



**AUDIT CERTIFICATE OF THE AUDITOR GENERAL  
ON THE ACCOUNTS OF THE REPUBLIC OF NAURU  
FOR THE YEAR ENDED 30<sup>TH</sup> JUNE 2016**

I have examined the Annual Financial Statements of the Republic of Nauru as at 30<sup>th</sup> June 2016, as certified by the Minister for Finance and transmitted to me under Section 10(1) of the Audit Act 1973.

**Basis of Disclaimer:**

I have not been able to confirm the opening balances of substantial number of account heads due to wrong adoption of figures which were not rectified despite repeated audit requests. The Financial Statements submitted for audit are incomplete in many respects. Large number of significant account balances showed substantial differences between the Financial Management Information System (FMIS) and Financial Statements. A large number of account balances are not available in the FMIS module as they are yet to be set up in the system. The financial statements prepared are also not in full compliance with the accounting standards (IPSAS) adopted.

Details of Audit performed may be referred to in the management audit report appended.

**Disclaimer:**

Based on the audit work performed, and because of the significance of the matter noted in the Basis of Disclaimer paragraph above, I am unable to and therefore do not express an opinion on the true and fair view of the Republic's Annual Financial Statements as at the 30<sup>th</sup> June 2016.

The accounts certified by the Minister for Finance are annexed to this Audit opinion.



MANOHARAN NAIR  
AUDITOR GENERAL

14<sup>th</sup> December 2018





**DEPARTMENT OF AUDIT  
CIVIC CENTRE, AIWO DISTRICT  
REPUBLIC OF NAURU  
Phone: 5573109**

---

**INDEPENDENT AUDITOR'S REPORT**

**To: His Excellency the President, Hon Baron Divavesi Waqa M.P**

**Report on the Republic of Nauru Whole of Government Financial Statements for the year ended 30 June 2016**

Pursuant to Section 10(1) of the Audit Act 1973 I have audited the Annual Financial Statements of the Republic of Nauru, including the Statement of Public Debt which comprises of the following:

1. Statement of Income & Expenditure
2. Statement of Assets & Liabilities
3. Statement of Revenue v/s Budget
4. Statement of Expenditure Vs Budget
5. Statement of Accounting Policies
6. Notes forming part of the Financial Statements

**Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Section 6 of the Audit Act 1973, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

**Auditor's Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. I conducted the audit in accordance with International Standards of Supreme Audit Institutions which is premised on the International Standards of Auditing. These standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the

circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

However because of the matters described in the Basis for Disclaimer of Opinion paragraph, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

**Basis for Disclaimer Opinion:**

I was unable to satisfy myself that the account balances disclosed in the financial statements were reliable or complete due to adoption of incorrect prior year figures, significant mismatch of figures between FMIS and financial statements, and others as narrated below.

I was unable to obtain sufficient and appropriate audit evidence. I believe that the audit evidence/clarifications that I have obtained are not sufficient and appropriate to provide a basis for our audit opinion. The grounds and issues pertaining to our findings which were identified during the course of the audit are detailed below. There were no other satisfactory audit procedures that we could adopt to obtain sufficient evidence on the matters referred therein.

1. Opening Balance, from the prior year closing balance, could not be verified on Leger in FMIS.
2. The Financial statements do not show correct figures for the prior year comparative information.
3. Cash flow statement is not included in the financial statements thereby making them incomplete.
4. Significant differences appear between Annual Financial statement and General Ledger in many account heads.
5. Fixed Assets purchases for the fiscal year were recorded as Expenses as GoN doesn't have an assets policy.
6. Bank Accounts were not reconciled.
7. The stated depreciation policy is not in accordance with the stated figures in the financial statement.
8. No confirmation/evidence to prove most of the Debtors/Creditors balances.
9. All Assets & Liabilities are not included in the Financial Statement.
10. Payroll balances do not tally with the ledger balances.

11. Revenue head balances, in most cases are not validated with supporting vouchers or evidences.

### **Disclaimer of Opinion**

Because of the significance of the matters described in the Basis for Disclaimer of Opinion paragraph, we have not been able to obtain sufficient and appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements as to whether they have been properly prepared, in all material respects in accordance with the Generally Accepted Accounting Practice (Nauru GAAP) and/or International Public Sector Accounting Standards (IPSAS) and the International Financial Reporting Standards (IFRS), as determined by Govt. of Nauru.

### **Report on Other Legal and Regulatory Requirements**

Under the Audit Act 1973, it is my statutory duty to report cases of non-observance of rules, orders and procedures, spending public moneys for purposes other than those for which the grants were made by the Parliament and non-recovery of Government revenues. On this basis I report that:

- 1 The Cash flow statement as required as per clause 10 of the Audit Act 1973, was not included in the set of Financial Statements.
- 2 The financial statement have, reportedly been drawn on IPSAS Cash basis and IFRS but many issues have not been complied with.
- 3 Statement of Changes in Equity are not attached to the Financial Statement.
- 4 Debtors, Creditors and Loan paid balances are not available in the Financial Management Information System for verification.
- 5 Accuracy of the figures presented in the Financial Statement is not free from material misstatement.
- 6 Schedule of Fixed Assets is not prepared and submitted along with the Annual Financials.



  
**MANOHARAN NAIR**  
**AUDITOR GENERAL**

Dated: 14<sup>th</sup> December 2018





## MANAGEMENT LETTER

The 1st draft Management letter was issued to the Secretary Finance, Government of Nauru on 23 August' 2018 for corrective actions and/or agreement to the findings and recommendations contained therein. Response to the management letter was received on 25th October' 2018 but audit find that still there exist inconsistencies, hence, asked to look into the oversights again and accordingly, after modifying few errors, a revised set of accounts was received on 13th November' 2018. Audit finds that still there are a number of errors appearing which was reported to the management. They acknowledged the errors and confirmed that it cannot be rectified at this juncture. The audit opinion is issued based on the Ministry of Finance response to the final Management letter and considered by the Department of Audit.

Auditor General, Nauru  
14th December 2018



Table of Contents	Page #
i. Abbreviations .....	2
ii. Introduction.....	3
iii. Audit Recommendations.....	4
iv. Detailed audit findings.....	5-26
v. Performance Analysis –Key Indicators.....	27-30
vi. Summary statements and overall conclusions.....	31
vii. Sample Annexures .....	32-33

1. GON ANNUAL FINANCIAL STATEMENT 2015-16	32 pages
2. AUDIT CERTIFICATE	1 page
3. INDEPENDENT AUDITOR’S REPORT	3 pages

**ABBREVIATIONS**

AG	Auditor General
AUD	Australian Dollar
DCA	Department of Civil Aviation
DOA	Department of Audit
FMIS	Financial Management Information System
GDF	GON Development Fund
GL	General Ledger
GON	Government of Nauru
IPSAS	International Public Sector Accounting Standards
ISSAI	International Standards of Supreme Audit Institutions
MOU	Memorandum of Understanding
NCHS	National Centre for Health Statistics
NFMRA	Nauru Fisheries & Marine Resources Authority
NPRT	Nauru Phosphate Royalties Trust
NRO	Nauru Revenue Office
PFTAC	Pacific Financial Technical Assistance Centre
PO	Purchase Order
PV	Payment Voucher
SLM	Straight Line Method
SOE	State Owned Enterprises
SOP	Standard Operating Procedures
WOG	Whole of Government

## **INTRODUCTION**

The financial statements of Republic of Nauru are subject to audit by the Auditor-General in terms of Section 10 of the Audit Act 1973.

The audit of the financial statements for the year ended 30<sup>th</sup> June 2016 was completed and the purpose of this letter is to bring to your attention the findings that were revealed during the audit.

### **SCOPE AND DETERMINATION OF RESPONSIBILITY**

The audit was conducted in accordance with the International Standards of Supreme Audit Institutions (ISSAIs). These standards require that the audit is planned and performed so as to obtain reasonable assurance that, in all material respects, fair presentation is achieved in the annual financial statements.

The audit includes:

- Examination on a test basis of evidence supporting the amounts and disclosures in the financial statements;
- Assessment of the accounting principles used and significant estimates made by management; and
- Evaluation of the overall financial statement presentation.

The audit also included an examination, on a test basis, of evidence supporting compliance in all material respects with the relevant laws and regulations which came to our attention and are applicable to financial matters.

The matters mentioned in this letter are therefore those that were identified through tests considered necessary for the purpose of the audit and it is possible that there might be other matters and/or weaknesses that were not identified.

The financial statements, maintenance of effective control measures and compliance with laws and regulations are the responsibilities of the Accounting Officer. Our responsibility is to express an opinion on these financial statements.

The audit findings which were identified during the course of the audit and our recommendations, are included below.



