the recycling activity commenced.

2.17 Based on DEH's own figures, the net cost of the programme for 1993-96 is approximately $650 to $670 per ton of materials recycled, including depreciation of specialist plant and equipment. This is about 14 times the assessed cost of disposal in the sanitary landfill. The Audit Office estimates that the quantity diverted from the landfill is less than 1% of the total waste stream over three years. Recycling has removed significant quantities of hazardous materials from the landfill. It is difficult to place a monetary value on the benefit of this service. The Department has commented that experience elsewhere has shown that costs tend to be high when a recycling programme starts. It expects to reduce future unit costs substantially. The Audit Office concluded that increasing the quantity recycled and keeping a tight control of costs should be one of the Department's key objectives if the recycling programme is to succeed. Comments on individual programmes follow.

Batteries

2.18 Apart from commercial considerations, recycling of used batteries is environmentally important, due to concern over the toxic components in batteries, including lead, cadmium and mercury. Used batteries are hazardous and a single unit can pollute large quantities of groundwater. Cayman Brac has also instituted its own programme for used batteries, which are shipped to Grand Cayman. The programme has enjoyed good support from garages, service stations and the general public. The DEH regularly collects batteries from pickup points. The programme appears to be very successful and DEH estimates that 70% of used batteries disposed of during 1996 were recycled.

Used Motor Oil

2.19 For many years used motor oil was dumped in the landfill or was used for private projects such as dust control on unpaved roads. One of the Department's main concerns is that used motor oil contains a number of substances harmful to human health, including lead, arsenic, zinc, cadmium, barium, chlorinated solvents and other toxic materials (benzene, toluene and polychlorinated biphenyls (PCBs). Around 80,000 gallons of oil are imported each year. The private sector has led Cayman Islands' oil recycling effort. Caribbean Utilities Company (CUC) commenced recycling about four years ago and presently ships over 30,000 gallons each year to the USA. CUC has also assisted DEH recycling efforts through the loan of shipping equipment. Texaco's recycling project began in June 1996 and the company shipped approximately 25,000 gallons of waste oil in its first year of operations. Both private sector operations are carried out at no cost to government. However DEH estimates suggest that between 20,000 and 30,000 gallons of used oil may be unaccounted for each year. It is assumed that much of this is dumped.

2.20 Recycling used oil is expensive and does not generate any revenue. Before 1997 DEH had to rely on borrowed shipping equipment, which limited the extent of recycling. Therefore, only 10,400 gallons of used oil were shipped to processors between 1993 and 1996. The average cost was $0.65 per gallon.

United States legislation now classifies oil with high concentrations of halogens as hazardous waste, which is more difficult and more expensive to dispose of. The Department's most recent shipment in April 1997 was classified thus, with the result that the unit cost of disposal increased dramatically to $3.30 per gallon. Now that the Department has purchased its own equipment for storing and shipping oil, it is expected that the frequency of shipments will increase. Effective disposal of all used oil could potentially cost government between $50,000 and $100,000 per annum. The Audit Office believes that there may be scope for reducing disposal costs through co-operation with the private sector.

2.21 Considerable quantities of used oil are stored in rusting fuel drums at the sanitary landfill. This is a potential environmental risk. At the date of our site visit in June 1997, there were pools of surface oil at the facility. There was a serious oil spill in 1995 due to inadequate storage facilities, which caused damage to the surrounding environment. The Audit Office found that the Department had properly assessed both the environmental risks and financial costs of oil storage and disposal. DEH has proposed essential improvements to the storage facility, including a concrete base and an oil drainage and recovery system to minimise pollution. The project has not yet been implemented. The Ministry of Agriculture, Environment, Communication and Works (AECW) considers that the proper collection and export of waste oil requires immediate attention. The Audit Office also noted that the Department has proposed an advance oil disposal fee from importers to help pay for the costs of disposal.

Corrugated Cardboard and Office Paper

2.22 Cardboard is estimated to make up about 12% of total solid waste, around 4,200 tons per annum. Recycling appeared to be a viable option to the DEH in 1995 when the cardboard programme began. The indicated recovery price at that time was US$180 per ton. The programme has been supported enthusiastically by the major supermarkets, which have co-operated with the Department. Regrettably, the viability of the programme has been weakened by low market prices for cardboard and by legislation in the United States. Shipments were initially made to Guatemala, but revenue earned was only US$70 per ton. This covered only part of the shipping cost of US$1,422 per container. By March 1996 the market price had fallen to US$15 – US$30 per ton. The buyer declined to accept any further shipments with effect from May 1996. The programme resumed in May 1997 with shipments to the USA. The current price of cardboard is only US$40 – US$50 per ton, which covers only about half the shipping cost. In order to meet the US Department of Agriculture regulations, DEH has to sort and remove all cardboard, which has contained meats or perishable foodstuffs. Apart from reducing the recycling yield, this makes the operation very labour intensive and even more costly.

2.23 The Department embarked on a pilot scheme for office paper recycling in the Tower Building in July 1996. The programme was extended to other government buildings in July 1997 and the Department expects to implement the programme in the private sector imminently. The long-term goal is to recycle 50% (estimated 358 tons per annum) of office paper generated in Grand Cayman. Collections from the pilot scheme have averaged 200 pounds per week. No shipments have been made to date. White bond paper is currently worth about US$120 per ton and continuous feed paper is about US$180 per ton. The Audit Office concluded that it was too early to evaluate the performance of this programme.

