


Financial and Performance Reporting

Statutory Authorities and
Government Companies for
the year ending 30 June 2011





Our independent work
promotes good governance,
transparency and
accountability in the use
of public funds

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EXECUTIVE SUMMARY

I am pleased to present this report to the Legislative Assembly on the outcomes of the audits of the statutory authorities and government companies (SAGCs) for the year ending 30 June 2011. I believe that Members of the Legislative Assembly will find this report useful in their role to ensure financial accountability and transparency for Government operations.

The annual reports and financial statements of the individual entities of government are the key documents that enable the Legislative Assembly and the citizens of the Cayman Islands to hold ministries, portfolios, statutory authorities and government companies accountable for their use of public resources. In December 2010 I delivered my first report on the preparation and tabling of financial reports and over the subsequent two and half years I have provided the Legislative Assembly with reports on the progress that government and its related entities have made in preparing and tabling these fundamental accountability documents. A significant amount of time and resources was devoted by government and my Office to clear the backlog of prior year financial statements while undertaking audits of more current financial statements.

We have now reached a position where it is possible to begin reporting effectively in more detail on the outcomes of the audits at individual entities. This report is the first step in producing general reports each year on the outcomes of the most recent fiscal year. Whilst this report is focused on the SAGCs for the fiscal year ending 30 June 2011, I intend to issue a similar report for the ministries and portfolios in due course. Similar reports will be produced in future fiscal years and as the completion of entity financial statements continues to be more timely, I will be able to issue these reports to the Legislative Assembly closer to the fiscal year end.

With respect to the SAGC financial reports for the fiscal year ending 30 June 2011, I saw improvements in both timeliness and quality. However, whilst the story is one of progress, there is still a significant way to go before accountability as envisioned in the *Public Management and Finance Law (PMFL)* is effectively achieved. The picture across the individual entities is varied, with some performing very well while others are still struggling. In this report, I highlight some general concerns regarding the timely completion and publication of credible financial and performance information highlighted by finding that:

- the financial statements for only 8 of the 26 entities were completed in line with the statutory timetable, and 4 entities have still to be completed nearly two years after the fiscal year end;
- whilst a significant number of annual reports and financial statements have recently been tabled in the Legislative Assembly, there have been significant delays in tabling by the responsible ministries;

- a number of entities have only been tabling their financial statements in the Legislative Assembly and not annual reports discussing their wider performance as required under the PMFL; and
- significant weaknesses in the internal control environments and governance arrangements of certain entities.

Therefore, for progress to continue being made towards the ultimate objective of restoring accountability, I believe the Legislative Assembly has an important role to play to hold the administration to account by ensuring entities continue to improve the quality of their financial statement submissions and underlying information, and strengthen their internal control environments and overall governance arrangements. This report and future updates can provide Members of the Legislative Assembly with the means to do that.

I look forward to working with government and the individual entities as they continue on the path of improving financial reporting and restoring accountability for the use of public funds.

INTRODUCTION

1. Timely, accurate and reliable financial information is a fundamental component in ensuring the effective governance and accountability of government and public entities. Without this information, the decision making of the Legislative Assembly, the core government and public bodies is compromised as legislators and officials cannot make effective and robust decisions regarding the allocation of resources and effectively manage the resources at their disposal. Furthermore, the Government and public bodies cannot be held accountable for how they have used public money.
2. My Office has issued a number of reports over the last few years which have discussed the issues around financial and performance reporting across the public sector and the progress that had been made in clearing the backlog of financial statements and restoring financial accountability. These reports document the progress that has been made in financial reporting by entities, but at the same time highlight that there are still fundamental gaps in the accountability of government for the use of public resources and a significant way to go before financial accountability is restored.
3. The purpose of this report is to provide information about the status of financial reporting in statutory authorities and government companies (SAGCs) for the year ending 30 June 2011. This report contains the following:
 - a summary of the results of the audits for the 2010/11 financial statements of the SAGCs;
 - the key issues that have impacted the audit opinions I have issued on individual SAGC financial statements;
 - the status of outstanding 2010/11 financial statement audits; and
 - other significant governance, internal control and financial management issues that been identified through our audits of the financial statements and reported to the individual entities.
4. I plan to issue a similar report on the status of financial reporting in ministries and portfolios of core government in the next few months.

RESULTS OF THE 2010/11 AUDITS

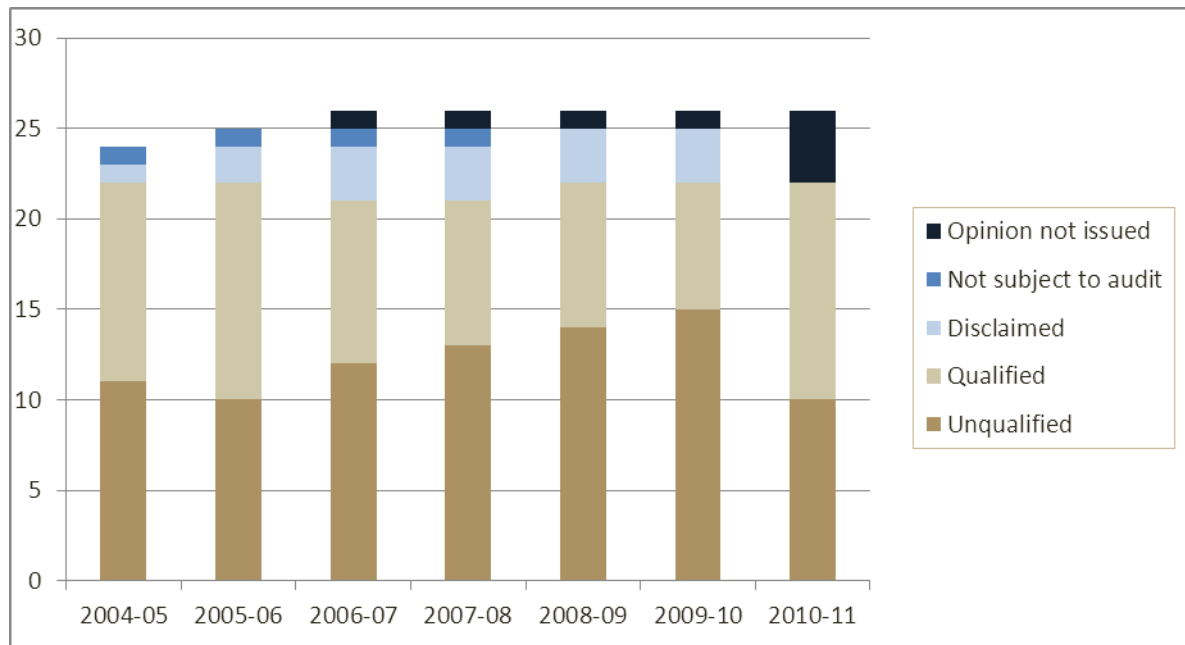
INTRODUCTION

5. At the date of this report, the audits of the 2010/11 financial statements for 22 statutory authorities and government companies (SAGCs) have been completed with four still outstanding. The four outstanding entities are:
 - Cayman Islands National Museum;
 - Cayman National Cultural Foundation;
 - Children and Youth Services Foundation; and
 - Sister Islands Affordable Housing Development Corporation.
6. Of the 22 audits completed, ten have received unqualified opinions, while the other twelve have received qualifications. Appendix 1 provides the detail of the audit opinions issued, the date they were signed and the date they were tabled in the Legislative Assembly if that has occurred. Appendix B provides definitions of the types of audit opinions I can give according to the *International Standards on Auditing* we follow.

QUALITY OF THE FINANCIAL STATEMENTS

7. The overall quality of the financial statements of the SAGCs continues to show improvements with respect to presenting fairly the financial results of the entities in line with the relevant accounting standards. I continue to see improved accounting practices, better supporting information and increased presentational quality.
8. Exhibit 1 below examines the trend in the opinions that my Office has issued since the introduction of the PMFL in 2004/05.