## AUDIT RECOMMENDATIONS

- **We recommend that Management of GON:**
- **Addresses** comprehensively the scope limitation items and matters of material importance included in this draft management letter with utmost urgency and responsibility.
- **Redraws** its Financial Statements by taking into consideration all observations included in this management letter.
- **Attaches** a Cash flow statement to complete the Financial Statements.
- **Re-computes** the schedule on Property, Plant & Equipment with correct impact on fair net assets value in accordance with the stated depreciation policy. The complete schedule on PPE should now be included in the Financial Statements (format provided as Annexure 1).
- **Reconciles** the differences noticed between the FMIS, Bank statements and the financial statements.
- **Prepares** a well-structured asset register to capture existing assets, disposals, fully depreciated assets and acquisitions as also non-cash asset donations. *Its 'fully depreciated working-assets' / 'charged off assets' may be tracked through Asset register in hard and soft copy forms for better internal control.*
- **Establishes** an accounting policy for accounting of non-cash donations, its valuation and correct the Financial statements.
- **Recognizes** correct liabilities of GON by obtaining direct confirmation from the parties concerned.
- **Evaluates** the figures of domestic and external borrowings based on documentary evidences that should now be located/collected.
- **Discloses** its exact investment (original and current fair value) in the SOEs from which GON expects/receives dividends.
- **Undertakes** as a matter of urgency, the review of its GON development fund bank accounts maintained with the Bendigo Bank with a view to adopt correct balances in the financial statements.
- **Advises** the departmental heads across the GON to maintain proper accounting and financial records that could be retrieved over the next five years and that handing over/taking over of the functional charges be regulated through a well-laid down SOP.
- **Underscores** the need to use the FMIS fully including the assets and liabilities modules and thereby establishes a robust system to retrieve all receipts and payments with supporting evidences.
- **Arranges** in-house or outsources the internal audit function to ensure effectiveness and improvements in the financial internal controls with a view to assure on fair presentation of financial statements and to perform tests of internal controls in other departments.
- **Reviews** internal controls surrounding pay and allowances (local and expatriates) and makes corrections as appropriate in the correct adoption and disclosure of expenses in the financial statements.
- **Reiterates** to all accounting officers the need to classify all expenses and revenues as per chart of accounts for fair presentation of financial statements.
- **Provides** comprehensive responses to the outstanding audit observations raised during the period of audit.

## **DETAILED AUDIT FINDINGS**

- **Presentation of results of audit:**

The results of the audit of the Financial Statements ended 30<sup>th</sup> June 2016 and the accompanying notes are presented in this section. These are grouped into four parts: (1) adjustments to affected accounts; (2) corrections in the presentation of Statements and supporting information to Notes; (3) additional note disclosures; and (4) other financial issues to improve financial transactions recording, processing and reporting. All the recommendations have been discussed and considered by Management during the course of the audit. There are several findings and recommendations that are agreed to by the Management but are still included herein to document the issues noted as part of work.

- **Adjustments to affected accounts**

- **Incomplete Financial Statements**

The Financial Statements presented to us for audit are not complete in all respects. We have not been provided with mandatory parts of the Financial Statements which are reportedly prepared under the IPSAS Cash basis of accounting and the Section 10 of the Audit Act 1973, namely, the:

- Cash flow statement
- Schedule of the fixed assets for the year with comparative details
- Government Loan Fund and Trust Fund showing receipts and payments (only net movements shown and consolidated in the Statement of Assets and liabilities)
- Accounts receivable accounting

Management reported that:

Cash flow statement will be included in the next year's financial statements.

Currently all assets purchases are treated as expenses but keeping in view of the importance of Assets Register, will ensure that assets valuation are put in place and will try to improve it in a later period.

As regards Loan Fund, these are outstanding loans for which supporting documents are not available other than the Deloitte, PFTAC and ADB reports.

As regards Account Receivable, all the debtors are not in the AR system with the FMIS, hence, unable to provide complete list of all AR details but will ensure that the requirements will be met in the next financial year.

- **Statement of changes in Equity**

Wrong figures were estimated in the Government equity which need to be rectified.

The data provided in the Financial statement reads as follows:

**GOVERNMENT EQUITY**

	<b>2015/16</b>	<b>2014/15</b>
	<b>AU\$</b>	<b>AU\$</b>
Surplus / Deficit	( 5,305,700)	(7,029,663)
Retained Earnings	<u>(38,818,827)</u>	<u>(31,789,163)</u>
<b>TOTAL GOVERNMENT EQUITY</b>	<b><u>(44,124,526)</u></b>	<b><u>(38,818,827)</u></b>

It need to be rectified as follows as comparative figures of prior year is wrongly exhibited in the Financial Statement:

**GOVERNMENT EQUITY**

	<b>2015/16</b>	<b>2014/15</b>
	<b>AU\$</b>	<b>AU\$</b>
Surplus / Deficit	(5,305,700)	(7,029,413)
Retained Earnings	<u>(38,818,576)</u>	<u>(31,789,163)</u>
<b>TOTAL GOVERNMENT EQUITY</b>	<b><u>(44,124,276)</u></b>	<b><u>(38,818,576)</u></b>

**Accumulated funds as at 30<sup>th</sup> Jun 2016**      **(44,144,526) (should be rectified as 44,124,276)**

IPSAS-Cash allows for additional statements to provide information that is calculated on accrual basis. However, paragraph 1.3.9 states that any additional statements will only report cash receipts, payments and balances which are controlled by the entity. We noted that the Statement of Equity included in the financial statements of GON is on accrual basis. It is recommended to review the inclusion of this statement to conform with the accounting standards adopted.

Management reported that To be conformity with IPSAS cash requirements for FY 2015/16 set of accounts, the statement of changes in equity has been removed from the final set of accounts. However, management is aware of the importance of this statement and therefore, additional statements will be provided in the FY 16/17 set of accounts to accompany inclusion of the changes in equity statement.

- **Current Assets**

**Cash & Cash Equivalents**

In the absence of a Cash flow statement, we performed a quick reconciliation of the Cash Balance in Note 1 below:

Cash Balance for 2015 (Note 1)	\$20,276,073
Add: Cash Receipts	\$121,843,418
Gross Cash balance	\$142,119,491
Less: Cash Payments	\$129,229,042

Net Cash Balance for 2016	\$12,890,449
Cash Balance – Note 1	\$14,414,495
<b>Variance</b>	\$1,524,046

The variance as shown above needs to be reconciled to balance.

Management reported that the full analysis of cash balance will be submitted to audit upon completion but did not receive any details till the time of production of this management report.

- **Current Assets**

**Special Funds**

**Note 2 - Statement of Special Fund Balances**

	2015/16	2014/15
Nauru Trust Fund	20,400,000	10,125,566

Nauru Trust Fund is an intergenerational Trust Fund set up in 2014 for the people of Republic of Nauru through MOU in which regular contributions (determined by applying a defined formula) are made by Nauru, Australia and Taiwan. Asian Development Bank made one-time contribution. The Fund invests in financial instruments and prepares its own financial statements. The surplus is ploughed back for investments. Government of Nauru cannot withdraw the surplus or invested amount till the year 2033. Given the MOU conditions, contribution of GON to the Nauru Trust Fund cannot be termed as Current Asset.

The investment must be shown as financial asset under non-current asset (Nauru share) with additional appropriate note to the accounts stating the audited opening and closing balances of joint corpus of the Fund and the movement in the Fund (with respective shares of Nauru, Australia, Taiwan, ADB and New Zealand).

Moreover, the note should also indicate that the Fund balances are not freely available for use by the Government and their use is subject to external restrictions under the MOU of the Fund.

Management reported that it will be included in the next submission of 2016-17 accounts.

- **Current Assets**

**Note 3: Statement of Debtors**

**Bank of Nauru/RONPHOS**

	2015/16	2014/15
Debtors	3,719,000	6,,660,472

The note above, reflects the revised dues from RONPHOS, based on our draft management letter, in the amount of \$3,719,000 as at 30.6.2016 which is matching with the confirmation received from RONPHOS (the audited financial statements of RONPHOS) as at 30.6.2016. The prior year receivable was \$6,660,471 but audit could not find any transaction during this year for the decrease, amounting to \$2,941,471 to substantiate the figure.

- **Current Assets**

**Note 3: Statement of Debtors**

**Government Housing Scheme**



	2015/16	2014/15
Total Government Housing Scheme	637,823	396,228

The above note shows that the Government Housing Scheme receivable has gone up from \$396,228 of 14 recipients to \$637,823 of 22 recipients during the year. No transactions took place during this year to authenticate the payment/difference of \$241,595. The finance department could not explain the reasons for the difference. The data is not available on FMIS but is kept separately in excel format.

#### Current Assets

#### Note 3: Statement of Debtors

##### Others

	2015/16	2014/15
Security Camps reimbursable	8,292,030	7,108,000

The above amount represents initial payments made during the year by GON on behalf of the Government of Australia in relation to the security camps for refugees in Nauru that have become due for receipt.

Management confirmed that the full amount of \$8,29,030 shown above is associated with security camp reimbursements and nothing to do with any other reimbursements

However, audit noticed that a sum of 9,000/- receivable from RPC towards visa fee form 23 April 2016 to 22 July 2016 is inclusive of this amount. We sought to verify the other amount with the corresponding actual payments made by GON through the Bank statement and/or supporting invoices requiring reimbursement. Neither the Bank statement nor supporting invoices are available for verification.