Aluminium Cans

2.24 This programme began in 1995. The Department's project appraisal concluded that recycling was economically feasible at the prevailing market price for aluminium of 63 cents per pound. DEH projections were based on the assumption that 463 tons of aluminium cans are potentially recoverable each year. The Department calculated that it would need to recover only 10% for the programme to be financially viable. The actual quantity recycled in a two year period was only 27.7 tons, including about 5.5 tons of extrusion and scrap. Revenues have ranged from 34 to 51 cents per pound. Both the quantity recycled and revenue generated are significantly below the assessed break-even point. The Department has followed a strategy of voluntary participation, accompanied by community collection sites with emphasis on public buildings and schools. DEH officials report mixed support from the tourism and restaurant sectors. Several properties have willingly participated in the scheme, but there appears to be apathy from many others. A major weakness of the aluminium can programme is the absence of a viable and cost effective collection system. The Department cites lack of incentives and the absence of "green" legislation as factors contributing to the low percentage of materials recycled.

Additional Programmes Planned

2.25 DEH intends to commence recycling of glass and tyres during 1997. Whilst these programmes will reduce the waste stream, they are unlikely to generate any significant revenues.

Other Issues

Medical Waste Incinerator

2.26 DEH operates a two-chamber burner for disposal of medical waste generated by government facilities and private practitioners. The latter pay a disposal fee of $1.50 per pound. The chamber is not equipped with air emission control devices and does not meet current USA EPA standards. The chamber was brought into service about six years ago. DEH has advised that the chamber has been malfunctioning for a lengthy period. The lower chamber does not heat up to the required level, with the result that medical waste is not incinerated properly. Essential repairs would be very costly and DEH considers that it would be more economical to replace the equipment. During a site visit in June 1997, the Audit Office learned that the burner had been temporarily withdrawn from service. We were advised that medical waste had been burned in open dumpsters intermittently over a period of several years. This is a serious health hazard which ought to be addressed as a matter of extreme urgency. The practice is in direct contravention of the Public Health (Infectious Waste) Regulations 1991 made under the Public

Health Law. Several requests have been made for funds to replace the incinerator. During 1996, DEH requested funding of $375,000 in the 1997 budget to replace the chamber with an autoclave. Although the Ministry of AECW supported the project, funds were not allocated.

Legislation

2.27 There are numerous laws and regulations covering garbage and solid waste collection services, fees for such services and incidental matters. However, no comprehensive legislation has been enacted to cover the importation of hazardous materials and subsequent safe disposal. The Ministry of AECW is presently reviewing legislation and is examining the disposal costs of certain materials.

Agriculture Department

Cattle Sales

2.28 The cattle purchase scheme was initiated in 1992 in conjunction with the Agricultural Development Plan. The scheme provides for individuals to purchase livestock on a credit basis. The Chief Agricultural and Veterinary Officer interviews recipients before placing orders. Applicants are required to deposit 25% of the purchase price and to enter into a formal purchase. Credit terms include a 24 month moratorium with repayment scheduled over 12 months. Since inception of the scheme, approximately $126,000 has been spent on the purchase of cattle for resale. The Department’s policy is to recover the full cost of livestock purchased, including freight, from the farmer. The Audit Office’s review confirmed that this objective has been achieved.

2.29 The Audit Office reviewed the adequacy of controls for recording sales and loan recovery performance. The main findings were:

- At December 1996, $27,577 was due from 38 farmers, of which $11,489 representing 27 accounts was in arrears.
- Ten accounts totalling $3,970 should have been retired as per credit agreements.
- Four clients made no payments on their accounts after making the required deposit.
- Six clients with delinquent accounts were identified as either civil servants or retirees. No salary deduction arrangements had been made with these officers.

2.30 Following the audit, the Department of Agriculture has reported improvements in the recovery of outstanding amounts. Eight overdue accounts have been brought up to date. Three of the four individuals who had made no payment after placing the required deposit have now made payment on their accounts. Salary deductions commenced in April 1997 for three individuals identified as civil servants or retirees, while two other accounts have been passed for legal action. The Audit Office concluded that remedial action taken by the Department had been effective.

Public Works Department

Road Maintenance and Construction

2.31 The Audit Office last reported on road maintenance and construction in 1992[2]. Between 1992 and 1996 some $23.6 million has been spent on road maintenance, improvement and construction, including approximately $3.0 million for Cayman Brac (**Figure 2.2**). Almost all road maintenance is carried out by Public Works Department's direct labour organisation (DLO). Much of the capital projects have also been carried out by the DLO, although the Department contracts out all hot mix and some chip and spray work.

Figure 2.2 Road Construction and Maintenance Costs 1992-96

	1992	*1993*	*1994*	*1995*	*1996*	*Total*
	$m	*$m*	*$m*	*$m*	*$m*	*$m*
Capital Projects	1.506	1.423	3.374	3.168	5.223	14.694
Road Maintenance (1)	1.133	1.069	1.158	1.188	1.262	5.810
Admin & Professional (2)	0.686	0.614	0.560	0.594	0.671	3.125
Total	**3.325**	**3.106**	**5.092**	**4.950**	**7.156**	**23.629**

Notes
(1) Road maintenance includes traffic lights, signs, drainage and wells
(2) Administrative and professional includes direct salary costs for administrative, professional and executive personnel allocated to the Roads cost centre.
Source: Audited accounts 1992-96

The Audit Office's examination focussed on services contracted for the George Town resurfacing programme in 1996 and the purchase of road construction materials.