Exhibit 1: Statutory Authority and Government Company audit opinions



9. As shown in Exhibit 1, very few entities have received adverse opinions or disclaimers of opinion, with a general trend over time toward more unqualified audit reports. For 2010/11, there are no adverse opinions or disclaimers of opinion issued so far, with two of the entities that had previously been disclaimed (Health Services Authority and the Tourism Attraction Board) receiving a qualified opinion in 2010/11. There has been a decrease in the number of unqualified audits, with a corresponding increase in the number of qualified reports, caused by some specific technical issues which have been identified for compliance with accounting standards rather than a general decline in the quality of financial statements.
10. I continue to see a decline in the number and significance of the issues on which financial statements are being qualified. With respect to the 12 financial statements that were qualified, in eight instances the audit reports contained just one qualification. In most instances the qualifications were due to the lack of appropriate supporting information, not enabling me to reach a conclusion on a specific material balance or transactions. In two instances the qualifications related to disagreement on the classification of specific items. Exhibit 2 provides an analysis across the 12 entities of the qualifications on their audit reports.

Exhibit 2: Statutory Authority and Government Company Qualifications

	Past Service Pension Liability	Related Parties	Loan Classification	Property Plant and Equipment Equity	Cash and Cash Equivalents	Asset Impairment	Insurance premium Classification	Completeness of revenue	Completeness of receivables	Inventory	Compliance with IFRS	Opening Balances	Over-paid contributions
Cayman Airways Limited													
Cayman Islands Airport Authority													
Cayman Turtle Farm (1983) Ltd.													
Civil Aviation Authority													
Health Services Authority													
Information and Communications Technology Authority													
National Gallery of the Cayman Islands													
National Roads Authority													
Port Authority of the Cayman Islands													
Public Service Pensions Board													
Tourism Attraction Board													
Water Authority of the Cayman Islands													

11. The exhibit demonstrates that there are a variety of reasons for the qualifications, and further detail on the qualifications for each individual entity are discussed in the next section of the report. However it is worth noting that three qualification matters are more prevalent: past pension service liabilities; related party transactions; and completeness of revenues.

12. **Past Pension Service Liabilities:** SAGCs are required to recognize an amount for past service pension liability in their financial statements. However we were not able to quantify the liability as at 30 June 2011 as an actuarial valuation had not been completed for this date. As a result, for the five entities where this liability was material I was unable to determine if the amounts that were established as a past service pension liability were fairly stated in their financial statements and qualified my opinions accordingly. For three entities, this was the only qualification in their financial statements.

13. **Related Parties/Conflicts of Interest:** Accounting standards require the identification of transactions with related parties including the total amount of related party transactions and any outstanding balances at year end. This is to ensure that the entity's financial statements contain the disclosure necessary to draw attention to the possibility that its financial position and financial performance may have been affected by such parties.
14. We found that most entities did not have systems in place to effectively identify, account for and disclose related party relationships including transactions for board members and senior management in order to support compliance with the requirements of the accounting standards.
15. In addition, the lack of transparency around these transactions goes against the principles of good governance for managing conflicts of interests, and in some cases legislation, that require the proactive declaration of conflicts of interest.
16. In response to raising this issue during our audits, most entities requested board members and senior managers to declare related party interests for the reporting period, and put in place the requirements for annual declarations. However, in a few instances, board members refused to declare their interests resulting in a qualification of the audit opinions and raising concerns about potential business conflicts.
17. We will be following up on this significant issue in future audits to encourage entities to put into practice effective arrangements for the declaration and management of interests.
18. **Completeness of Revenues:** A number of entities derive a significant portion of their revenue through cash receipts (donations) that are not subject to the kind of controls that permit independent audit verification. Accordingly, the audits of these revenues were limited to the amount recorded in the accounts and I could not opine on how much should have been recorded.

MATTERS OF EMPHASIS/ OTHER MATTERS

19. I also included in my audit reports on the financial statements of eight entities a number of matters, which without further qualifying my opinion, I believed needed to be brought to the attention of the reader of the related financial statements.

20. Again there are a variety of matters that I have reported and details are discussed in the next section of the report for each relevant entity. However, one matter that I have raised in two entities was their inability to generate sufficient revenues to cover their expenditures and their dependency on funding from core government to continue operating as a going concern. While the financial statements of all SAGCs were prepared on the basis that they would continue to operate as a going concern, and no audit opinions were modified in regard to this; the audit reports for Cayman Airways and the Cayman Turtle Farm have highlighted their dependence on government support to continue operating. In addition I have also raised concerns about the ability of the Port Authority to continue operating as a going concern in the future without Government support.

OTHER SIGNIFICANT ISSUES

21. Whilst not directly affecting the opinions reached in my audit reports, I have also reported to the boards and management of the individual entities other important issues that I found during my audits requiring action to improve the governance, financial management and the control environment of the SAGCs. Details of my concerns are included from paragraphs 98 to 160.
22. It should be noted that an audit of financial statements is designed to enable an opinion to be expressed on the financial statements, and it is not designed to identify all matters or deficiencies in the internal control environment of audited entities. Accordingly, our audits do not ordinarily identify all such matters and those matters which we report to the entities are only those which came to our attention as a result of the performance of our audits.

TIMELINESS OF THE FINANCIAL STATEMENTS

23. I continue to see improvements in the timeliness of the provision of draft financial statements for audit and the related supporting information, which in turn is leading to improvements in the completion and certification of the financial statements.
24. For the 2010/11 financial statements, we received submissions by the 31 August deadline for all entities for the first time since the introduction of the PMFL. Whilst the quality and auditability of these initial submissions varied, this was a significant step forward. In terms of completion eight audits were completed by the statutory deadline of 31 October 2011, as compared to five for 2009/10, and by 31 December 2012, 21 audits were complete compared to 17 in the prior year, including all the significant and material entities. This is indicative of the continued improvement in the timeliness which directly relates to improvements in the quality of the submissions being made.

25. However significant improvement in the quality of submissions is still required if the objective of meeting the statutory timescales set out in the PMFL are to be achieved. Undoubtedly the backlog of financial statements continued to have an impact on the timely completion of some of the 2010/11 financial statements and issues around quality of initial submissions and supporting information also continued to have an impact. However I would expect the impact of these to diminish for 2011/12 onwards as the number of backlog financial statements becomes minimal.

ORGANISATIONAL CAPACITY

26. Organisational capacity of entities to produce compliant financial statements is a significant issue for a number of entities. As at 7 June 2013, the audits of four entities are still not completed and a major factor (as with a few others) is the ability to retain the resources with the necessary skills and expertise due to their size. Whilst I would expect that for the financial statements ending 30 June 2012 we will see further progress, I believe the scale and size of some of the entities will continue to impact on their ability to produce timely and reliable financial statements.

27. As a result it is my opinion that the Government needs to consider whether the organizational structure of public sector is appropriate, not just from the perspective of the producing timely and reliable financial information, but also from the perspective of efficient and effective service delivery.

DELAYS IN AUDIT COMPLETION

28. The timely issuance of financial statements is a critical element of good accountability by entities. As I noted in Appendix A, a significant number of our audits have been or will be signed off after the statutory deadline of October 31. While the results for 2010/11 represent an improvement on previous years, I am still concerned about the time it is taking between the date of audit work completion and the date of final sign off of the financial statements by management and the boards.

29. I expect management and boards to respond in a timely manner to our audit findings leading to more timely financial reporting. For future audits, I am looking for an improvement in the timeliness by which entities deal with the audit process to expedite the completion of their financial statements.

TABLING OF ANNUAL REPORTS

30. The final link in the accountability chain for the use of public resources from the initial approval of the budget in Legislative Assembly is the tabling of each SAGCs annual report, including their financial statements in the Legislative Assembly. It is only at this stage that the stakeholders, Legislators and citizens, can see how public resources have been used and hold Government and public bodies accountable.