- Non-current Assets read with accounting policy on depreciation**

		2015/16	2014/15
Plant & Equipment	Note 4	854818	1,130,005
Buildings	Note 4	19,460,415	20,555,151

The Financial statements prepared under cash basis do not show the depreciation as expense, its being non-cash item. However, net block is reflected in the non-current assets after depreciating the assets in line with the accounting policy that states the depreciation rates for Plant & Equipment- furniture (@33%), Air-conditioners (@33%), Motor Vehicles (@20%) - and Buildings (@5%. In this regard, following audit observations are made:

- The figures of Plant & Equipment and buildings are carried forward from 2013-14 onwards based on revaluation of WOG Assets performed by M/S Carlo & King vide their report dated 9 Aug 2014. No additions, deletions, impairments since then have been reflected in the non-current assets. Purchases of furniture, motor vehicles, air conditioners, etc. during the financial year 2015-16 have been charged off to expenses without updating the total amount of non-current assets as required. The above figures therefore represent static number of assets as in the financial year 2014-'15 and are therefore incorrect.

- Given the audit findings above, the non-current assets are not shown correctly at the balance date. Note 4 must also transparently explain the movement in non-current assets preferably in a format consistently applied as recommended in Annexure 1.
- Audit noted that the FS 2014-15 and 2015-16 net block of assets has been incorrectly worked out by applying SLM rates of depreciation on written down value. The effect of this incorrect calculation is worked out as follows.

Assets	SLM Rate	*Based on Valuation report	2014-15 depreciation calculated (SLM)	2015-16 net block to be shown	2015-16 actual net block shown	Difference in Net block
furniture	33%	\$343,188	\$113,252	\$116,684	\$209,242	-\$92,558
air condition	33%	\$84,922	\$28,024	\$28,874	\$44,254	-\$15,380
motor vehicles	20%	\$894,825	\$178,965	\$536,895	\$601,322	-\$64,427
<b>Plant &amp; Equipment</b>						<b>-\$172,365</b>
<b>Building</b>	5%	\$21,671,500	\$1,083,575	\$19,509,176	\$19,460,415	<b>\$48,761</b>
<b>Net difference</b>						<b>-\$123,604</b>

\* first Opening balance taken from the Re-valuation report submitted in 2014 for the financial year 2014-15. (Note: although the figures were reflected in FS 2013/14, no depreciation recognized in those accounts).

The result of the above is that the Plant & Equipment under Non-current assets are overstated by \$172,365 whereas Buildings are understated by \$48,761 in the Financial Statements ended 30 Jun 2016.

Management reported that it will be taken care of in the next financial year 2016-17. Also management suggests the government to take a full valuation of all its assets to determine a complete list of assets so that the government could accurately calculate annual depreciation for all categories of government assets.

• **Non-current Assets**

		2015/16	2014/15
Development Funds (Aggregate)	Note 5	15,836,660	15,516,779

**Note 5:**

**Statement on Balance of GON Development Fund (GDF) Accounts by aggregate receipts and payments**

- The Statement provides aggregate development fund balance of \$15,836,660 as at 30<sup>th</sup> Jun 2016 after offsetting the GDF movement of \$2,079,925 representing net of donor payments and receipts in various bank accounts as detailed. Our test checks of movements showed that the Westpac bank accounts were closed in the previous year and amounts transferred to Bendigo Bank Agency. Three of these accounts are maintained separately from the GON accounts. These are, (1) AusAid Account (DFAT Account) (2) NZAID account, and (3) Development Fund Account. Other accounts appearing in Note 5 do not exist. As such, the entire statement containing Westpac bank details as disclosed in Note 5 is redundant, irrelevant and misleading information.



- The three major accounts maintained in Bendigo Bank agency as on 30 Jun 2016 were analyzed with reference to bank statement, FMIS and Financial Statement. There are significant differences as calculated below.

Donor	Receipts			Difference	
	As per FS	As per FMIS	As per Bank st	FS with FMIS	FS with Bank st
AusAid	5,017,315.00	0	9,583,663.37	5,017,315.00	-4,566,348.37
Development Fund	1,318,584.00	8,365,817.96	1,380,631.86	-7,047,233.96	-62,047.86
NZAid	539,991.00	305,717.95	670,004.95	234,273.05	130,013.95
			11,634,300.18		

Donor	Payments			Difference	
	As per FS	As per FMIS	As per Bank st	FS with FMIS	FS with Bank st
AusAid	3,377,896.00	5,592,507.71	8,368,383.55	2,214,611.71	4,990,487.55
Development Fund	190,059.00	0	1,589,251.99	190,059.00	1,399,192.99
NZAid	1,372,084.00	2,942,563.00	4,338,964.92	1,570,479.00	2,966,880.92
			14,296,600.46		

Given the significant differences noticed in the Financial Statement with reference to FMIS and the Bank statements for the respective accounts, the net GDF movement shown at \$2,079,925 cannot be relied upon. Taking bank statement figures of receipts and payments as authentic, the correct GDF movement that can be shown is as follows.

Receipts as per bank statement	11,634,300.18
Payments as per Bank statement	14,296,600.46
2015/16 GDF movement	<b>(2,662,300.28)</b>

The GDF movement calculated conservatively would affect the Total surplus/ (Deficit) by the same amount. The total deficit, accordingly, works out to \$10,047,925 instead of \$5,305,700 with consequent effect on total government equity as shown under Statement of Assets and Liabilities, Development funds (aggregate) shown under Non-current assets.

- The summary statement also included unrepresented cheques worth \$1,760,044 as at 30<sup>th</sup> Jun 2015 for which the Finance department could not provide any detail. We place scope limitation on this amount.

Management reported the recommendation has been noted and further works are needed to address the issue associated with the variance between the three sources of documentations (FMIS, bank statement and financial statements).

- Current Liabilities**

	Note	2015/16	2014/15
Accounts Payable		4,682,019	5,751,947
Trade credits- domestic debts	6	10,591,852	9,202,341

Creditors- external debts	7	6,842,000	6,863,000
---------------------------	---	-----------	-----------

The initial submission of Account payable was \$6,547,055 whereas on re-revision the accounts it has substantially reduced to \$4,682,019 resulting to a difference of \$1,865,036 against which neither any explanation given to audit nor audit could find any corresponding transaction in the book of accounts.

The above figures do not tally with the FMIS balances. Reportedly, the finance department does not believe that the figures are accurate having taken them (two years back) from several sources such as PFTAC report, Deloitte report and others. These documents are also not available with the Finance Department.

Confirmation of domestic debts (Note 6) from Eigigu, Ronphos, NUC and NRC could not be obtained or supporting documents evidenced. Their respective financial statements for the year also do not show these balances as their assets either.

Note 7 refers to external debts which have been set up based on ad-hoc documents. No confirmation of these payables was sought by the GON or received from the international organizations listed. Except for extinguishing the liability of Global Forum on Tax Transparency (OECD), there was no movement in the balances for last three years. These outstanding may have increased over the years, but apparently no efforts were made to enquire about their status.

Since there are no supporting documents for the balances totaling \$22,115,871 appearing under current liabilities, we place Audit Scope limitation on these balances.

Management reported that Treasury will take up the matter with regard to debts associated with international organizations and see if they can be taken off upon agreement by the creditor. The work need to be done in the next financial year and upon receiving confirmations from the various creditors, Treasury will then update the list of government external liabilities.

Similarly management is fully aware of the need for all these debts entered into FMIS and therefore, work has been commenced in uploading all the debts into the FMIS under the AP module. This will ensure accuracy and completion of data associated with liabilities on the financial management information system.

- **Non-Current Liabilities**

**Note 8**

**Domestic (Loans & Borrowings)**

	2015/16	2014/15
Bank of Nauru (Net private sector)	34,519,549	34,526,786

The above amount was personally verified by the AG (being highly confidential information) with the soft data available in the NRO office. There was a difference of \$7,237.03 between the amount shown in the initial set of financial statements and the NRO records which has been rectified and the amount shown above is matching with the records now.

**Note 8**

**Domestic (Loans & Borrowings)**

	2015/16	2014/15
--	---------	---------



NPRT (Unconsolidated)		26,865,764	26,865,764
RONPHOS (Unconsolidated)		2,402,913	2,402,913

The above figures are static for last three years and are not supported by any document whatsoever. The rationale of bringing them on the balance sheet as loans & Borrowings is also not known. As such, we place audit scope limitation on these balances.

Management reported that the NPRT (unconsolidated) and Ronphos (unconsolidated) figures have been static for years as there has not been any payment made towards these debts. The amounts were brought into the books as balance sheet items in the financial year 2013-14 following the termination of Deloitte as the Bank of Nauru (BON) Liquidator.