[2] Report of the Auditor General, 1991, pages 22 - 29

Road Resurfacing Contracts Awarded

2.32 During 1996 Public Works Department (PWD) undertook several major road resurfacing projects on Grand Cayman comprising 6.7 miles of hot mix overlay and 4.1 miles of chip and spray, in total costing $2.297 million. These works were carried out by contract. The specification for hot mix overlay called for a tack coat, two inch asphalt overlay and regulating uneven surfaces. The hot mix budget was based on a rate of $20 per square yard, including a tack coat and regulating. There were only two recognised contractors for hot mix overlay. Originally PWD considered that neither company was in a position to carry out all the work within the required time frame. The Department therefore concluded that the work should be divided between the two companies. Tenders were invited from both companies. One tender was received two hours after the closing date, and was returned unopened in accordance with normal procedures. All works contracted out were completed during 1996 except for phase II of the hot mix works valued at $205,686, which was completed during February 1997. Works carried out under contract are covered by a 12 month maintenance period.

2.33 Tender prices for hot mix overlay were considerably less than budgeted cost. The Department attributes this to a competitive bidding situation and volume discounts. PWD engineers supervised all contracted works and the Department is satisfied that the works have been executed in accordance with specifications. Subject to the following observations, the Audit Office was satisfied that tendering procedures and the award of the various contracts had been carried out in accordance with Financial and Stores Regulations.

- Resurfacing works to the value of $155,218 were authorised through non-competitive quote purchase orders (POs). PWD officials explained that it was not feasible to put these projects out to competitive bid, complete the works and effect payment before Treasury closed the books in early December. Although unit costs charged were generally consistent with prices obtained through competitive tender, this procedure is contrary to financial regulations and could have been avoided with better long term planning. The normal 10% contract retention was not deducted from payments to the contractor, although contract retentions were applied in all other resurfacing projects awarded under competitive tender.

- Three tenders were received for all chip and spray projects reviewed by audit. Contracts were awarded to the lowest bidder in every case except T96/055, where the second lowest bidder was successful. The Department advised that they wanted to try out the particular company. If performance was satisfactory, it was intended to award additional work to the company. The Department also pointed out that the lowest bidder was committed elsewhere and there were some doubts that the company might be over stretched. The additional cost was $22,026.

Materials Testing

2.34 The Department is unable to carry out materials testing locally. Only one materials test was carried out for all the resurfacing works carried out by contract. PWD personnel agree that regular testing should have been carried out on both the resurfacing works and on other road construction materials purchased. The Department has a materials testing laboratory which is not operational, although there are qualified and experienced personnel on staff who are able to carry out the necessary tests. Management has indicated that they are presently looking at re-establishing the facility and have obtained some price quotations.

Purchase of Road Construction Materials

2.35 Only limited supplies of road construction materials are available on island. During 1996 only one supplier was able to produce the quantities required by PWD. Most materials therefore had to be purchased from this single source on a non-competitive basis by POs, almost all of which exceed the $10,000 limit specified in regulations. The Audit Office established that the Department had purchased over $2.7 million of materials from this supplier between 1992 and 1996, including approximately 52,500 tons costing $850,125 in 1996. We noted that the prices of materials increased by an average 8% during 1996. PWD presently pays $17 per short ton (2,000 lbs) for crusher run delivered ex quarry. Despite the substantial quantities purchased, the Department did not negotiate a price discount in either 1995 or 1996. We also noted that the Department has not negotiated a fixed or firm price supply agreement or a call-off contract, which would provide some assurance about price levels and continuity of supply. Management has since negotiated a price discount on one item of construction materials. As government is planning major road development projects, every attempt should be made to reduce the cost of construction materials. The Audit Office **recommends** that the Department should investigate the cost and feasibility of importing road construction materials.

2.36 Subsidiary matters arising from the review of purchases were reported to and discussed with management. These include: non availability of an official price list; an inadequate audit trail linking delivery tickets with supplier's invoices; variances between quantities ordered and actually delivered; and stores accounting and control over materials stockpiled. Management has confirmed that, where necessary, remedial action will be taken. Spot checks revealed that one vehicle's tare weight was understated by 1,780 lbs. As a result, the Department has been overpaying for almost one ton of material on each load. Management is investigating this discrepancy and the supplier has confirmed that all overpayments will be refunded in full.

Public Works Department

Purchasing Procedures

2.37 Public Works Department (PWD) is responsible for the management and provision of services necessary for the design, construction, improvement and maintenance of government buildings and roads. The Department's major task is supervision and management of the capital programme. Most large projects are contracted out, but the Department's direct labour organisation (DLO) carries out much of the road construction programme, as well as providing services to maintain and improve government buildings. The Department has 52 permanent employees and a fluctuating weekly paid labour force. The Department's 1996 direct operating costs were $6.586 million (1996 budget $6.790 million). During 1996 PWD issued 6,003 purchase orders totalling $6.346 million for goods and services to be used for both the capital and maintenance programmes. The computerisation of PWD's project expenditures [PWSS] has permitted greater transparency of the purchasing process than manual inspections would have achieved in similar time frames. Management advises that implementation of the IFHRIS project will significantly improve the oversight process with far greater effectiveness than PWSS currently achieves. The Audit Office reviewed purchasing procedures generally and carried out a more detailed examination in a number of selected areas. The audit revealed evidence of non-compliance with departmental purchasing procedures and financial and stores regulations. Key points arising are summarised below.

- In many instances, there was no obvious evidence of three competitive quotations for purchases in the range $1,000 to $10,000. It is noted by PWD that competitive quotations are obtained where feasible.

- There was no evidence that discounts had been negotiated with any major suppliers in 1995-96. A discount has since been negotiated with one major supplier.

- Works over $10,000 are required to be authorised by departmental tender committee (DTC) after competitive tender process. Auditors noted that the Department had issued a significant number of purchase orders (POs) from single source suppliers exceeding $10,000 without the approval of the DTC. The Audit Office concluded that controls to ensure compliance with departmental purchase limits had not been fully effective and need to be strengthened. Management has acknowledged that some personnel have failed to comply with established procedures and have placed POs without proper authority.