31. As at the date of this report, the annual reports for only 15 entities have been tabled for the year ending 30 June 2011. 17 SAGC reports for prior years have also still to be tabled. This position is a significant improvement since my previous reports. However, in most cases where an annual report has been tabled for 2010/11 or the prior years, it is just the financial statements rather than the full annual report as required by the PMFL, and in all cases this has occurred, a significant amount of time after the financial statements were signed off.
32. The timely production and tabling of an annual report in the Legislative Assembly is probably the most fundamental element in the accountability framework for a public sector entity. Without this, the accountability of these entities for their performance and use of public resources is undermined. In effect, all the effort by the entities to produce and issue timely financial statements has little or no value if there is no way for legislators and the general public to understand what they mean and to assess how well the entity has performed.
33. In the future, as financial statements are signed off within the statutory timeframes, it is important that entities ensure that they are in a position to prepare an annual report which talks more widely about their operational and financial performance, as well as including their financial statements, and that these are tabled in Legislative Assembly in accordance with the timescales required in the PMFL.

ENTITY QUALIFICATIONS

34. In the previous section, I discussed the overall results of our audits for the 2010/11 financial year. This section provides further detail on the specific issues that resulted in qualifications for each individual entity along with any other matters that I brought to the readers' attention in the audit reports.

CAYMAN AIRWAYS LIMITED (CAL)

35. The opinion was qualified in respect of the misclassification of long terms loans. In addition the audit report included a matter of emphasis in respect of CAL's ability to continue operating as a going concern.
36. CAL was in breach of certain loan covenants during 2010 and 2011. The balances of the loans where breaches occurred were US\$30,803,892 at 30 June 2011, and US\$35,652,222 at 30 June 2010. The entity classified these loan amounts as long term liabilities.
37. In our opinion, this classification did not accord with accounting standards requiring their classification as current liabilities, because the breach of the loan covenants changed the classification to loans payable on demand. Furthermore, the accounting standards require the restatement of prior period errors and the resulting changes disclosed in the financial statements. The entity decided not to restate prior period financial statements.
38. The breach in these covenants has subsequently been resolved and at 30 June 2012, this qualification should no longer be required.

CAYMAN ISLANDS AIRPORT AUTHORITY (CIAA)

39. CIAA's opinion was qualified in respect of past service pension liability and related party transactions.
40. **Past Service Pension Liability:** Pension contributions for eligible employees of CIAA are paid to the Public Service Pensions Fund which is administered by the Public Service Pensions Board. CIAA is required to recognize its own portion of the past service pension liability from the date of incorporation. However, it was not able to quantify the liability as at 30 June 2011 as an actuarial valuation had not been completed for this date. As a result, it could not be determined if the amount of \$4,706,000 that CIAA has established as a past service pension liability in their financial statements was fairly stated.

41. **Related Party Transactions:** Accounting standards require the identification of transactions with related parties and disclosure of related party transactions and outstanding balances in the financial statements. This is to ensure that the entity's financial statements contain the disclosure necessary to draw attention to the possibility that its financial position and financial performance may have been affected by the existence of related parties and by transactions and outstanding balances with such parties. There was insufficient information provided to my auditors for complete reporting in the financial statements.

CAYMAN ISLANDS DEVELOPMENT BANK (CIDB)

42. CIDB's opinion was unqualified for the year ended 30 June 2011. However, without qualifying the opinion, I highlighted one matter for the attention of readers regarding future debt obligations.

43. The financial statements state that CIDB successfully negotiated with the bondholders for a US\$6m bond, which matured on 30 June 2010, to extend maturity for another 5 years. They also describe how CIDB refinanced a US\$20m bond originally due in July 2017 to a new credit facility which will be due in 2015. As a result of these actions, CIDB now has debt totaling CI\$30.5m which becomes due and payable in 2015. In my opinion, this amount of debt due and payable in 2015 will be a significant challenge for the Government to meet and puts at risk the ability for CIDB to be a going concern after 2015.

CAYMAN TURTLE FARM (1983) LTD. (CTF)

44. For the year ending 30 June 2011, the CTF's financial statements received a qualified opinion on 26 October 2011. The opinion was qualified on three matters:

- impairment of assets;
- pension payable; and,
- the treatment of insurance premium paid on behalf of the CTF.

45. A matter of emphasis was also included regarding the CTF's ability to continue operating as a going concern because of the funding arrangement with the owner, the Cayman Islands Government.

46. **Impairment of Assets:** Accounting standards require the disclosure of assets that may be impaired (i.e. subject to loss or devaluation). Due to the nature, size and complexity of the CTF's property, plant, equipment and exhibits, management could not estimate whether there was any indication of impairment to be recorded in the financial statements at 30 June 2011.

47. **Past Service Pension Liability:** The statement of financial position at 30 June 2011 includes an amount for pensions payable of CI\$1,022,000. This amount is based on the 30 June 2009 estimate provided by the actuary at the Public Service Pensions Board. In the absence of an actuarial valuation as at 30 June 2011, I was unable to opine on the amount for pensions payable in the financial statements.
48. **Insurance premiums:** From 2007 to 2011, the Cayman Islands Government, the sole shareholder, has paid insurance premiums on behalf of CTF in the amount of CI\$4.6 million which are recorded as liabilities in the financial statements at 30 June 2011. There is no agreed schedule of repayment and it is not possible to estimate when this amount will be repaid. These payments are, in my opinion, capital contributions according to the accounting standards as CTF does not have the ability to repay this obligation. Therefore, I reported that the classification of this amount as a liability in the statement of financial position at 30 June 2011 should be reported instead as a contribution from the shareholder and form part of equity.

CIVIL AVIATION AUTHORITY (CAA)

49. For the year ended 30 June 2011, I issued a qualified opinion with respect to the valuation of pension liabilities.
50. Pension contributions for eligible employees are paid to the Public Services Pension Fund which is administered by the Public Service Pensions Board. At the time of reporting, management of CAA was discussing their understanding of the particulars supporting the 30 June 2009 valuation recommended by the actuary. Management was not confident with the supporting information used to prepare the report and opted not to record the recommended liability of \$709,000 until the issue had been resolved. In the meantime, management obtained an estimated valuation for the 2011 year end which indicated the liability had increased to \$1,011,000.

HEALTH SERVICES AUTHORITY (HSA)

51. For the year ended 30 June 2011, I issued a qualified opinion on the financial statements on 17 October 2012. This is the first year since the introduction of the PMFL that I have been able reach an audit opinion on HSA's financial statements; in all prior years I have issued a disclaimer of opinion. In qualifying my opinion I identified four areas of concern.

52. **Ineffective internal controls over the completeness of patient revenues:** To ensure that all revenue is properly identified, invoiced and collected by the HSA, management is required to put in place appropriate systems, practices and internal controls. In doing so, management can be assured that all the revenues are recorded in the financial statements. We found that the internal controls to ensure the complete recording of patient revenues were not properly designed. As a result, management does not have assurance that all revenues are properly accounted for and were unable to demonstrate to my auditors, by way of the records being maintained, that the revenue amount of \$68.5 million was fairly presented because management could not tell us they were complete.
53. **Completeness and valuation of accounts receivable:** I was unable to determine the completeness and valuation of patient-related accounts receivable reported on the balance sheet for similar reasons as reported for patient revenues.
54. **Inability to audit year-end inventory:** When conducting an audit of the amount recorded as inventory in the financial statements, my auditors have to ensure that management can support the amount by a physical count of the assets themselves and appropriate documentation to support the valuation of the items. The inventory amount of \$6.8m in the financial statements at 30 June 2011 could not be audited because HSA could not provide sufficient and appropriate information regarding the individual items included in inventory and how much they are worth.
55. **Effect of issues related to prior year's financial statements:** For the five years leading up to the audit of the financial statements for 30 June 2011, my Office had not been able to conduct a full audit of the accounts resulting in the issuance of a disclaimer of audit opinion. As a result, I was unable to determine the accuracy of the accumulated deficit as reported in the balance sheet and the statement of changes in net worth.
56. The audit report also included an "emphasis of matter" discussing note 22 to the financial statements that describes the uncertainty of the valuation related to the HSA's post-employment health benefits. Starting in April 2010, the HSA has been paying the medical expenses for employees who retired and whose medical coverage was dropped by the Portfolio of the Civil Service (POCS). The continued payment of these medical bills constitutes what is known as a constructive obligation whereby the HSA may be liable for future medical bills of these retirees even though there is no decision by Government as to who should be liable for the medical costs of these retirees. There has been no liability estimated or recognized in the financial statements and the HSA is trying to engage an insurance company to provide coverage for the retirees' medical benefits. Subsequent to issuance of the financial statements, the Board made a policy decision that all new employees hired after 1 November 2010 would no longer be provided lifetime medical benefits.
57. Given the potential significance of this liability and its impact on the future operations of the HSA, we believe this situation should be resolved as soon as possible providing an opportunity to report an accurate liability amount on the financial statements.