- Note 9**

**External (Loans & Borrowings)**

		2015/16	2014/15
<b>Menen Hotel Loan</b>			
Debt outstanding		-	-
Principal repayment		-	-
Yen Bond debt		33,618,367	31,242,826
<b>Taiwan Exim Bank commercial loan</b>			
Debt outstanding		6,277,500	7,002,000
Principal		2,344,300	2,399,000
<b>External loans &amp; borrowings</b>		<b>42,240,167</b>	<b>40,643,826</b>

- There is a reduction of \$779,200 in liability on account of Taiwan Exim Bank Commercial loan as follows.

Debt outstanding (\$7,002,000 - \$6,277,500)      \$724,500

Principal (\$2,399,000 - \$2,344,300)              \$54,700

The above reduction of \$779,200 in liability is not matched by corresponding payment of cash/bank transfer to the Taiwan Exim Bank and as such we could not vouch the veracity of this amount.

Management reported that the corresponding payment of \$779,200 for the Taiwan Exim Bank cannot be located as this was paid off directly by Taiwan from its annual grant allocation for Nauru

- Differences between Trial balance (GL) and Financial Statements**

The GON uses the accounting software FMIS to capture accounting information and data.

No trial balance was prepared for the balance sheet items as FMIS was not used to record balance sheet items of assets and liabilities.

The FMIS is used for preparation of financial statements. We carried out review of the balances appearing in both FMIS and Financial Statements, the results of which showed following

Dept. of Audit, Nauru  
Audit of GON Annual Financials 2015-16  
Management Letter

differences which was brought to the notice of the management for consideration, correction, reconciliation and adjustments to be made in the General Ledger.

	<i>As per Trial balance</i>	<i>Amount as per FS</i>	<i>Difference</i>
<i>Balance as per TB</i>	-130,091,592.72	-121,821,030.00	-8,270,562.22
<i>Balance as per FS</i>	-130,115,458.00	-121,823,428.00	8,292,030.00
<b><i>Difference</i></b>	<b>23,865.28</b>	<b>2,398.00</b>	<b>21,467.78</b>

**Expenses**

	<i>As per trial balance</i>	<i>Amount as per FS</i>	<i>Difference</i>
<i>Balance as per TB</i>	129,053,100.12	128,794,627.00	258,473.12
<i>Balance as per FS</i>	129,229,042.00	129,229,042.00	0
<b><i>Difference</i></b>	<b>-175,941.88</b>	<b>434,415.00</b>	<b>258,473.12</b>

Following is the summary of trial balance differences with Financial statements in gross amounts.

<b><i>FS amount does not match with amounts as per trial balance</i></b>	<b>9,239,550.25</b>
<b><i>Balance in Trial Balance but zero balance in FS</i></b>	<b>398,256.00</b>
<b><i>Special Project expenses without contra entry for cash</i></b>	<b>8,981,077.98</b>
<b><i>Unexplained differences</i></b>	<b>159,141.96</b>

Management reported that the variance between Trial Balance and Financial Statement is to do with donor funded transactions. In preparing the P&L, all donor related transactions were excluded from the P&L as they should not form part of the Government performance. However, the figures reported by the Audit contains both GoN and donor funded transactions, hence, the variance in the figures between Trial balance and Financial Statements.

- Public Debt repayment treated as expenditure**

**Recurrent Expenditure**

	<b>2015/16 Actual</b>	<b>2015/16 Rev Budget</b>	<b>2014/15 Actuals</b>
Public debt	1,900,471	1,900,930	5,824,922

As reported in the Auditor General's Management letter on the Financial Statements for 2014/15, repayment of public debts is not an expense item and therefore cannot be included in the Income & Expenditure statement. Interest paid on the debts can only be treated as expenditure. We could not find corresponding public debt balances in the Balance sheets of current year/previous years detailing the amount payable as debt.

An analysis of payments indicated that this amount is represented by payment of pending rentals, outstanding salaries, overdue international membership fees, unpaid construction contracts, non-payment for air services and others. These may have been outstanding for the previous years but not shown as public debts in the respective balance sheet. The correct disclosure could have been, *under the IPSAS Cash basis*, to show these items as public debt and set them up as liability. Any repayment could be shown as reduction in liability with the same being reflected in the Cash Flow statement.



Consequently, the expenses for the financial Year 2015-'16 have been overstated by AUD 1,900,471.

The management reported that the recommendation of audit has been noted and until all the liabilities are accurately recorded in FMIS, Government will continue treating debt related payments as expenses instead of treating them as reduction in liabilities with debt interest being the only component to treat as expenditure under the P&L statement. Management fully noted the importance of accurately treating debt reduction payment and therefore Treasury will have to enhance its efforts in improving the debt areas through effectively utilizing the FMIS available AP module.

• **Review of the Payroll transactions:**

We sought to review the payroll transactions with the expectations (a) that the transactions are recorded in the accounting period to which they relate to, (b) that the figures reflected in the Financial Statements match those in the General Ledger, (c) that the transactions are duly approved by authorized officer, and (d) that the payment vouchers are correctly classified.

Our review could not be carried out as the payroll data was reportedly lost with the upgrade to the payroll software. The HR could not provide hard copy of the payroll for 2015-'16 or retrieve the data from the system. Under the circumstances, audit testing, for example, of payroll for new staff, separated staff, existing staff, leave salaries, bank reconciliation with pay authorizations, and likely ghost employees could not be carried out. As an alternative to payroll testing, Audit painstakingly totaled up the payroll expenses for each month of the financial year for all the departments (expatriates and local staff) and matched the figures with the General Ledger and financial statement.

The result of this exercise showed following discrepancies.

Recurrent expenditure	Note	Amount as per Financial Statement	Amount as per General Ledger	Variance (AUD)
Total Salary –local	Note 16	16,074,478	16,525,021	450,543
Total Salary-Expatriates	Note 17	18,,243,429	20,101,475	1,858,046
<b>Total variance</b>				<b>2,308,589</b>

As could be noted from the summary table above, the financial statement understates salaries (local and expatriates) by \$2,308,589 with consequent impact on the Surplus for the year.

Management reported that there is no variances between GL and the reported figures on the financial Statements, as per details provided in Note 16 and 17, and the reported understated figure is not correct and needs to be removed from the report.

But Audit further verified and finds that our findings are correct and there is a variance between the General Ledger and Financial statement. However, on further scrutiny we find that the receipt of following Aid fund amount, towards salary, has been removed from the GL balance, hence, the difference is appearing in the financial statement.

Recurrent expenditure	Expenses as Per Financial Statement (Note 16 & 17)	Aid fund receipt	Net Expenses per FMIS	Difference
Salary –local	13,621,187	401,319	14,022,981	475
Salary Expatriate	5,063,435	588,272	5,651,707	-
Consultants fee	4,141,011	1,713,996	5,537,469	-317,538
<b>Total variance</b>				<b>-317,063</b>

Including the Aid Fund shown above, the figures were matching with the General Ledger but in the revised set of Financial statement, the consultancy fee has been changed to \$4,141,011 consequent to rectification of incorrect classification of expenses which along with the Aid fund exceeding the amount available in FMIS Ledger. Hence, the Statement of Income & Expenditure needs to be adjusted with the correct figures.

## 2. Corrections in the Statements and Notes presentation

### a. Comparative figures of financial statements ended 30<sup>th</sup> June 2015

The financial statements ended 30<sup>th</sup> Jun 2016 do not show correct figures for the previous financial year as comparative information. In other words, the audited financial statements of 2014-15 figures were not reflected in the 2015-16 financial statements against most items. When enquired, the management agreed with the observation and accordingly corrected the omission in the financial statements but the following figures are still not amended in the revised version of Annual Financials, which need to be rectified again.

Item	Comparative figures in 2015-16 Financial Statements	Figures in 2014-15 audited Financial Statements
<b>Statement of Revenue and Expenditure by Heads</b>		
Recurrent Income	95,161,411	95,161,662
Recurrent Surplus/Deficit	6,902,554	6,902,303
Total Surplus/Deficit	7,029,663	7,029,413
<b>Statement of Assets and Liabilities</b>		
Surplus/Deficit	7,029,663	7,029,413
Total Government Equity	(38,818,827)	(38,818,576)
Total Current Assets	50,235,815	50,236,066
Total Assets	87,437,750	87,438,001
Total Net Assets	(38,818,826),	(38,818,576)
<b>Statement of Revenue &amp; Expenditure by Head</b>		



94 DCA	938755	938754
95 ICT	358463	358464
<b>Total Other Revenue and Expenditure</b>	7,029,663	7,029,413
<b>NOTE 3: Statement of Debtors</b>		
Total Others	12,760,978	12,760,977
<b>Note: 22 Miscellaneous Expenses</b>	124,185	124,012
Total	12,256,124	12,411,431

\* A significant difference has occurred because of wrong carry forward of 2014/15 figures as shown in the table above. This will impact the recurrent surplus to be brought forward to 2015/16 Financial Statements.

Management responded that they dispute the audit findings as the comparative figures on the financial statement that Treasury has is the correct comparative figures, but Audit reaffirms that the above differences are still persisting, hence, the omissions calls for correction in the Financial Statements.