- Over an 18 month period one company selected for examination had been given 14 POs totalling $317,685, apparently without competitive tender. The value of individual POs ranged from $4,723 to $78,459.

- Several instances were observed where requirements were broken down into multiple purchases so that the value of each individual PO was less than $10,000. The Department recognises that this is an incorrect procedure and has taken action with personnel concerned to ensure that this is not repeated in future.

2.38 A review of POs issued by the air conditioning section revealed a number of anomalies.

- In many cases purchases over $1,000 were not supported by quotations from three suppliers as required by regulations.

- In many cases invoices were received before the issue of a PO. A random check of one supplier revealed 10 POs totalling $29,352 which were dated up to 53 days after the date of the supplier's invoice.

- The description of air conditioning parts was often not stated properly on either the PO or the invoice. This made it impossible to carry out substantive audit checks to establish that the parts had been used for authorised projects.

- In one transaction in 1995, PWD issued three consecutive POs to a company for the purchase of air conditioning compressors for the Administration, Tower and Legislative buildings. No competitive price quotes appear to have been sought. The total value of POs was $8,545, charged to capital and recurrent votes, which was paid on three separate invoices. Further enquiries revealed that only one compressor was required and had actually been purchased. Three invoices had been issued by the supplier to match the three POs issued. Management are presently investigating this transaction and will inform the Audit office of the results of enquiries. This particular transaction undermined audit confidence in the requisitioning officer's actions.

- The Department paid $2,741 for air conditioning work carried out at a leased property. On examination the invoice was found to be made out in the name of the property owner. PWD personnel stated that efforts would be made to recover this amount and management has confirmed that reimbursement is expected imminently.

- Due to staff shortages, the Audit Office did not carry out a comprehensive study of operational performance but considered this would be beneficial in order to assist the Department improve procedures and to secure better value for money.

2.39 The Audit Office noted that a number of single quotation purchases had been obtained from one company. Between January 1995 and September 1996 the company supplied approximately $580,000 of goods. We identified five instances where purchases for building materials and windows costing over $100,000 in total had been broken down into 16 POs, each of less than $10,000. Management has commented that this was done to facilitate internal project accounting. We noted a further five purchases totalling $86,241 where purchases costing over $10,000 had not been referred to the DTC as required by regulations. One of the more notable purchases involved a contract for $83,644, which was placed for the supply of 176 hurricane windows. The supply was based on a single, non-competitive local tender. The DTC directed the requisitioning officer to seek alternative tenders from local suppliers and to report back. However we noted that a contract was issued, apparently without the approval of the DTC. We were not able to locate any further report requested by the DTC and no additional tenders appear to have been obtained. Management has explained that there was no intention by the officer concerned to ignore the directives of the DTC, and there appears to have been some misunderstanding regarding these directives.

2.40 In view of these observations, the Audit Office carried out a pricing test of three purchases using Customs import entry documentation. This revealed mark-ups of over 100% in two cases by the local supplier. It also established that another middleman, or purchasing agent, had been used by the local supplier to purchase the goods in the United States.

Goods	*Supplier's Landed Cost**	*Price Paid By PWD*	*Mark-up*
	$	*$*	
176 aluminium windows	39,965	83,644	109%
11 portable turnstiles with base	17,232	24,508	42%
galvanised guard rails and fittings	15,008	33,011	120%

**landed cost is based on the amended value CIF plus regular duty established by the Collector of Customs*

The prices and mark-ups are considered to be excessive by the Audit Office and result from non-compliance with departmental procedures by individual officers. Management has advised us that orders for additional windows for other schools have been placed with a new local supplier, who was selected through competitive quotation.

2.41 As the invoices supporting the Customs declarations were handwritten, the Audit Office requested the Collector of Customs to check the authenticity of the import entries. Customs Department established that false documentation had been used to support two of the entries, which had been under-declared for duty purposes. The exporter was unable to provide acceptable documentation, such as a paid cheque, to support the third importation. Customs Officers were told that the purchase had been made by credit card and that the exporter could not trace additional supporting documentation. Customs Department levied additional duty, penalty and restoration fees of $10,980 for under-declaration of duty on two of the imports only. The Audit Office recognises that further investigations might reveal more evidence of excessive mark-ups, or possibly further evasion of customs duty. Management has assured us that the Department will not tolerate any unethical practices by suppliers and has directed that no further business is to be placed with either the exporter or the local supplier.

Conclusions

2.42 Our overall conclusion was that insufficient importance is being placed on the need to secure the best possible value for public funds. However we acknowledge that the Department is often placed under time and other operational constraints which prevent procurement in the most cost-effective manner. There appear to be opportunities for the Department to secure lower prices for goods and services purchased by:

- Establishing improved competitiveness within procurement procedures.
- Ensuring that all personnel comply with authorised procedures.
- Adopting single source supply arrangements only after thorough evaluation and prior authorisation by management.
- Consolidating and co-ordinating departmental requirements wherever feasible and practicable in order to secure lower prices or volume discounts from suppliers.
- Developing bulk supply and, where appropriate, call-off contracts.
- Establishing direct purchasing from main suppliers or overseas manufacturers.