INFORMATION COMMUNICATION AND TECHNOLOGY AUTHORITY (ICTA)

58. ICTA's opinion was qualified with respect to the valuation of past service pension liabilities. ICTA has one employee who is an active participant in the public service defined benefit plan and was unable to quantify and report the past service pension liability as at 30 June 2011.

MARITIME AUTHORITY OF THE CAYMAN ISLANDS (MACI)

59. Whilst I did not qualify my opinion on MACI, the audit report highlighted a contingent liability that I believe needed to be disclosed involving MACI's operations in the United Kingdom.

60. In my audit report, I indicated that there is uncertainty as to whether the MACI UK operations could be required to pay either corporation tax on any operating surpluses and/or VAT on services provided. This is based on a United Kingdom law requiring all foreign Governments that have revenue generating enterprises operating in the UK to pay corporation tax. If enforced, MACI could be liable for significant corporate taxes on its United Kingdom operations.

61. In my letter to those charged with governance at MACI, I have informed them that this matter needs to be resolved as quickly as possible in order for proper disclosure to be provided to the readers of the financial statements.

NATIONAL GALLERY OF THE CAYMAN ISLANDS (NGCI)

62. The NGCI opinion was qualified with respect to the amount reported for revenue as a result of control weakness around cash receipts.

63. The NGCI derives a significant portion of its revenue through cash receipts that are not subject to the kind of controls that permit independent audit verification. Accordingly, our audit of these revenues was limited to the amount recorded in the accounts and could not opine how much should have been recorded.

NATIONAL HOUSING DEVELOPMENT TRUST (NHDT)

64. Whilst I did not the qualify opinion of NHDT, I highlighted two matters in my report:

65. **Impairment losses:** The notes to the financial statements refer to a legal opinion regarding housing units held by the Trust that do not comply with the Land Registration Legislation. As a result, NHDT had sold and rented unregistered properties which were deemed unfit for habitation. This necessitated the evacuation and demolition of the housing units and a consequent reduction in the assets' value of \$5.8m.

66. **Procurement:** A total of 41 houses were constructed in East End and West Bay during 2010/11 at a cost of \$4.2 million. The Trust issued 41 individual contracts with the work being shared between 25 different contractors. The *Financial Regulations* prescribe that any contract with a value of \$250,000 or more should be reviewed and approved by a Tender Committee in the entity and submitted through the Central Tenders Committee. These construction projects were not submitted to the Central Tenders Committee for evaluation as breaking the project into multiple contracts resulted in the individual cost of each contract falling below the two hundred and fifty thousand dollars threshold.

NATIONAL ROADS AUTHORITY (NRA)

67. The opinion for the NRA was qualified with respect to related party transactions. The NRA did not have systems and practices in place to identify, account for and disclose related party relationships and transactions for all of its board members and senior management in order to comply with accounting standards and the principles of good governance.

68. As a result of our audit, management of NRA took action to comply with the accounting standard, however, due to the reluctance by a member of the Board to provide information about their activities, my opinion was duly qualified.

PORT AUTHORITY OF THE CAYMAN ISLANDS (PACI)

69. I issued a qualified opinion on 30 July 2012 in respect of related party transactions. The PACI did not have systems and practices in place to identify, account for and disclose related party relationships and transactions for board members and senior management in order to comply with accounting standards and the principles of good governance.

70. Without further qualifying my opinion, I also highlighted two matters in my audit report that I considered important for the readers of the financial statements:

- non-compliance with the *Port Regulations (2011 Revision)*, as the Authority was unable to charge tender fees totaling \$548,601 for the manifested cruise passengers as required by the Regulations due to an existing agreement with the FCCA which prohibits the Authority from unilaterally increasing fees; and
- the ability of the PACI to continue operating as a going concern.

PUBLIC SERVICE PENSIONS BOARD (PSPB)

71. I qualified the opinion of the PSPB as I was unable to effectively audit the overpaid contributions by members. In conducting my audit, I was unable to verify the amount reported for overpaid contributions amounting to approximately \$1.7 million due to a general lack of evidence including the absence of an adequate subsidiary ledger showing the amounts attributable to individual participants. As I was unable to perform alternative audit procedures to verify the amount reported which is material to the financial statements, I qualified my opinion.
72. Whilst my opinion was not qualified for any other matters, I also highlighted two matters for the readers of the financial statements in my audit report.
73. **Actuarial Valuation Report:** The notes to the financial statements indicate that the 2011 and 2008 actuarial valuation reports completed on April 2012 and March 2009 respectively were submitted to the Financial Secretary in April 2012 and April 2009. Neither report had been accepted and approved as at the date of the audit report and used by PSPB for reporting in its 2010/11 financial statements. This contravenes *Public Service Pensions (Amendment) Law, 2004* which states that:
- “After receiving a report under subsection (3) the Financial Secretary shall submit the report to the Governor and the Governor, shall either accept the report and approve, by regulations, the changes to the contribution rates recommended by the Board; or within 90 days of receiving the report, cause its own actuarial valuation to be carried out if it determines that there is good reason to do so.”*
74. We have been informed that both the 2011 and 2008 actuarial valuation reports have been taken to Cabinet for approval. However Cabinet deferred the relevant Cabinet papers and thus the reports have not been sent to the Legislative Assembly.
75. **Separate Accounting of Pension Funds:** The *Public Service Pensions Law (2004 Revision)*, *Parliamentary Pensions Law, 2004* and *The Judges’ Emoluments and Allowances Order, 2005* each state that
- “...the Board shall prepare and submit to the Auditor General in respect of that year a balance sheet and a statement of revenue and expenditure by the Board during the year; and such other financial statements as may be required...”*
76. The PSPB pooled the funds for each of the plans into one set of financial statements and did not identify or disclose the investments and administrative expenses for each Fund. In response to our concerns raised with PSPB, management stated that: *“the Passage of the Parliamentary Pensions Law in 2004 created the unintended effect of requiring the Board to prepare and maintain a distinct and separate set of financial statements for the Parliamentary Pensions Fund.”*

77. We believe it was the clear intent of these laws to have separate reporting of financial information for each Fund. Section 9 (3) of the *Parliamentary Pensions Law, 2004* and *The Judges' Emoluments and Allowances Order, 2005* and Section 11(3) of the *Public Service Pensions Law (2004 Revision)*, clearly details the Auditor General's responsibilities in relation to each Fund requiring an opinion be provided on separate sets of financial statements that disclose separately the assets, liabilities and operations of each Fund for transparency and accountability purposes.

TOURISM ATTRACTIONS BOARD (TAB)

78. I issued a qualified opinion on 6 March 2013. In the previous four years' I had issued disclaimers of opinion as I was unable to obtain sufficient information to audit and on which to base my opinion. The opinion was qualified in respect of six issues.