**b. Assessment of Financial Statements against IPSAS cash basis:**

The financial statements have, reportedly, been drawn up to conform to IPSAS Cash basis and IFRS. Refer to accounting policies under 2 and 2.1. Following issues have been noted while performing assessment of compliance thereof. Recommendations for their correction are included.

- I. An entity is required to prepare and present financial statements which include a statement of cash receipts and payments which recognizes all cash receipts, cash payments and cash balances controlled by the entity (IPSAS ref 1.3.4). It is observed that the Statement of Income and Expenditure does not present the cash balances for the year ended 30<sup>th</sup> Jun 2016.

Management responded that it will be taken care of in the next financial year

- II. The statement of cash receipts and payments must present beginning and closing balances of the entity (IPSAS 1.3.12). Contrary to this requirement, opening and closing balances are not included in the Statement of Income and Expenditure (cash).

Management responded that it will be taken care of in the next financial year

- III. The financial Statements are required by IPSAS 1.7.8 to present a comparison of the Budget amounts with Actual amounts for each level of legislative oversight for the financial year. The standard also requires disclosure of Original and Revised budget amounts with explanation of material differences between the Budget and Actual amounts. This comparison is noted only for Revised Budget and that too without explaining the differences.

Management responded that it will be taken care of in the next financial year

- IV. IPSAS 1.7.23 requires the entity to explain if the changes between the original and final budget figures are because of reallocations within the budget or other factors either (a) by way of note disclosure or, (b) cross reference to any report issued in this regard. This explanation has not been provided by the notes to the Financial Statements ended 30<sup>th</sup> Jun 2016.

Management responded that it will be taken care of in the next financial year

- V. The Financial Statements do not disclose the budgetary basis, period and classification followed for the approved budget contrary to the IPSAS requirements under 1.7.33 and 1.7.37.

Management responded that it will be taken care of in the next financial year

- VI. The notes to the financial statements also do not include information on entities included in the approved budget which is required to be disclosed as per IPSAS 1.7.39.

Management responded that it will be taken care of in the next financial year

- VII. Disclosure of foreign currency exchange differences is required by IPSAS 1.6.5 as reconciling items between opening and closing cash balances for the financial year. No such disclosure is made in the notes to the Financial Statements ended 30<sup>th</sup> Jun 2016.\

Management responded that it will be taken care of in the next financial year

- VIII. The notes to the Financial Statements also do not report on unrealized gains and losses from changes in foreign currency exchange rates at the balance date as required by IPSAS 1.6.8.

Management responded that it will be taken care of in the next financial year

- IX. IPSAS 1.3.25 requires additional information to be provided for a fair presentation of cash receipts, cash payments and cash balances. Although there are significant receipts such as VISA revenues and taxation revenues, and significant payments such as special projects, subsidies & donations, overseas medical expenses and land lease; these are not explained by way of explanatory notes. Similarly, description of Special Funds, terms of its investment and interest received/due are the relevant details that are missing from the notes. Long term debts and Borrowings are not explained too.

Management responded that it will be taken care of in the next financial year

- X. IPSAS 1.3.27 expects that the Financial Statements present information that is:

- Free from material error. However, many of the comparative prior year figures are incorrect as detailed in page 16 last para.
- Timely. Contrary to this, Financial Statements for 2015-'16 were submitted in October 2017. Audit Act 1973 requires that the financial statements should be submitted within 3 months from balance date.
- Verifiable. However, many departments have not kept supporting documents for their revenues/expenses for 2015-'16. Some balance sheet items also are not supported by verifiable documents.

- XI. Since IPSAS Cash have been adopted in preparing the financial statements, the Statement of income and expenditures needs to be **retitled** as Statement of Receipts and Payments. This title should be used throughout the Financial Statement including notes to the accounts to maintain internal consistency.

Management reported that the recommendation taken on board and the statement of income and expenditure has been retitled as Statement of Receipts & Payments.

**(c) Recurrent Income**

	2015/16 Actual	2015/16 Rev Budget	2014/15 Actuals
Income from other SOEs	628,160	950,000	1,041,339

The income from other SOEs (\$628,160) for the financial year 2015-'16 includes remittance of \$149,751.56 from Department of Civil Aviation which is a department of the GON and not a SOE. This is a misclassification of revenue in the financial statement and needs to be corrected.

Management responded that the error has been corrected amount has now been moved to DCA.

Audit noticed that there has been no changes effected to this error, so far.

**(d) Recurrent Income**

	2015/16 Actual	2015/16 Rev Budget	2014/15 Actuals
Customs Duties Note 12	17,951,992	13,391,910	8,923,352

We expected the Department of Customs to have adequate system of filing of records and documents in support of the revenues being collected by them for the Government of Nauru. We also anticipated the administrators to provide sufficient evidence that revenues are collected effectively, efficiently and economically. However, we could not find any document related to FY 2015-16 despite several reminders. The Secretary, Customs confirmed that all records have been destroyed in a major clean up last year and that they have not recorded any transaction manually in the register.

In view of the non-availability of records to check customs revenue, we could not perform tests of transactions or link them with the receipts at the Nauru Revenue office. We therefore place audit scope limitation on the entire amount appearing under Customs duties.

Management responded that Customs department needs to strengthen its filing system or enhanced its automated systems to ensure that all records are available for auditing purposes.

**(e) Recurrent Income**

	2015/16 Actual	2015/16 Rev Budget	2014/15 Actuals
Port fees	1,282,520	1,229,732	1,295,761

We were informed by the Port authorities that invoices and deposit remittances (receipts from NRO/Bendigo) are not available with the office for the year 2015-16 due to absence of accountant. Apparently, the port office has not (a) maintained proper records for the revenue generated through port fees (b) performed bank reconciliation for the receipts, and (c) linked clearance of imports (containers) with receipts evidencing payment of invoices.



In view of the non-availability of records to check port fees revenue, we could not perform tests of transactions or link them with the receipts at the Nauru Revenue office. We therefore place audit scope limitation on the entire amount appearing under Port Fees.

Management responded that Recommendation for Port is noted and Treasury will work with Port to ensure that a more effective and robust system is established to enable Port perform its financial tasks in a more effective, efficient and transparent manner.

### 3. Inclusion of additional note disclosures

#### C) Accounting policy no. 1.0 on Government of Nauru

The accounting policy states that all State Owned Enterprises (SOEs) are not consolidated into the Government of Nauru accounts. It specifically mentions the SOEs such as Ronphos Corp, Nauru Rehabilitation Corp, Nauru Utilities Corp and Our Airlines.

However, the Financial Statements have consolidated the financial results of Nauru Port Authority and Nauru Fisheries & Marine Resources Authority although these are corporations under the Nauru Corporations Act and are therefore required to prepare separate financial statements and lay them before the Parliament after statutory audit along with separate Audit reports.

Additional note disclosure is required to transparently bring forth the above anomaly to the accounting policy with appropriate disclosure as to estimated amounts pertaining to these SOEs.

Management responded that additional note has been inserted to reflect that statutory bodies such as Fisheries and Nauru Port Authority finances are included in the whole of Government (WoG) account.

#### D) Recurrent Income

	2015/16 Actual	2015/16 Rev Budget	2014/15 Actuals
<b>Ronphos royalties</b>	0	3,972,109	0
<b>Ronphos dividends</b>	40,195	0	0
<b>Income from other SOEs</b>	628,160	950,000	1,041,339

As could be noted the above income represents dividends and royalties received from Ronphos and income from other SOEs (Digicel, Eigigu) against the GON investments in their equity, etc. However, the Republic's investment in the SOEs is not included in the Annual Financial statements. The corresponding GON's investment (original and current) in Ronphos, Nauru Air Corporation, Nauru Corporation/Eigigu Holding Corporation and other SOEs must be disclosed in the Financial Statements ended 30<sup>th</sup> Jun 2016.



Management responded that the GoN investment in all SOE's is currently unknown and only upon confirmation of amount in the future, then they would be included or disclose in the future accounts.

**E) Recurrent Income**

	2015/16 Actual	2015/16 Rev Budget	2014/15 Actuals
<b>General Budget Support</b>	4,368,805	3,339,214	7,335,990

The General budget support is at times received by Nauru from countries and international organizations. During the financial year 2015-16, the above mentioned amount was received. However, details are not available. The nature of receipt requires adequate disclosure by way of a note such as name of the country, organization or others and the amount from each.

Management reported that an additional note explaining the general budget support has been included in the statement as Note.25.

The note states that the amount is received from ROC (Taiwan) in accordance with agreed MOU between the two countries.

**4. Other financial issues to further improve financial transactions recording, processing and reporting**

**Statement of Revenue & Expenditure by Heads  
Budget approved on cash basis**

**(a) Review of the budget against the actuals for the year ended 30 Jun 2016**

GON Budget and financial statements are not prepared on a comparable basis. This requires that, in conformity with the IPSAS Cash, a separate statement of comparison of budget and actual amounts is presented. This statement should ideally have the significant differences explained so that readers do not misinterpret financial information. A suggested format is provided at Annexure 2.