2.43 Management acknowledges that these irregularities occurred during 1995 and 1996 and has emphasised that control weaknesses identified will be rectified. Management has agreed in principle with the audit recommendations, which will be implemented. However there are several negative factors in the Department's operating environment, which impede cost effective purchasing. Factors highlighted by the Department include:

- fluctuations in materials demand, particularly the road maintenance and construction programmes
- delays in project approval and late supplementary approval of projects which impose tight completion deadlines
- the length of time taken to process suppliers' invoices which prevents negotiation of favourable discounts
- partial approval of certain project budgets
- the principle of annuality, whereby all warrants and appropriations lapse at the end of each year
- the CPI has increased by 57% since 1986 when FSRs were introduced. The current range of $1,000 to $10,000 for competitive quotations equates to $1,600 and $16,000 at 1997 prices. This significantly reduces today's purchasing environment. PWD recommends revision to this financial range to reflect the CPI increases.

PART III

Audits of Statutory Authorities and Other Public Bodies

3.1 With the exception of the Civil Aviation Authority and the Public Service Pensions Fund, the financial statements of Statutory Bodies have been audited generally in accordance with time limits prescribed by the relevant laws.

3.2 For fiscal 1996 the Audit Office undertook the audit of six Statutory Authorities: the Agriculture and Industrial Development Board; the Community College; the Cayman Islands Currency Fund; the Housing Development Corporation; the Public Service Pensions Fund and the Water Authority. Private sector auditors were engaged by the Auditor General to carry out the audits of the Civil Aviation Authority and the Port Authority. The workload in this area is growing. For 1997 it is expected that three additional statutory authorities will fall to be audited by the Audit Office. We have also offered to provide assistance and guidance to help two authorities establish their financial administration systems.

3.3 Since presentation of the 1995 Annual Report, audits have been completed on the following financial statements.

3.3.1 **The Agricultural and Industrial Development Board**: Audit of the 1996 financial statements was completed on 6 August 1997. I have no report to make on this account.

3.3.2 **Civil Aviation Authority:** There have been delays in preparing the Authority's financial statements for the years 1994 to 1996. The problems and issues arising were summarised in the Auditor General's Reports for 1994 and 1995. The 1994 financial statements were eventually certified on 24 September 1996, following discussions between the Authority, the Ministry of Tourism, Aviation and Commerce and the Portfolio of Finance and Development. The audit of the 1995 statements was completed in March 1997 and the Board approved the financial statements on 22 July 1997. With the continuing co-operation of the Director of Civil Aviation and his staff, the 1996 audit should be completed in time to table the financial statements during the November 1997 sitting of the Legislative Assembly.

3.3.3. By 1996 the financial position between the Authority and Government had become somewhat entangled with several outstanding claims and counter claims. Details of how these claims were settled are disclosed below for record purposes.

- The Authority's contributions to Government for 1994 and 1995 ($1.5 million and $2.0 million) were treated as full and final settlement. The arrears of revenue claimed by government from the Authority and disclosed in the 1995 Arrears of Revenue Statement (1994: $1,108,796 and 1995: $608,794) were not pursued.

- The Authority waived settlement of rental increases accrued from government departments for 1994 ($466,103) and for 1995 ($526,673 estimate). The subject of increased rental payments for 1996 (CAA estimate $831,171) claimed by the Authority and agreed previously by government was not settled. Most of the Authority's budgeted revenue from this source for 1996 was not collected. It would appear that adequate provision has been made in government's 1997 Estimates for rental charges, but charges for utilities had not been paid when the situation was last reviewed.

- The Authority waived settlement of a $198,434 contribution from government in respect of the 1992 operating costs of the National Weather Service.

- The Authority settled legal fees of $25,000 per annum for 1994 and 1995, payable in accordance with Executive Council's general directive.

- Government assumed responsibility for settling Cayman Airways Ltd debts amounting to $1,236,792 owed to the Authority. The expenditure was charged to subhead 08-071 Cayman Airways Re-capitalisation. Settlement was processed through Government's books in 1995 by crediting the Authority's repayment of assets vested account. This resulted in prepayment of the Authority's annual loan repayments to government at the rate of $421,090 per annum, covering the period 1995 to 1997 and part of 1998.

- The Ministry of Tourism, Aviation and Commerce paid an amount of $297,777 for the Authority's 1996 grant for the operating costs of the National Weather Service.

3.3.4 **The Community College of the Cayman Islands:** The College's financial statements for the year ended 31 December 1996 were certified on 28 July 1997. A brief report is provided at paragraph **3.5** about the College's accounting problems.

3.3.5 **The Cayman Islands Currency Fund:** Financial statements for the year ended 31 December 1996 were certified on 28 May 1997. These are the final accounts of the Currency Board, which was superseded by the Cayman Islands Monetary Authority on 1 January 1997. There was no requirement to table the financial statements of the Currency Board in the Legislative Assembly, although the audited accounts are reproduced in the Gazette. I am pleased to report that this anomaly has been rectified. Financial statements of the new Monetary Authority will be tabled in the Legislative Assembly.

3.3.6 **The Housing Development Corporation:** Financial statements for the year ended 30 June 1996 were certified on 7 March 1997. I have no report to make on this account.

3.3.7 **The Port Authority:** Financial statements for the year ended 31 December 1996 were certified on 13 June 1997. I have given an unqualified audit opinion on these financial statements.

3.3.8 **The Public Service Pensions Fund:** Audit of the Fund's 1996 financial statements had to be deferred for two reasons. The rate of employer's contribution was increased from 4% to 6% with an intended effective date of 1 January 1996. Unfortunately the amendment to the law did not make the increase effective until July 1996. Management and auditors agreed that a further amendment to the law was needed in order to regularise the increased contributions collected for the period January to June 1996. At the date of preparing this report the amendment had not been passed. It was also intended to include all Caymanian group employees within the scheme, also with effect from 1 January 1996. Controlling Officers were advised about the increased contribution rate (6% employer and 4% employee) in November 1996. Managers were advised to make appropriate provision in their 1997 budgets, to include a supplementary provision to cover 1996 arrears. However it appears that some Controlling Officers still do not appreciate that contributions should now be collected on behalf of all Caymanian Group employees. There seems to be confusion with an earlier (and erroneous) direction that contributions should be collected only in respect of group employees with seven or more years service.