79. **Cash & Cash Equivalents:** Based on the omission of two bank accounts from the TAB's records as well as lack of supporting documentation related to these two bank accounts, my verification of cash was limited to the amounts recorded in the records of TAB. As a result, I was unable to opine on the completeness and accuracy of the cash and cash equivalents balance of \$1,332,367 at 30 June 2011.

80. **Property, Plant & Equipment and Depreciation:** No adjustments were made to the carrying value of the TAB's properties at 30 June 2011 to reflect the results of a revaluation conducted subsequent to the year end. Based on the valuation carried out, the potential understated differences to property values are in excess of \$1,000,000. Due to the significant differences noted, property, plant and equipment of \$9,323,386 are not fairly stated at 30 June 2011 and I was unable to opine on the accuracy of the associated depreciation expense of \$241,772.

81. **Equity:** Due to the significant unadjusted balances noted during the current year which impact on the accuracy of equity, the equity balance of \$10,055,634 was not fairly stated at 30 June 2011.

82. **Revenue:** Due to the lack of adequate controls over revenue transaction noted at Pirates Week and the Botanic Park as well as some revenue transactions not being recorded in the financial statements as a result of the omission of two bank accounts, I did not opine on the completeness and accuracy of gross revenues totaling \$683,957, out of the overall revenue balance of \$2,792,340 as at 30 June 2011.

83. **Receivables:** Based on differences noted of \$20,491 in addition to the control issues noted with revenue, I was unable to opine on the accuracy of the receivables balance of \$102,207 at 30 June 2011.

84. **Non-compliance with International Financial Reporting Standards (IFRS):** TAB did not fully comply with a significant IFRS standard, IAS 24 (Related Party Disclosures). The register of interests provided was incomplete and as a result I was unable to verify the completeness of the related party disclosure.

UNIVERSITY COLLEGE OF THE CAYMAN ISLANDS (UCCI)

85. UCCI's opinion was unqualified for the year ended 30 June 2011. However, without qualifying my opinion, the audit report highlighted information in the financial statements regarding an ownership issue for buildings and land.

86. The financial statements included the value of land and buildings used by UCCI for its operations. The disclosure in the statements would lead the reader to believe that UCCI owns the assets. We found that land and buildings are not technically owned by UCCI and remain registered in the name of the Crown. While it is a technicality as UCCI is 100% owned by the Cayman Islands Government, legally UCCI has no title to the assets and therefore, should not have the assets recorded in its financial statements. From a governance perspective, the management and the Board have no effective authority to authorize any transactions dealing with these assets.

WATER AUTHORITY (WA)

87. For the year ended 30 June 2011, the WA's opinion was qualified with respect to the amount reported for past service pension liabilities.

88. Pension contributions for eligible employees of the WA are paid to the Public Services Pension Fund. According to the accounting standards, the Water Authority is required to report a liability amount related to the past service pension of its employees from the date of incorporation. The WA, however, was not able to determine the amount of the liability as at 30 June 2011 as there was no actuarial valuation performed for this date. As a result, I was unable to determine whether the amount of \$1,172,000 reported as a past service pension liability in the financial statements for 2010/11 was fairly stated. The information reported in the financial statements for this liability was based on an actuarial report for the year ended 30 June 2010 and, therefore I was required to qualify my audit opinion.

OUTSTANDING AUDITS

89. With respect to the audits that are still outstanding, the continued delays in completing these audits effectively undermines the accountability of these organisations for their use of public funds. The details on the position and issues for each entity are described below. However, these are all small organisations, which have had difficulty engaging appropriate accounting staff to enable the efficient preparation of their financial statements and which have led to significant delays in their audits being completed.

CAYMAN ISLANDS NATIONAL MUSEUM (CINM)

90. At the date of this report, CINM's financial statements for the year ending 30 June 2011 are subject to ongoing audit. The audit is being conducted concurrently with the audit of the financial statements for the year ending 30 June 2012. It is expected that the financial statements for both years will be completed by 30 June 2013.

91. The audits for the previous five years up to the year ending 30 June 2010 have now been completed with audit reports issued. For all five years, I have issued a disclaimer of opinion mainly due to a lack of supporting information, but also due to inherent weaknesses in the internal control environment for controlling revenue. As a result of these concerns, it was not possible to reach an opinion on the accuracy, completeness and existence of the underlying financial transactions and balances. As a result, accountability for the CINM has been effectively undermined and the lack of controls and records has created significant risks of fraud and error.

CAYMAN NATIONAL CULTURAL FOUNDATION (CNCF)

92. At the date of this report, CNCF's financial statements for the year ending 30 June 2011 are subject to an ongoing audit. The audit is being conducted concurrently with the audit of the financial statements for the year ending 30 June 2012.

93. The audits of the financial statement up to the year ending 30 June 2010 have been completed. The audit reports for the last five years have been qualified in respect of the amounts reported for revenues. CNCF derives a significant portion of its revenues from various sources (donations), the completeness of which is not predisposed to independent audit verification because of a lack of controls. Without changes in how the entity collects its revenues, audit reports on the financial statements for 2011 and in the future will be qualified in this respect.

CHILDREN & YOUTH SERVICES FOUNDATION (CAYS)

94. At the date of this report, CAYS' financial statements for the year ending 30 June 2011 are still being audited. I have issued audit reports on the financial statements up to 30 June 2010.
95. My Office has issued qualified reports for the last six years. For 2010 they were qualified in respect of revenues and pension liabilities:
- CAYS derives a significant portion of its revenues from various sources (donations), the completeness of which is not predisposed to independent audit verification because of a lack of controls. Accordingly, our audit of revenues was limited to the amounts recorded; and
 - at the date of my audit report, the defined benefit pension asset and liability of CAYS' defined benefit pension plan was not known, as an actuarial valuation had not been completed, and no amount had been recorded in the financial statements.
96. In all likelihood, the audit report on CAYS' financial statements for the year ending 30 June 2011 will be qualified in respect of these issues.

SISTER ISLANDS AFFORDABLE HOUSING DEVELOPMENT CORPORATION (SIAHDC)

97. We received draft 2010/11 financial statements along with the previous four years on 31 August 2011 for SIAHDC. As a result of delays in receiving the supporting records and awaiting a policy decision by the Board regarding the requirement for the years up to 30 June 2008 to be audited, we are still in the process of conducting the audit of all five years' financial statements concurrently.

OTHER SIGNIFICANT ISSUES

INTRODUCTION

98. Whilst not directly affecting the opinion reached in my audit report, I have reported to the boards and management of the individual entities, other significant underlying issues which impact good governance, good internal control, and effective financial management and reporting, and which also have the potential to significantly impact the efficient use of resources and the achievement of results.
99. Before providing details of the other significant issues identified in our audits of each individual entity, I wish to highlight two common themes across our audits:
- Governance: unclear role of boards and management; and
 - internal control weaknesses.

GOVERNANCE – UNCLEAR ROLE OF BOARDS AND MANAGEMENT

100. For entities to function effectively and be well governed, boards and executive management need to have a good working relationship based on clearly delineated roles and responsibilities. The quality of the financial statements and its underlying transactions depends heavily on an organization having a good governance framework.
101. In our audits, we found there was an unclear understanding between the role of the board and executive management. Boards should provide strategic direction, approve policy, provide effective oversight, and hold management to account for the efficient and effective operation of the entity. Executive management, on the other hand, is responsible for managing the operations of the entities respecting the established policies, and being accountable to the board for their actions.
102. We found examples where the boards are getting involved in the day-to-day operations of the entities, rather than letting the executive management run the business for which they are remunerated, or instances where the working relationship between the board and management are strained. These kinds of issues have a negative impact on entities and their ability to deliver effective and efficient services/activities.

103. I also have significant concerns about how boards are appointed and members are chosen for various roles that they are required to perform. While these issues undermine the fundamental ability for SAGCs to operate effectively, and in compliance with their legal and fiduciary duties I will be discussing these concerns in other reports on governance.