In the absence of such analysis, Audit conducted a broad review of the budgeted amounts as revised against the actuals for the financial year 2015-16 that showed following significant variances (above 25% of the budgeted amounts).

- Significant variances between 'Budget' and 'Actual' – **Revenue Heads**

Head of account	Actual	Revised Budget	Significant Difference	Explanation (Main reasons)
3. Chief Secretariat	319,089	25,700	293,389	Fees for change of constituency by voters
11. Finance Secretariat	1,054,489	6,111,000	-5,056,511	No royalties received
16. Finance- other payments	9,015,378	14,113,762	-5,098,384	DJBC reimbursable delayed from SOEs to next year
17. Nauru Customs	17,951,992	13,391,910	4,560,082	Increase due to new tariff

office				rates
31. Fisheries	37,467,386	35,222,079	2,245,307	Increase in rates for fishing days
43. Justice-secretariat	14,874,738	9,006,686	5,868,052	Increase in VISA fees & DJBC land rentals
45. Border control	21,958,765	28,985,817	-7,027,052	Decrease due to RPC visa collection delayed to next year
84. Lands & Survey	11,043	2,175,890	-2,164,847	Land rental being accounted for under Justice dept.

- Significant variances between 'Budget' and 'Actual' – **Expenditure Heads**

Head of account	Actual (AUD)	Budgeted (AUD)	Significant Difference	Explanation (Main reasons)
20. Customs office	331,063	518,762	(187,699)	Underutilization of local salary and consultant fees
30. Youth Affairs	105,319	158,568	(53,249)	Amounts earmarked under special projects not utilized.
35. Foreign Affairs-Suva	233,954	421,406	(187,452)	Savings under Salaries and house rentals
43. Dep of Land Mgt	238,383	355,063	(116,680)	Plants & Equipment not purchased during the year
45. Lands Transport	388,777	679,472	(290,695)	Consultants fees not paid

- Actual expenditure significantly higher than budgeted.

The GON actual expenditure was, as per income expenditure statement, \$129,229,042 compared to the receipts of \$121,843,418 thereby showing a deficit of \$ 7,385,624. This deficit is likely to be higher given the incorrect figures adopted as noted in this report.

Management reported that Treasury noted the recommended format for presentation of budget against actuals data's in conformity with IPSAS cash and will be utilized in the next year set of accounts.

**b) Review of internal controls surrounding Expenditure function**

The GON manages all payments for the whole of government Ministries/Departments through centralized system of FMIS located in the Ministry of Finance. Accordingly, payment vouchers are raised by individual departments, duly approved by the Head of the Department, and posted on the FMIS for approval of authorized signatory. The authorized signatory (Minister of Finance for more than \$1000 and Chief Accountant for less than \$1000) approves it after initial assessment in the Finance department. Upon approval, payment is released through EFT or cash/cheque by the Nauru Revenue Office (NRO)

Our test of controls showed following issues.

- a. **Incorrect classification of expense items:** Incorrect classification resulted in payments being accounted against incorrect natural accounts thus causing these accounts to be overstated



and the correct ones being understated. Following errors, found in audit test checks, are required to be adjusted to show correct balances for each of the affected accounts.

#	Classification of expense adopted	Classification of expense ought to be adopted	Amount (AUD)
1.	R&M Nauruan House (61-0000-00000-2216)	Expenses were for pharmaceuticals- Hence, correct classification 61-000-00000-2470	\$83,116.00
2	Social Services NTSS salaries payment ( Social Services Aged Pension) –(16-0000-00000-2400)	Consultants' fees (16-0000-00000-2055)	\$28,699.84
3	Social Services NTSS salaries payment ( Social Services Aged Pension) –(16-0000-00000-2400)	(No classification could be sighted by audit under the chart of accounts)	\$120,909.15
4	Miscellaneous expenses – Payment for consultancy Services	Correctly classified as Consultancy fees (16-0000-00000-2055)	\$288,838.00
5	Miscellaneous expenses – purchase of air-conditioners & Other equipment for TVET supplies	Correctly classified to Plant & Equipment (2495)	\$19,392.00
6	Land rental payment from Electricity expenses (15-0000-00000-2315)	Correctly classified as Land rental 15-0000-00000-2160)	\$4632.00
7	Electricity expenses shown as paid from Stores (04-0000-00000-2135)	Correctly classified as Electricity (04-0000-00000-2315)	\$3000.00
<b>Total amount misclassified under expenditure</b>			<b>\$548,586.99</b>

Management reported that the incorrect postings for some of the expenses highlighted in the draft audit report have been corrected by debiting correct expense line code and crediting the vote in which they were initially allocated to.

However, Audit further verified and find that:

- a. R&M Nauruan House (61-0000-2216) (1) has been rectified to the account head Drugs and Dressings under miscellaneous expenses;
- b. Social Services NTSS salaries and Miscellaneous expenses (2) & (4) has been ratified and moved to Consultants fee and
- c. NTSS Salaries payment earlier debited to Pension (2400) has also been rectified and now debited to Expatriate salary.

The changes effected only to the Financial statements and not in the Ledger FMIS, hence the Ledger balance still remains the same. Besides, the other account heads provided above are not corrected, so these has to be adjusted to show correct balances for each of the affected accounts.

- b. **Incomplete documentation for payments:** Audit noted several payments that are not supported by proper documentation (e.g. list of pension beneficiaries not signed, land rental recipients not formally authenticated). Most of the NRO payments do not have the signed documents supporting the cash payments. It is suggested that the pre-authorization assessment function is adequately resourced to ensure proper documentation in all cases.

Management reported that recommendation is noted and Treasury ensures that improvements to the overall documentation process for payments is strengthened. The introduction of the Financial Instructions (FI's) would greatly assist Treasury and line agencies in improving the documentations process for payments.

- c. **Amounts on payment vouchers (PVs) not matching attachments/ invoices:** Audit noted several PVs that mismatched with the invoices. It is reiterated that the authorization process must be adequately controlled to ensure that PVs are properly supported by invoices.

While analyzing the above exceptions, we find that the main causes could be found in (a) authorizing officer and Assessing officer not observing the internal controls on purchases, (b) not recording correct FMIS coding on the PO/Payment voucher, (c) habit of making payments without supporting documents, (d) not filling up budget amount and available budget columns and (e) inadequate filing system.

Consequences foreseen for these practices are that the GON may be (a) purchasing items not related to the individual department business (b) paying the wrong suppliers (c) overspending under certain heads of account (d) paying without receiving goods and services, and (e) allowing actual or potential frauds or fraudulent practices in the GON.

Management reported that Treasury noted the findings and staffs have been reminded of the need to be more vigilant and careful when assessing payments.

• **Review of internal controls surrounding Revenue function**

The major revenues of the GON are (a) fishing licenses (b) Visa revenues (c) customs duties and (d) taxation which together amounted to \$92,820,186 or 76.18% of the total revenues during the year ended 30 Jun 2016. Audit performed tests of controls on selected samples, the results of which are as follows.

**Fishing licenses:** The NFMRA issues invoices to raise revenues from (a) support vessel charges (b) Fishing licensing, and (c) 'fishing days' licences when requested by the customers. The CEO approves the invoice prepared by License/Revenue officer and hands it over to the customer. The customer pays the invoiced amount either at the NRO or the Nauru Receipting account maintained by Bendigo bank agency (earlier Westpac). Receipt issued by the NRO/Bank is then presented by the customer to the NFMRA. The CEO then issues the License/Fishing days authorization. Subsequently, at the back-end, the NFMRA files the receipt and the invoice and performs reconciliation with the NRO/Bank. Our test checks showed following deficiencies.

- NFMRA has not maintained the Receipts against the invoices for the revenue during the year 2015-'16.



- NFMRA has not maintained proper records on the licenses issued during the year.
- NRO did not send the confirmation slips evidencing payments received to the NFMRA and the NFMRA did not remind them on it. As a result, no bank reconciliation took place during the year.
- NFMRA is not in a position to assure that the licenses have been issued only on the basis of payment of invoices.

**Visa revenues:** These comprise of (a) visa fees levied on all foreigners entering Nauru administered through the Department of Immigration (Border Control), and (b) visa fees and other charges for the Australian refugees and workers at the Regional Processing Centre (RPC) administered through the Multi-Cultural Affairs department. The Department of Immigration receives applications for relevant visa, scrutinizes eligibility and supporting documents and issues an invoice. The applicant is required to deposit the visa fees in cash or through direct transfer to NRO. The remittance slip issued by NRO is presented to the Department of Immigration and it then issues appropriate visa after another scrutiny.