3.3.9 In summary, contributions have been collected from some, but not all, Caymanian group employees for 1996. Before the audit can be finalised, pensions management should review payroll records to identify group employee contributions payable as at 31 December 1996. It is also understood that a further amendment to the law is contemplated to define the term "Group Employee". The audit was postponed in order to give management an opportunity to rectify these issues and thereby avoid the need for audit qualification of the financial statements. The audit will be completed promptly once these outstanding matters are dealt with.

3.3.10 **The Water Authority:** Financial statements for the year ended 31 December 1996 were certified on 17 June 1997. I have no report to make on this account.

3.3.11 **Financial Statements of Non-Government Organisations:** Accounts certified in the previous 12 months include:

- The Commonwealth Parliamentary Association (Cayman Islands Branch): accounts for the year ended 31 December 1996;

- Cayman Islands / UK Overseas Students Fees (Refund) Statement for academic year 1996/97.

3.3.12 A number of financial statements for UNDP funded projects are outstanding and overdue, as described in paragraph **1.31 to 1.33** of this Report.

3.3.13 With effect from 1997 statutory authorities are being charged fees to cover the cost of audit work carried out by the Audit Office. The Public Service Pensions Fund will be charged an audit fee once it becomes self-sustaining.

Contributions from Statutory Authorities

3.4 Total contributions from Statutory Authorities were above budget for fiscal 1996 (**Figure 3.1**).

Figure 3.1: Contributions from Statutory Authorities

Authority	Subhead	Budget *1996* $	Collected *1996* $	Budget *1997* $
Currency Fund	71-101	800,000	1,272,889	1,300,000
Turtle Farm Ltd (1)	71-161	160,000	320,000	150,000
Port Authority	71-201	225,855	482,517	1,000,000
Civil Aviation Authority	71-301	2,600,000	1,500,000	3,000,000
Water Authority	71-401	Nil	500,000	1,000,000
Total		**3,785,855**	**4,075,406**	**6,450,000**

(1) Two financial years

The Audit Office notes that there are continuing attempts to improve co-ordination of the budget process between government and statutory authorities. However it appears that significant differences remain between the expectations of government and the plans of individual authorities concerning the amount of authorities' annual contribution to Government. This situation has continued into fiscal 1997. The contribution levels expected by government were not notified formally until after the March 1997 Budget session. The contribution levels expected by the Authorities were considerably less than government's expectations and it is not clear whether the full budgeted contribution will be collected.

- The Port Authority agreed that a contribution equivalent to 25% of the Authority's profits of the preceding year would be paid to government. The amount budgeted for 1997 was $419,438 (subject to audit). Government subsequently directed that the Authority's 1997 contribution would be $1 million. The Board has agreed to pay the increased amount.

- The Water Authority produced its 1997 budget in October 1996. In view of the Authority's capital commitments, the Board did not include a contribution to Government. The Authority was informed in April 1997 that the level of contribution approved by the Legislative Assembly was $1 million. The Board has concluded that it would not be prudent to commit the amount requested immediately. An interim contribution of $250,000 has been paid over and the Board will examine the Authority's financial position later in 1997 to determine what further money can be paid.

- The Civil Aviation Authority did not include a contribution to government in its 1997 budget and has now been advised that $3 million has been budgeted by government. The Board has resolved to examine the Authority's cash position and to pay the contribution requested by government, apart from a balance of $100,000.

One difficult area is the capital investment plans of Authorities, and the amount of operating profits which can be retained to finance these plans. This is not helped by the relevant laws, which refer to the authorities being permitted to retain a balance of $100,000. This type of restriction is not an appropriate method of controlling the finances of authorities and, in any case, has never been enforced by any government. The relationship between government and each statutory authority should be formalised so that both parties are agreed on the following financial issues: the scale of fees and charges levied by authorities, and any increases thereto; the scope and timing of capital investment plans; how the approved capital investment programme will be funded; and an agreed formula for distributing realised surplus or profit.

Community College of the Cayman Islands

3.5 Since 1994 the College has experienced continuing difficulty preparing annual financial statements to a reasonable standard. This situation deteriorated further during 1996. Most basic accounting records were not maintained during the year and the College was without the services of an accountant for six months. Bookkeeping and accounting functions were deficient, which caused considerable difficulty in preparing the 1996 financial statements. Draft statements were initially presented for audit on 24 March 1997. These were compiled from incomplete records and were acknowledged to be only an approximation. No general ledger, cashbook, trial balance or reconciliation of bank accounts existed. There was a cash difference in excess of $20,000 and fundamental uncertainty as to whether all transactions had been included in the draft statements. Audit Office concerns were communicated to the Principal in April 1997. It was agreed that revised draft financial statements would be submitted by 30 April 1997. The Audit Office had to provide significant accounting and investigative assistance in order to finalise the accounts. It was not possible to eliminate all imbalances and reconciling differences, but the unadjusted errors were within tolerable limits. As a result, the financial statements received an unqualified audit opinion 28 July 1997. The Audit Office is reasonably satisfied that the accounting problems have now been resolved. Significant audit observations and weaknesses will be brought to the attention of the Board of Governors in our annual management letter.