104. The lack of clarity between the roles of boards and management is a key indicator of poor governance of the SAGCs which can lead to higher risks of mismanagement (including fraud and corruption), poor internal controls, and lower quality external reporting including substandard financial reporting.

INTERNAL CONTROL WEAKNESSES

105. A robust internal control environment is a critical component in organizations that ensures management can provide assurance to their boards regarding the:

- effectiveness and efficiency of operations;
- responsibility to safeguard assets;
- reliability of information in financial reports; and
- compliance with applicable laws and regulations.

106. In paragraphs 107 to 160 I report on a significant number of internal control weaknesses in most of the entities we have audited. Many of the issues we have identified are remediable if the organizations spent the time necessary to ensure their internal control framework was properly implemented and operating effectively.

SIGNIFICANT ISSUES AT INDIVIDUAL ENTITIES

107. For each individual statutory authority and government company, this section of the report provides information about other significant issues we identified through our audits, but which did not impact on my audit reports contained in the respective financial statements. The issues reported in this section were reported to the boards' and management of the individual entities through a governance report or other means. Not all of the issues reported to individual entities are included in this section, only those which we believe are significant, and I have not included issues relating to audits for those entities that have yet to be completed.

108. It should be noted that an audit of financial statements is designed to enable an opinion to be expressed on the financial statements, and it is not designed to identify all matters or deficiencies in the internal control environment of audited entities. Accordingly, our audits do not ordinarily identify all such matters and those matters which we report to the entities are only those which came to our attention as a result of the performance of our audit.

109. In addition for five entities, our audits did not identify any issues that were significant enough to be included in this report. These were:

- Cayman Islands Monetary Authority;
- Cayman Islands Stock Exchange;
- Electricity Regulatory Authority;
- Public Service Pensions Board; and
- Segregated Insurance Fund.

CAYMAN AIRWAYS LIMITED (CAL)

110. The report to those charged with governance identified material weaknesses in the internal control environment that need to be addressed. Whilst the audit identified a significant number of individual internal control issues, I have summarized them into two main concerns.

111. **Material weaknesses related to financial controls:** We found a significant number of internal control weaknesses across nearly all financial systems, including:

- reconciliations, including basic bank reconciliations, not being performed on a regular or timely basis. Many reconciliations were performed because the auditors requested them, whereas they should be prepared regularly to provide management with assurance that the systems and practices operated by the entity are working effectively;
- a lack of segregation of duties relating to the processing of journal entries, expenses or certain aspects of the payroll process; and
- general lack of evidence of monitoring and review by senior management that the internal controls of the organization are working effectively.

112. The totality of these individual weaknesses equates to a material weakness in the processing of financial transactions. The pervasive nature of these weaknesses resulted in one large audit adjustment and a number of unresolved accounting differences partly due to issues in prior periods. In addition to the risks of losses due to fraud and error, there is also the risk that management reports used for decision making by senior management, the board and legislators may contain erroneous information and that inappropriate decisions are taken.

113. CAL management has indicated that it has subsequently taken action to address these issues and there have been notable improvements in the control environment, in particular around the lack of reconciliations and the monitoring and review of the financial reporting controls by management. Work from the 2012 audit is also indicative of internal control improvements and this will be reported on in due course.

114. **Material weaknesses concerning the establishment of information technology (IT) governance, and IT related policies, controls and procedures:** For an entity with the size and complexity of CAL, we would expect that there be a comprehensive risk assessment done for the operations of its IT environment and that the risks identified are effectively managed and monitored on a regular basis. CAL has not done this. As a result, the required policies, controls and procedures related to its IT control environment have not been fully developed and implemented.
115. We also found a multitude of weaknesses related to the IT control environment that could result in significant errors occurring in the processing of financial and non-financial transactions. Examples of findings include:
- programming changes to information systems are not formally documented, properly tested, or approved by management prior to being implemented. This increases the risk that any programming changes could have a negative impact on system operations resulting in problems with data integrity; and
 - an appropriate segregation of duties has not been established for the operations of the IT systems. We found that in many cases, individuals were given access to IT systems that would increase the risk of fraudulent, inappropriate or unauthorised transactions being processed.
116. The failure to identify and manage IT risks and the resulting lack of IT policies, controls and procedures significantly increases the risk that the transactions processed and the data stored by information systems is inaccurate and unreliable. In addition, there is a high risk of fraudulent transactions being processed by the entity or data being fraudulently manipulated.
117. For an organization with such a large number of significant business risks to manage, I am concerned about the issues identified. I do note, however, that the airline's operations are regulated and audited by the Civil Aviation Authority of the Cayman Islands, the United States Department for Transportation, the United States Federal Aviation Authority, the United States Transportation Safety Authority and other international regulators. Nonetheless, I have taken note of these matters for a more in-depth performance audit of the operations of CAL in the future.

CAYMAN ISLANDS AIRPORT AUTHORITY (CIAA)

118. **Governance:** CIAA's Board of Directors ("the Board") is responsible for the organization's operations and its results. Our expectation is that, in line with good governance practices, that the board would be responsible for assessing the risks of the organization, setting the strategic direction, approving plans and policies and providing effective oversight of the executive management and holding them to account. Executive management, on the other hand, should be responsible for the operational activities and report to the Board.

119. We found that the Board was operating in a capacity beyond the oversight role described above. For example:

- board members sitting on an interview panel to recruit employees at a grade level below senior management;
- board members participating on project evaluation committees for procurement;
- approving application(s) for businesses to operate at the airports; and
- approving decisions for the disposal of equipment and the hiring of personnel.

120. The actions noted put at risk the efficient and effective operations of the entity and provide a significant opportunity for corrupt practices to exist.

121. Furthermore, I have identified issues regarding the appointment of board members and the lack of procedures in place to ensure the effective management of conflicts of interest. I am concerned that an entity with such significant legislative responsibilities as the CIAA has been operating outside the realm of acceptable governance practices.

122. **Non Compliance with Financial Regulations:** We identified two instances of non-compliance with the *Financial Regulations* relating to procurement. They were:

- a project for the installation of a card access system with a value of \$78K was awarded without being tendered; and
- an emergency project was undertaken where a contract was entered into with a sole source supplier due to exceptional circumstances after one of the two companies contacted declined verbally. The *Financial Regulations* require that a copy of the contract be forwarded to the Director of Internal Audit and the Auditor General, which did not happen.

123. **Leases:** A number of lease agreements relating to office/shop rentals at the Owen Roberts International Airport were not properly put in place, exposing the CIAA to the risk of lost revenues.

CAYMAN ISLANDS DEVELOPMENT BANK (CIDB)

124. **Board of Directors acting in an administrative role:** In 2009/10, the Chairman of the Board approved a Financial Stimulus Loan in the amount of \$131K that had a shortfall in the life insurance coverage of 62%. The loan was not supported by the General Manager as the customer had a poor payment history. During 2010/11, the loan was converted to a business loan and increased to \$329K to facilitate a payout to other financial institutions of \$170K (consolidating external loans), despite the former loan being 5 months in arrears. This was approved by the Chairman. The total debt service ratio of the new loan was 53%, which is 8% in excess of the CIDB normal lending ratio of 45% and a credit reference check also revealed poor credit worthiness. The conditions stated on the appraisal form were also waived by the Chairman on the offer letter.

125. A charge of \$136K was registered on a property with value of only \$132K. The CIDB standard / official practice is to register a maximum charge of 90% of property value. As at May 2012, the loan was 183 days in arrears.

126. The overrides by the Board chairman were not in line with CIDB policy and resulted in CIDB being exposed to a significant loss.

127. **Political interference in the operations of CIDB:** A customer that did not meet CIDB's credit criteria, was granted a loan in the amount of \$232,500 as a result of requests made by several Members of the Legislative Assembly and the Chairman of the Board that "the loan be favorably considered".