RPC visa revenues comprise of visa fees for refugees, fees for asylum seekers, reimbursement for venue hire, maintenance, salaries of local and expatriate employees of RPC, security services, and others. The system in operation is that the Multi-Cultural Department uses the FMIS system to generate invoices based on nominal roll forwarded by the Australian Home Affairs in the first week of each month. The Australian Home Affairs, on receiving the invoices from GON, directly remits the amount in the Nauru Receipting account maintained by the Bendigo Bank in Australia. The Multi-Cultural Affairs Department is required to check the receipts with the invoices with the Bank statement and raising appropriate general ledger entries

Our test checks of VISA revenues could not be undertaken for the tests of completeness, occurrence, accuracy and classification for the following reasons.

- Bank deposit confirmations for select samples could not be found at the NRO, Multicultural Affairs Department or the Department of Immigration.
- Invoices raised by Department of Immigration and Multicultural affairs during the year were not available for verification.
- The Australian Home Affairs payments were made for the bulk of the invoices. These were not reconciled to bank account and invoices by the Multi-Cultural Affairs Department.
- Department of Immigration could not produce all the invoices raised by them during the year due to lack of proper hand over/take over of charge of the incumbents in the department as also loss of documents during the office renovation.

**Customs duties:** Customs duties are levied on tobacco, Alcohol, Sugar, Machinery/vehicles/equipment, petrol, Diesel and JetA1 and others. An importer submits a declaration of imports, either himself or through customs brokers, to the Customs office. Thereupon, customs officer checks all paper work for air freights/sea freights and stamps the declaration form. Importer thereafter, pays the invoiced amount to the NRO/Bendigo bank agency and obtains a receipt thereof. The receipt and invoice are submitted to the Customs officer who checks the amount against the invoice and an 'approved' document is returned to the importer to get the release of imported goods. At the backend, the NRO office posts the transaction in the FMIS against the customs related Head of Account.

As the department confirmed loss of all records pertaining to 2015-16, no audit could be performed.

**Taxation revenues:** Tax on businesses is levied on the rates calculated on profits /turnover as the case may be. There is a slab system for the rates to be applied. Tax returns are filed by the business owners upon TIN registration and is generally self-assessed. Tax amounts can be deposited in cash or through bank transfer at NRO/Bendigo Bank agency. There is no system of tax assessment by the tax officers and generally the compliance is ensured through periodical review of list of companies/employees liable to pay taxes. Non-compliance with tax payments invites fines and penalties.

Audit recommends that a system of checking of tax returns on a sample basis should begin to check so as to prevent revenue leakages due to understatement of turnover/profit or suppression of employee data.

• ***Review of internal audit function:***

- It is a requirement that the Finance department establishes sufficient and adequate internal controls and makes a representation that these controls are working efficiently and effectively. A system of internal audit, whether in-house or outsourced, is required to test these controls as to their efficacy and assure the management in their representational duties. A periodic and continuous check of its operations, governance and policy decisions is a requirement.
- It may be stated that one of the important parameters for the external auditors to place reliance on the internal controls relating to preparation of financial statements of the government is its internal audit capacity, independence and work plan. It has been noted that the Finance Department has not established an internal audit function.
- Our review of the internal controls noted several deficiencies in the financial controls system and leads us to conclude that the Finance Department is seriously deficient in terms of ensuring and representing on the adequacy of internal controls. A system of checks and balances and informal controls must be established in the Government.

• ***Review of Fixed assets register:***

- We expected the GON to have internal controls surrounding the fixed assets in its possession and that each asset being marked or numbered, system of periodic physical count performed and a well laid down system of procurement and disposal of assets to be in place. We noted that some of the assets are well identified but a large number still need to be recognized with unique numbers.
- It was noted that the GON has got its vehicles, furniture & fixtures, air conditioners and buildings revalued in Aug 2014 through the ADB consultancy firm to account for fair value of these assets to establish opening balances in accordance with the IAS 20 for the financial statements ended 30<sup>th</sup> Jun 2014.
- The financial statement ended 30 Jun 2016 shows net block in respect of Plant & Equipment (air conditions, vehicles, furniture) and buildings after adjusting depreciation at rates laid down in Accounting policy 3.4. Though the policy lays down straight line method of depreciation, the practice is to apply the depreciation rates on the written down net blocks of assets. This practice needs to be revisited and correct methodology applied.
- There is no system of maintaining proper Assets Register where each asset is identified, coded, linked with purchase order, date of purchase, cost and location of the asset monitored. The register must also record additions, deletions and transfers as well as maintenance costs for either capitalization or for expensing. There is a need to establish an SOP for this item of work.

- There is no system in place to record donated fixed assets, their valuation, maintenance expenses, and unique identification. As the financial statements are progressing towards accrual based accounting, in times to come, these donated assets will have to be treated as 'deferred revenue' items in the balance sheet.
- The draft register of assets cited by Audit showed several shortcomings such as (a) unreasonable useful life (furniture for 60 years, vehicles, 120 years etc). The register must be prepared professionally to capture all details and should enable calculation of fair value thereof.
- **Outstanding audit observations seeking management response: SCOPE LIMITATION**

We have issued 27 preliminary audit observations (POMs) and several Requests for Information memos seeking management response. Whereas a few POMs were responded to, there are several POMs pending response from the Finance Department and as such we are not in a position to conclude on several important issues that have financial implications, systems oriented controls management or the accuracy of the financial information included in the financial statements. These are subject to review for inclusion or exclusion from the final management letter to be issued after receiving comments from the management on this draft management letter.

Management is encouraged to respond to these memos as early as possible, but not later than one week of the receipt of this draft management letter.

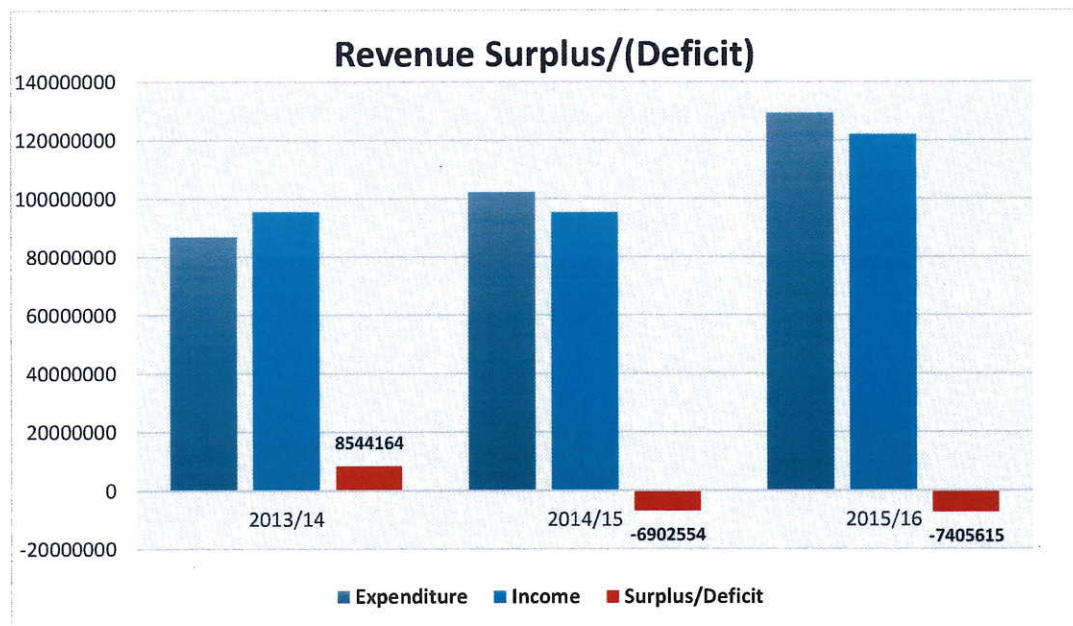
## PERFORMANCE ANALYSIS – KEY INDICATORS

Following findings are based on a set of parameters considered important in assessing the performance of the GON. We have selected a few key indicators to arrive at some conclusions using the Financial Statements prepared on cash basis and presented for audit as on 30.06.2016. The findings may undergo changes if the management revises the financial statements.

- **Analysis of Revenue surplus/ deficits**

As a good fiscal discipline, GON would be in an advantageous position if its receipts were more than its expenses. Such a situation would have enabled it to fund capital assets for generating higher GDP. Ideally, borrowed funds should be used for acquiring capital assets and not the consumption goods.

Using the presented information in the financial statements of the WOG accounts under IPSAS Cash, following is the trend of revenue surplus/ deficits over the last three years.