PART IV

Administrative Matters

Staffing

4.1 The Audit Office faced a difficult year due to high staff turnover. Five out of 11 audit personnel left the office during the year under review. Two Caymanian graduates were recruited in June 1997, but once again it was not possible to fill vacancies at Senior Auditor grade locally. Replacements have been recruited from the region and will be in post by the end of August 1997. Staff vacancies have somewhat restricted the scope of audit activities, particularly the number of comprehensive audits carried out. Audits of two statutory authorities were slightly delayed beyond the target completion dates due to staff vacancies and to pressure of work. I apologise to the respective Boards and management and I assure them that we will do all we can to meet their 1997 timetables. One planned study on grants to local organisations was not completed and will be included in the next report. It is interesting to note that the complement of the Audit Office has remained at 13 persons since 1986. During that period our workload has increased considerably, both in terms of the dollar value and complexity of transactions. As part of our own *Reinvention* exercise, I intend to carry out a thorough review of the work of the office, which will consider how we can best serve the interests of legislators and taxpayers, whilst assisting managers and the government to add value to government services.

Staff Movements

Mr R Roberts, Senior Auditor	Left the office in March 1997 on promotion to Internal Audit.
Mr I Perera, Senior Auditor	Left the office in June 1997 for a position in the private sector.
Ms S Ramsay, Auditor	Left the office in August 1996, for a position in the private sector.
Mrs J Williams, Auditor	Left the office in September 1996, on promotion to Treasury.
Mrs V Watler, Auditor	Retired in May 1997 after 29 years total service.
Ms W Bush, Auditor	Joined the office in May 1997 after college graduation.
Ms L Lawrence, Auditor	Joined the office in June 1997 after college graduation.

4.2 On the positive side, a new staff grading scheme for the Audit Office was introduced during 1996. The main objective of the scheme is to provide career opportunities for Caymanian personnel who have a long term commitment to the civil service. Graduate accountants will now be promoted to the AP1-2 scale upon completing three years satisfactory service and to the AP2-3 scale on completing professional qualifications. As I have said before, this scheme alone is unlikely to be sufficient to retain high calibre staff in the longer term. The civil service cannot compete with the private sector in terms of job opportunity.

Training

4.3 The Audit Office actively supports professional and technical training for all personnel. The Office participates in the regional training programme provided by the Caribbean Organisation of Supreme Audit Institutions (CAROSAI) with funding from the Inter American Development Bank. Government has also provided financial support for training and grants study leave to participants. Training activities during the year under review included:

Name	*Post*	*Training Activity*
N Esdaile	Auditor General	3 day "Transformation" course for senior managers (2)
D Welcome	Audit Manager	1 week training workshop, St Kitts (1) 3 day "Transformation" course (2)
K Jefferson	Audit Manager	1 week training workshop, St Kitts (1) 3 day "Transformation" course (2)
R Roberts	Senior Auditor	5 week financial and value for money auditing course, UK (2)
S Edwards	Auditor	CPA preparation (3)
D Wesley	Assistant Auditor	Level 2 AAT, Community College (2)

Notes:
(1) Sponsor: CAROSAI - Inter American Development Bank (IADB)
(2) Sponsor: Cayman Islands Government
(3) Sponsor: Officer

Computers

4.4 I am pleased to report that funds were allocated in the 1997 Budget for much needed computer equipment. This has enabled the office to replace obsolete computers, to add additional equipment and to standardise software packages with the rest of the civil service. This meets most of our present needs.

Reinvention of Government

4.5 A recent report by the United Kingdom National Audit Office (NAO)[3] revealed that of the 14 British Dependent Territories, only one (Cayman Islands) had up-to-date audited accounts and only three (including Cayman Islands) had fully functioning Public Accounts Committees. Cayman Islands also

[3] *Contingent Liabilities in the Dependent Territories*, HC 13 Session 1997-98, paragraphs 4.10 –4.12, Appendix I, 20

compares favourably with regional standards. Whilst this may help to place our financial and accountability performance in perspective, it does not mean we can be complacent. On the contrary, the *"Reinvention of Government'* programme presents an opportunity to improve budgeting and accounting for the taxpayers money.

4.6 Some of the broad objectives of public service reforms implemented elsewhere include:

- making public service managers more accountable
- establishing stronger incentives for good management
- developing reporting requirements which make good or bad performance clearly visible

Under our existing arrangements for financial reporting, the primary objective of managers is to keep within budget and to comply with financial procedures. There is only limited accountability in terms of outputs or results of programmes, and few valid assessments of economy, efficiency and effectiveness. In order to make informed judgements about the quality and affordability of services, both legislators and taxpayers need better financial and non-financial information, which links programme expenses with outputs and results. Several Commonwealth countries now focus much more on results and outcomes, rather than the amount of cash spent. Statements of service output and performance and cost statements analysed by output, objective or service have been introduced in several countries. There is also a trend to move away from the cash basis of accounting. My personal view is that the changes outlined above could help Cayman Islands government evolve into a results-oriented organisation. However any changes must be balanced with the principle that the legislative branch of government should be given every opportunity to exercise control and oversight of the Executive.

Acknowledgements

4.7 Once again I wish to record my sincere appreciation to all my colleagues in the Audit Office for their hard work and dedication in a difficult year. As usual I am pleased to acknowledge the continuing co-operation and support of Controlling Officers and their staffs.