128. **Breaches of the CIDB's credit policies:** The Bank's credit policies, approved by the Board of Directors, are designed to ensure that loans are only disbursed to customers who are credit worthy. When a breach occurs this exposes CIDB to increased risk of losses due to delinquency. We identified a number loan disbursements where the Bank's credit policy was breached. The following examples were noted:

- the established credit policy for the granting of loans with maximum "Total Debt Service Ratio" of 45% was disregarded on a number of occasions without documentation of rationale;
- while credit checks revealed that a customer had a loan at another financial institution that was 78 days in arrears at the time the loan application was being considered and was found to have had negative net worth, a loan in the amount of \$36,000 was still granted on a customer's verbal statement that he could repay the loan;
- incremental loan granted to a customer without any corresponding increase in collateral held as security; and
- missing documentation on two loan files including applications and offer letters .

129. Management have subsequently indicated that policies have been established to mitigate against the issues identified, and the results from our 2012 audit, which will be reported in due course, indicate that similar issues have not been identified during the course of our work.

CAYMAN TURTLE FARM (1983) LTD. (CTF)

130. **Discharge Permit:** The CTF has failed to meet the reductions to its effluent discharge as required under its discharge permit from the Water Authority.

CAYMAN ISLANDS NATIONAL INSURANCE COMPANY (CINICO)

131. **Risk assessment and analysis policy:** As an insurance company, CINICO has certain requirements set out by CIMA. At 30 June 2011, CINICO did not implement a risk assessment and analysis policy required by CIMA legislation. Subsequent to our audit, a draft policy had been prepared but not yet approved by the Board of Directors.

CIVIL AVIATION AUTHORITY (CAA)

132. **Dividends:** As required by the *Civil Aviation Law 2005*, CAA is to make an annual payment to core government related to its profits and calculated according to a prescribed formula. For 2010/11, CAA recorded an amount of \$1.0 million which was not calculated according to formula. CAA was waiting at the time of our audit to have further discussions on the formula.

133. **Non-compliance with *Financial Regulations*:** The *Financial Regulations (2010 Revision)* require all procurements over \$50,000 to be subject to tender. During the reporting period, CAA negotiated and approved a contract for approximately \$96,000 with Brac Informatics which did not go through a competitive tendering process. There was not sufficient and appropriate documentation provided to support Brac Informatics as a sole provider of the services as provided for in the *Financial Regulations*.

134. Whilst the actions of CAA may well have been appropriate, a business case setting out the circumstances and justification for using a sole supplier should have been clearly documented and a copy of the contract should have been provided to the Director of Internal Audit and the Auditor General.

HEALTH SERVICES AUTHORITY (HSA)

135. **Accounting system weaknesses:** The HSA was unable to substantiate an asset account with a balance of \$60,000 as of 30 June 2011 consisting of purchase orders for goods and services not yet received. In addition, the IRIS accounts receivable module is incapable of providing sequential numbering for HSA specific customer invoices. We also noted differences between the trade payables per IRIS general ledger and the sub ledger.

136. **Inventory system weaknesses:** HSA uses Encom as its inventory management system for its inventory valued at \$6.8m as of 30 June 2011. The audit team and HSA management have identified various weaknesses exhibited by this system and management intends to replace it in 2012-13. Some of the concerns I raised include weak user profiles which leaves the system vulnerable to unauthorized entry or deletion of transactions and weak database management which would affect accuracy of information produced by the inventory system. We also noted that HSA over relied on one consultant who has expertise on querying the system which poses a business continuity risk should the consultant be unavailable.

INFORMATION COMMUNICATION AND TECHNOLOGY AUTHORITY (ICTA)

137. **Non-compliance with Licensee Fee Regulation:** ICTA regulations state that a licensee shall deliver full audited financial statements to the ICTA within three months of the end of the licensee financial year. We found that only six of the fifteen (40%) licensees submitted this information to ICTA. Failure of the licensees to deliver audited financial statements in the stipulated time set by the Authority is in contravention to the terms and conditions of their licenses. Without audited financial statements from the licensees, ICTA is unable to determine whether it is receiving appropriate license fees due to them and Government for royalty fees.

MARITIME AUTHORITY OF THE CAYMAN ISLANDS (MACI)

138. We identified a number of issues in our report to those charged with the governance that require management to address. Apart from the potential liability relating to the MACI UK operations other matters mentioned included the need for improved foreign exchange management, accounting system enhancements and the formalization of policies and documents with regard to related parties, write-off of accounts receivable and the need for more rigour around the UK salary contracts.

NATIONAL DRUG COUNCIL (NDC)

139. The most significant issues raised in my letter to those charged with government were related to NDC's ability to present meaningful financial statements in a timely manner. In prior years the Council employed a full-time or a part-time Administrative Finance Officer who had limited experience in preparing financial statements. Coupled with weak internal controls, processes and procedures, this led to significant issues in the ability for NDC to prepare financial statements, and challenges in carrying out our audits. In the absence of a full-time or a part-time Administrative Finance Officer in 2012, the NDC employed the services of an accounting firm to assist in bringing the outstanding audit matters up to date, reconstruct the accounts and prepare the financial statements.

NATIONAL GALLERY OF THE CAYMAN ISLANDS (NGCI)

140. The report to those charged with governance identified a number of internal control issues requiring management's attention. Some of the more significant internal control issues include poor monthly bank reconciliations, improper recording of income and expenses for the capital project, in-kind donations not being recorded, and poorly prepared financial statements resulted in a number of errors and adjustments by the auditors.

NATIONAL HOUSING DEVELOPMENT TRUST (NHDT)

141. **Directors Fees:** Directors fees rose to \$110,000 during 2010/11 from \$49,000 a year earlier with meetings conducted more than four times a month. The amount paid to directors was increased by 100% to \$800, \$400 and \$300 per meeting respectively for the Chairman, Deputy Chairman and other Directors by way of a resolution of the Board.

142. During our audit, we identified directors were overpaid in the amount of \$18,700 due to payment of fees at an incorrect rate. This amount included overpayment subsequent to the audit year and related to fees paid to the former Chairman and Deputy Chairman.

143. **Management of Accounts Receivable:** As at 30 June 2011, the NHDT had outstanding receivables of \$1.1 million, the majority of which related to outstanding rental and mortgage payments. During the year, management reviewed the provision for doubtful accounts and increased the amount by \$284,000 to \$607,000. On this basis, the net amount that NHDT expects to recover on these outstanding receivables is only \$499,000, which is a recovery rate of 45%. There were no receivables written-off during the year, however in the prior year the Trust wrote off nearly \$300,000 in outstanding debts.

144. **Segregation of duties:** We found that the same person prepares, reviews and approves the bank reconciliation statements. Likewise the same individual was responsible for taking cash receipts, making the deposits and accessing the accounting records. The lack of segregation of duties for these key activities unnecessarily increases the risk of employee fraud significantly.

145. NHDT management has indicated that it has recently taken action to address the issues in its control environment and this will be reported on in due course as the audits for 2012 and 2013 are completed.

NATIONAL ROADS AUTHORITY (NRA)

146. **Segregation of duties:** We found a number of instances where there was virtually no segregation of key operational duties needed to reduce the risk of employee fraud and error.

147. **Payments made outside the Payment Cycle:** We identified instances of payments being made outside of the established NRA payment cycle and authorised by individuals without the appropriate authority.

148. The findings from our 2012 audit did not identify any repetition of these internal control weaknesses.

PORT AUTHORITY OF THE CAYMAN ISLANDS (PACI)

149. **Hiring of employees:** Two employees were documented as being hired as a result of instructions from the then Premier, Hon. McKeeva Bush. The employees were initially hired in January 2004 under his instruction at a time when he was Chairman of the Board of Directors. Their duties were to install and maintain a buoy system used to control access of boats on top of the North Sound Stingray Sandbar, as well as to monitor the activities of boaters in the area and report on non-compliance with rules. In 2005, the two employees were terminated. In June 2009, the Premier verbally instructed the Port Director to reinstate the arrangements with the same two individuals at a rate of pay of \$1,000 per month. Up to February 2012, a total of \$90,000 had been paid to these individuals without any evidence of work being done.