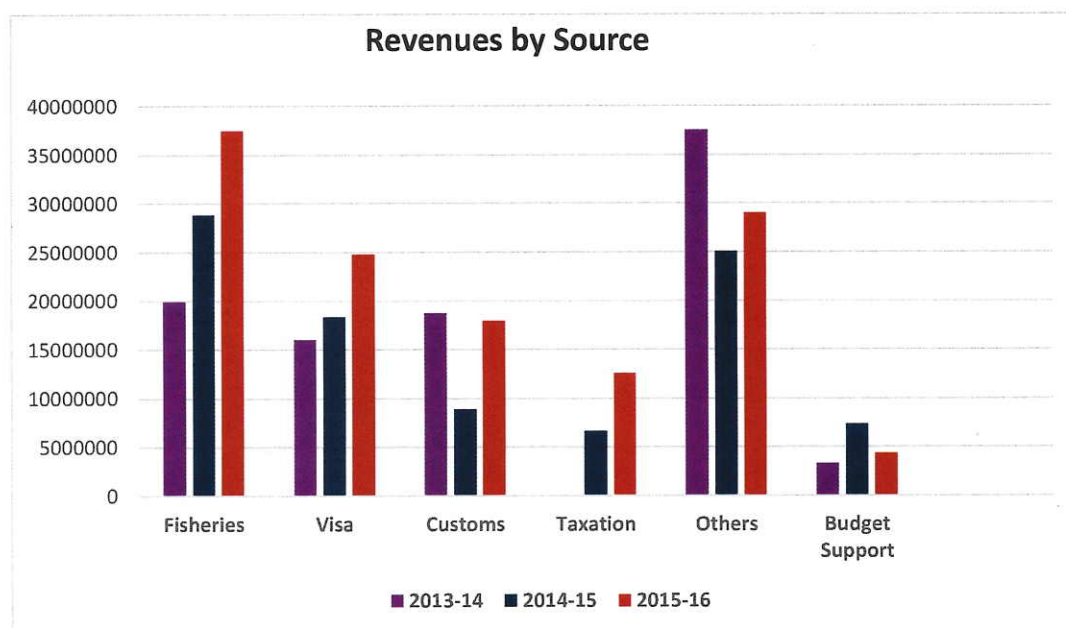
The revenue deficit in respect of 2015/16 is likely to be more than depicted if errors and omissions pointed out in the above sections of the report are adjusted in the financial statements ended 30 Jun 2016.

We have not worked out other deficits such as Budgetary deficit, Fiscal deficit or Primary deficit in the absence of credible financial information in the light of 'disclaimer opinions' on the earlier two years' financial statements from the Auditor General.



- **Growth of revenues by Source**

The main revenues of Nauru are Fishing licenses, Visa revenues, Customs duties and Tax revenues, aggregating to about 79% of the total revenues excluding General budget support received from other countries. Component level performance for last three years is tabulated below.

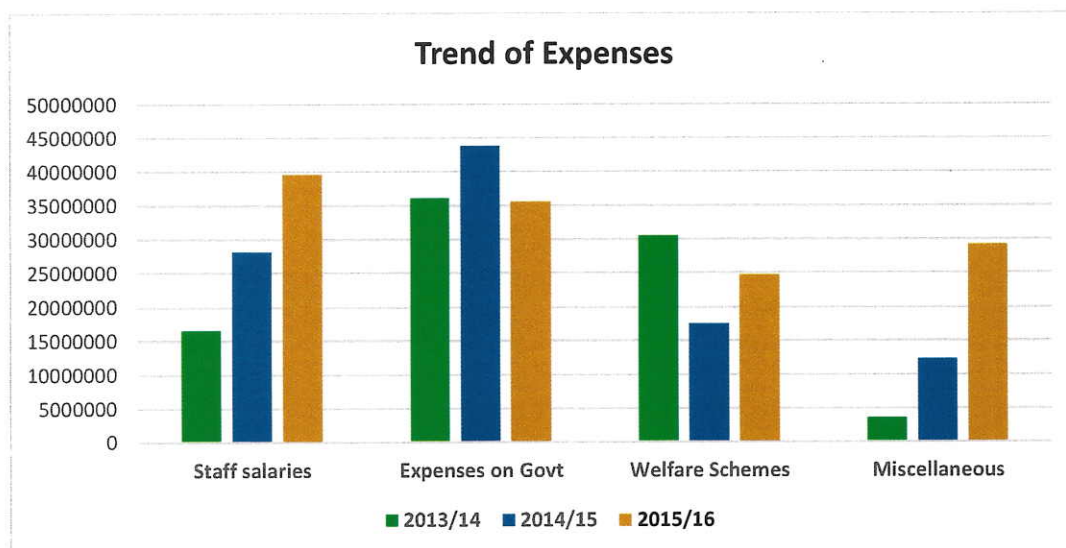


As could be noted from the chart above, revenues from Fisheries is gaining steady momentum over the last three years. There remains an issue related to 'others' where several types of revenues have shown wide fluctuations.

- **Trend of expenditure by application of funds**

The main role of the State is to ensure well-being of its people through direct expenditure on welfare schemes. However, spending on capital items generates steady economic benefits to be derived over the future years and contributes to higher GDP.

In order to ascertain the nature and extent of GON expenditure on various categories, we have segregated the figures for comparison purposes as (a) Staff salaries, (b) Expenses on Govt, (c) Welfare schemes, and (d) Miscellaneous.



Overall, expenses on government for managing the affairs of the State have remained more or less static. Staff salaries have gradually increased over the last three years thereby cornering the highest budgetary outlay during 2015-'16. The total spend on welfare schemes for the people at large is on the decline. However, this is partly off-set by funds set apart for Nauru Trust Fund and expenditure to meet Nauru Housing Scheme, both of which may be termed as welfare oriented expenditure although included in Miscellaneous Expenditure.

- **Use of borrowed funds**

In the absence of disaggregated information in the Finance Department, and audit concerns with the figures of domestic borrowings and external borrowings, we are not providing any analysis given the credibility of the amounts included in the financial statements.

The rationale of analyzing the use of borrowed funds is primarily to understand if GON is borrowing in order to meet the consumption needs or for capital goods. The result of such analysis would throw up issues of debt servicing and management of consumer goods in the country.

- **Returns from GON investments**

GON has invested in its seven State Owned Enterprises (SOEs) over the years. Whereas it is receiving some amount of dividends from certain SOEs, the figures of investment are not included in the financial statements. As a result, it is not possible to calculate the percentage return on its investment and whether it is an acceptable rate of return in GON context.

- **Indebtedness**

In the absence of credible information on its payables and loss of original records evidencing liabilities, it is not possible to calculate indebtedness of GON at this juncture.

- **Indicators of financial performance**

In view of the above scope limitations as to available financial information, we are not in a position to plot and evaluate the trend of GON financial performance in terms of its (a) sustainability, (b) flexibility, (c) vulnerability, and (d) transparency.

- **Going concern evaluation**

As long as the Government of Nauru is able to lawfully levy the taxes and duties, collect them and make budget appropriations through Parliament; it may be taken as a 'going concern' in accounting terms.

We have noted that,

- a) all reasonable precautions have been taken to safeguard the collection of public moneys and that the laws, directions or instructions relating thereto have been duly observed; and,
- b) all moneys appropriated or otherwise disbursed have been expended and applied for the purpose/s for which the grants were made by Parliament and that the expenditure generally conforms to the authority which governs it.

Analysis of current assets with current liabilities should ideally indicate if GON would be able to meet its liabilities in short term. The available figures indicate that it can meet its obligations in the short term.

## SUMMARY STATEMENTS AND OVERALL CONCLUSIONS

### ***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the international Accounting standards (IPSAS Cash) read with International Financial Reporting Standards (IFRS) and Audit Act 1973, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### **Overall Conclusions**

Because of the significance of the matters and materiality of the amounts under audit observation as described in the draft management letter above, we have placed a number of scope limitation on several issues as also questioned the accuracy of figures and presentation matters that must be aligned to IPSAS cash standards.

If the management does not comprehensively provide information on the issues contained in the draft management letter, and revise the financial statements; we will be constrained to express 'disclaimer' opinion on the financial statements.

\*\*\*end\*\*\*



**Annexure 1**

**Non-current assets**

**Movement in 2015-16 (amount in AUD)**

	Plant & Equipment				Buildings
	Furniture	Air conditioners	Motor vehicles	Total	
<b>01-Jul-15</b>					
Gross Carrying amount					
Accumulated depreciation					
Net carrying amount					
<b>Movement in 2015-16</b>					
Additions					
Disposals					
Disposals depreciation					
Total Movements in 2015-16					
<b>30-Jun-16</b>					
Gross Carrying amount					
Accumulated depreciation					
Net carrying amount					

**Movement in 2014-15 (amount in AUD)**

	Plant & Equipment				Buildings
	Furniture	Air conditioners	Motor vehicles	Total	
<b>01-Jul-14</b>					
Gross Carrying amount					
Accumulated depreciation					
Net carrying amount					
<b>Movement in 2014-15</b>					
Additions					
Disposals					
Disposals depreciation					
Total Movements in 2014-15					
<b>30-Jun-15</b>					
Gross Carrying amount					
Accumulated depreciation					
Net carrying amount					

**Annexure 2**

Suggested format for comparison of budget with actuals.

**STATEMENT OF COMPARISON OF BUDGET AND ACTUAL AMOUNTS – REVENUE 2015-'16**  
**for the year ended Jun 30, 2016**  
**(in Australian dollars)**

Head of account Revenue	Original Budget	Revised budget	Actual	Difference	Main reason for difference

Head of account Expenditure	Original Budget	Revised budget	Actual	Difference	Main reason for difference