N K Esdaile	Grand Cayman,
Auditor General	31 July 1997

Appendix A

Expenditure Details	Expenditure Charged To	Amount	Reason Why Auditors Considered Items Misclassifications
Payment for purchase of a TV and VCR.	06-002 Electricity	$1,317	The items bought are capital items and should not have been charged to this vote
Cost of cat and dog food.	03-011 Dietary/Food Supplies	$162	The vote is not intended to cover this type of expenditure.
Cost of purchasing bedroom, living and dining room sets.	08-038 Welfare Funds/Social Security	$3,293	It is incorrect to charge capital expenditure to a recurrent vote.
Cost of an electronic access system.	03-036 Printing - Other	$5,984	It is not appropriate to charge these costs to a printing vote.
Cost of a farewell party.	07-045 Miscellaneous Visits & Entertainment	$1,657	Funds are not placed in the vote for this purpose. Is this an appropriate use of public funds?
Payment for water usage.	06-006 Telephones	$72	There is no connection between the expenditure incurred and the ambit of the vote. The relevant Portfolio agrees this is a misclassification.
Accommodation, car rental and air travel costs.	41-104 Communication Equipment	$4,834	It is appreciated that these recurrent costs have been incurred because of a Capital project. It is inappropriate to charge recurrent expenditure to a Capital Vote.
Payment for salary and unused leave.	07-014 Professional Fees	$5,648	The payee is a former Civil Servant, not a consultant. The payment should not have been charged to this vote.
Costs of purchasing water.	03-032 Office Supplies	$260	The Department agrees that it is inappropriate to charge the expenditure to this vote but felt that all other votes were even more inappropriate.
Payment for muffler repairs.	07-080 Censuses & Surveys.	$110	It is inappropriate to charge this cost to the vote – there is no commonality between the expenditure and the ambit of the vote.

Expenditure Details	Expenditure Charged To	Amount	Reason Why Auditors Considered Items Misclassifications
Payment for water usage.	03-020 Fuel and Oil Supplies.	$208	The responsible Department accepts an error was made and requested that Treasury correct this by an appropriate Journal Entry. This was done in December 1996.
Cost of computer equipment Cost of computer equipment	07-007 Collateral and Photography. 07-073 Operating Expenses – Overseas Offices	$53,804 Paid direct US$49,834 Paid by DoT Miami	The Audit Office is of the opinion that it is incorrect to charge the cost of computer equipment to these recurrent expenditure votes. The Controlling Officer disagrees with the Audit Office's interpretation and has stated that Overseas Offices Operating expenses is meant to cover all overseas costs.
Costs of air travel (numerous transactions)	Various classifications in subheads 07 and 08	$41,536	Air travel costs should be charged to subhead 02 and not to Other Operating And Maintenance Services (07) or to Grants, Contributions and Subsidies (08)
Numerous charges for: Hotel expenses Car rentals	Various classifications in subheads 07 and 08	$9,338 $8,203	These expenses appear to relate to various tourism promotion activities
Costs relating to business lunches, parties, banquets, functions, &c.	08-906 Tourism Development Programme	$14,850	These amounts relate to entertainment costs. The Audit Office noted numerous additional payments of a similar nature, which were charged to other votes. The view of the Audit Office is that the expenses would be more appropriately described as entertainment or hospitality expenditure. The Controlling Officer does not agree.
Cost of computer network installation	07-073 Operating Expenses-Overseas Offices	$5,400	This is capital expenditure. It is incorrect to charge such costs to a recurrent vote.
Payment for production of a calendar.	07-061 Maintenance-Other Equipment	$11,400	It is clearly inappropriate to charge such costs to this vote.

Expenditure Details	Expenditure Charged To	Amount	Reason Why Auditors Considered Items Misclassifications
Donation made.	07-061 Maintenance-Other Equipment	$10,000	The donation was made to a non-governmental entity. It was not used to maintain equipment owned by Government; it should not be classified as Maintenance of Equipment.
Cost of special receptions, dinner, banquet and business lunches	08-032 Support Grants	$7,262	It is incorrect to charge such costs to Support Grants.
Cost of advertisements for temporary relief helpers for residential care.	03-015 Education Supplies	$736	It is incorrect to classify these costs under the Education Supplies vote.
Cost of trophies, nets and flags.	07-061 Maintenance - Other Equipment	$3,553	The expenditure incurred is not consistent with the vote to which it has been charged.
Cost of water usage.	07-038 Maintenance – Buildings	$875	This is clearly wrong
Payment for acting allowance.	07-014 Professional Fees	$5,210	The Controlling Officer instructed payment to be made from this vote because the Acting vote did not have sufficient funds. This is clear manipulation. A Supplementary or a virement request is the correct approach in this circumstance.
Salary	07-054 Public Relations and Publicity	$18,877	Salary costs should be charged to subhead 01.
Cost of office desk.	07-061 Maintenance -Other Equipment	$140	Purchase of an office desk cannot be maintenance of other equipment. The classification is therefore incorrect.
Cost of computer parts.	07-054 Public Relations and Publicity	$799	There is no logical connection between the expenditure and the vote to which it is charged; the classification is incorrect.
Cost of repairing sidewalk wheelchair ramp.	07-057 Security Services	$540	The relevant Department accepts this error. Auditors were told that the former Controlling Officer approved payment from this vote because there were no funds left in the vote used to cover repairs.

Expenditure Details	**Expenditure Charged To**	**Amount**	**Reason Why Auditors Considered Items Misclassifications**
Cost of a photocopier.	52-106 Construction of Roads	$10,812	This should be charged to the Office Equipment vote. The Department disagrees.
Cost of computer equipment and an airconditioning unit.	52-106 Construction of Roads	$15,577	It is inappropriate to charge the cost of computers and A/C equipment to a Roads capital vote. The Department disagrees.
Cost of servicing a fax machine.	07-014 Professional Fees	$382	Such costs cannot be regarded as Professional Fees.
Car rental charges.	02-015 Subsistence	$319	It is inappropriate to charge car rental hire to a subsistence vote. The responsible Department argues that they do not have a more appropriate vote to charge this to.