150. Senior management informed my auditors that the installation of the Buoys was never completed and no report of any kind has ever been filed.

151. Management is responsible for the employment practices of PACI. Board members and politicians should have no role to play. The action identified above is a clear example of undue political influence and override that undermines the ability of an organization such as PACI to operate effectively.

152. **Compliance with the Port Authority Law (1999 Revision) and Regulations (2011 Revision):** The Port Authority Law needs to be amended and brought in line with current day practices. For example: the fiscal year being used is not consistent with the Law. Other examples include the accounting for and remittance of profits to core government, the activities related to the development of real estate and commercial activity, and several fees being charged.

153. **Management of commercial leases:** There is a lack of policies and procedures regarding how tenants are contracted. In addition, we noted several discrepancies in how rental agreements are managed and the enforcement of the contractual terms and conditions.

154. **Board members involved in contract negotiations:** We noted instances where members of the Board of Directors acted as agents in contract negotiations. In one instance, for example, we noted that the Chairman of the Board signed a Service Level Agreement (SLA) for the repairs of the Port Authority's facility and then directed it to the Port Director who signed it a day later. We reported to PACI that the practice of having Board members involved in the operations of the entity is inappropriate and creates considerable additional unmanaged reputational risks for this important public sector organization.

155. **Procurement of goods and services:** We found that PACI purchases most of its parts and supplies through sole source contracts without going through appropriate tendering processes.

TOURISM ATTRACTION BOARD (TAB)

156. The main issues that have been included in the report to those charged with governance are adequately covered by the qualifications on the audit report highlighted in paragraphs 78 to 84. The only further comment I would make is that the internal control environment within the TAB is seriously deficient, and there are significant risks of fraud and error as a result, particularly with respect to revenues.

UNIVERSITY COLLEGE OF THE CAYMAN ISLANDS (UCCI)

157. **Uncollected tuition fees:** When we analyzed the tuition fees revenue outstanding (uncollected) at year-end, we found that approximately 85% of the amount was over 90 days in arrears. This is an increase from prior year when it was 78% of the total amount. While management indicated to us that they have made extra effort to collect on these overdue accounts, it appears that their efforts are not having the desired effect. We recommended that management review and amend their collection strategy.

158. **Uncollectable accounts receivable:** At 30 June 2011, we noted that there is an amount of \$211,390 included in accounts receivable carried forward from 2008 related to a former UCCI President. This amount, while not material enough for me to qualify my opinion, is uncollectable and should be written off.

WATER AUTHORITY (WA)

159. **Non-compliance with legislation:** The Water Authority follows the International Financial Reporting Standards (IFRS) as the basis to prepare its financial statements. This is consistent with the *Water Authority Law (1996 Revision)* which indicates the accounts should be prepared "in a form which shall conform with the best commercial standards...".

160. The *Water Authority Law (1996 Revision)* indicates that “any balance of account in favour of the Authority after provision for all expenditures provided by subsection (2) up to an annual amount to be prescribed in regulations may be transferred forward to a general reserve fund, and any balance in excess of that sum paid into the general revenue of the Islands”. At present there is no general reserve fund or amount prescribed in regulations up to which balances can be transferred to such a fund. The WA only transferred \$50,000 to core government on operating profits of \$8.2m and is potentially not in compliance with the Law.

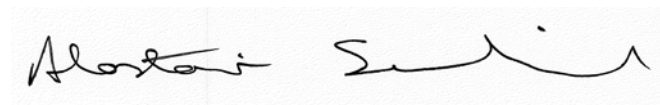
CONCLUSION

161. This report provides a summary of the outcomes from our audits of the statutory authorities and government companies of the Cayman Islands Government for 2010/11.

162. Whilst I continue to see improvements in the quality and timeliness of the financial statements for the SAGC's a lot more work is required before effective financial accountability for the use of public resources is restored across all entities. In particular I have ongoing concerns about a number of the smaller entities that continue to struggle to present reliable and credible financial statements for audit.

163. There is also still considerable room for improvement in the governance, internal controls and financial management of most entities. I believe there is key role for officials in core government to provide leadership across the entire public sector around these matters, and support the effective management of the public resources made available for the operations of these entities.

164. A number of matters I have raised in the conduct of my audits, such as the breakdown of governance, are very significant. I believe the Legislative Assembly should act to ensure SAGCs take action to mitigate the risks and opportunities for loss or abuse in the use of public resources.



*Alastair Swarbrick MA(Hons), CPFA
Auditor General
George Town, Grand Cayman
Cayman Islands*

11 June 2013

APPENDIX A – STATUS OF THE 2010/11 AUDITS

Entity	Date Audit Completed or Progress	Audit Opinion	Tabled in the Legislative Assembly
Cayman Airways Limited	13 July 2012	Qualified	13 March 2013
Cayman Islands Airport Authority	30 July 2012	Qualified	10 Jan 2013
Cayman Islands Development Bank	28 September 2012	Unqualified	14 March 2013
Cayman Islands Monetary Authority	31 October 2011	Unqualified	4 April 2012
Cayman Islands National Museum	In progress		
Cayman National Cultural Foundation	In progress		
Cayman Islands Stock Exchange	14 December 2011	Unqualified	13 March 2013
Cayman Turtle Farm (1983) Ltd.	26 October 2011	Qualified	10 Jan 2013
Children & Youth Services Foundation	In progress		
CINICO	19 June 2012	Unqualified	13 March 2013
Civil Aviation Authority	28 October 2011	Qualified	
Electricity Regulatory Authority	31 October 2011	Unqualified	
Health Services Authority	17 October 2012	Qualified	13 March 2013
Information and Communications Technology Authority	19 October 2011	Qualified	
Maritime Authority of the Cayman Islands	28 February 2012	Unqualified	13 March 2013
National Drug Council	31 October 2012	Unqualified	
National Gallery of the Cayman Islands	3 May 2012	Qualified	
National Housing Development Trust	28 June 2012	Unqualified	5 Nov 2012
National Roads Authority	24 October 2011	Qualified	31 August 2012
Port Authority of the Cayman Islands	30 July 2012	Qualified	
Public Service Pensions Board	28 June 2012	Qualified	5 Nov 2012
Segregated Insurance Fund	31 October 2011	Unqualified	13 March 2013
Sister Islands Affordable Housing Development Corporation	In progress		
Tourism Attractions Board	6 March 2013	Qualified	
University College of the Cayman Islands	19 October 2012	Unqualified	15 March 2013
Water Authority of the Cayman Islands	26 October 2011	Qualified	13 March 2013

APPENDIX B - AUDIT OPINION DEFINITIONS

The opinions that I can render on an entity's financial statements and their definitions are as follows:

- **Unqualified** - The information contained within the financial statements can be relied upon;
- **Qualified** - A qualified opinion means that a portion of the financial statements cannot be relied upon, but that the rest of the statements can be relied upon by the reader;
- **Adverse** - There are such significant deficiencies with the information in the financial statements they should be considered unreliable for the user and the information contained therein is not trustworthy; and
- **Disclaimer** - I was not provided with sufficient information to conduct an audit.

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Complaints

To make a complaint about one of the organisations we audit or about the OAG itself, please contact Garnet Harrison at our address, telephone or fax number or alternatively email: garnet.harrison@oag.gov.ky

Freedom of Information

For freedom of information requests please contact Garnet Harrison at our address, telephone or fax number. Or alternatively email: foi.aud@gov.ky

Media enquiries

For enquiries from journalists please contact Martin Ruben at our phone number or email: Martin.Ruben@oag.gov.ky



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