

**DEMOCRATIC REPUBLIC OF TIMOR-LESTE  
CONSOLIDATED FUND OF EAST TIMOR**

**MANAGEMENT REPORT**

**30 JUNE 2005**



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## **INTRODUCTION**

We have completed our audit of The Consolidated Fund for East Timor (CFET) for the financial year ended 30 June 2005 and have issued an unqualified audit report.

### ***Scope and responsibilities***

We conducted an independent audit of the financial report in order to express an opinion on it to the President and Honourable Members of the National Parliament of Timor-Leste. Our audit was conducted in accordance with International Standards on Auditing in order to provide reasonable assurance as to whether the financial report is free of material misstatement.

Our procedures included examination, on a test basis, of evidence supporting the amounts and other disclosures in the financial statements. Our audit also included assessment of the accounting principles used and the significant accounting estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion. The nature of an audit is influenced by factors such as the use of professional judgement, selective testing, the inherent limitations of internal control, and the availability of persuasive rather than conclusive evidence. Therefore, an audit cannot guarantee that all material misstatements have been detected.

The Ministry of Planning and Finance, Office of the Treasury is responsible for preparing a financial report that presents fairly the financial position and performance of the government and the consolidated entity. This includes responsibility for the maintenance of adequate accounting records and internal controls that are designed to prevent and detect fraud and error, and for the accounting policies and accounting estimates inherent in the financial report.

### ***Independence***

We are independent of the Ministry of Planning and Finance, Office of the Treasury, and we have met the independence requirements of the International Federation of Accountants ("IFAC") Code of Ethics for Professional Accountants.



## **EXECUTIVE SUMMARY**

### ***Key Financials***

The consolidated entity achieved revenues of US \$288 million for 2005, an increase of 168% over the 2004 revenues of US \$107.66 million. The majority of this increase relates to Timor Gap tax revenues of US \$209 million (increase by US \$171 million over the 2004 year revenue of US \$38m). Total expenditure incurred during the year amounted to US \$80.26m compared to the previous year of US \$73.05 million, representing an increase of nearly 9.9% over 2004. As indicated in the table below, the increase relates to all areas of expenditure with Capital expenditure percentage increases most significant at 22.6% in the 2005 year.

In total, the Government of the Democratic Republic of Timor-Leste recorded an excess of revenue over expenditure of US \$208.22 million in 2005, in comparison to a surplus of US \$34.61 million in 2004.

Summary of financial performance, for the Whole of Government (in millions of \$US):

Item	2005	2004	%Change
Revenue	288.48	107.66	168.0%
Less expenditure:			
Salaries	25.57	24.21	5.6%
Goods and Services	42.58	38.96	9.3%
Capital	12.11	9.88	22.6%
Total expenditure	80.26	73.05	9.9%
Surplus (deficit)	208.22	34.61	

As at 30 June 2005, the Government of the Democratic Republic of Timor-Leste, held cash and cash equivalents totalling US \$348.05 million (30 June 2004 - US \$80.9 million). These funds are almost all held with the Banking and Payment Authority ("BPA") of the Democratic Republic of Timor-Leste. It is our understanding that the BPA has the responsibility for the control and investment of the funds. Outstanding commitments recognized by the Government at 30 June 2005 totalled US \$19.51 million (30 June 2004 US \$16.47 million).

### ***Audit report modifications***

As noted, our audit report is not qualified, however we have clarified the scope section of the report to reflect that our audit was directed at verifying the amounts deposited to and paid from the relevant bank accounts of the Consolidated Fund of East Timor. In additions, additional explanation was included regarding our audit not covering off on completeness of electricity charges revenue.





## EXECUTIVE SUMMARY (CONT'D)

### *Key audit findings*

Our examination for the year ended 30 June 2005 disclosed a number of other matters, which are appropriate to be brought to your attention, these are included in the accompanying report.

Some of the more important items highlighted during our audit are as follows:

- As the major source of revenue of the Government of Timor-Leste, the Timor Gap Tax Revenue services warrants a structured and formal audit process on the tax returns submitted by the various entities operating in the region.
- Monies collected and recorded as revenue by Treasury are not reconciled with the revenue recorded in the various individual agencies, other than in the Lands and Property Division of Ministry of Justice and in the Ministry of Health.
- During our audit we noted the deficiencies in the Power Invoicing Management System ("PIMS") as used by the Power Service remained as in the previous years.
- No evidence of reconciliations between the ETRS Domestic Tax revenue system with the Treasury records and instances were noted where the domestic tax was classified incorrectly.
- Our visits to the district offices identified a number of issues concerning non compliance with the Treasury procedures and lack of documentation. These are outlined in the detailed report.
- In the area of payroll, a number of issues were noted that represented a breakdown in the controls as outlined in the detailed report.
- There is concern that there are a limited number of trained individuals with adequate back up knowledge and skills to prepare the financial reports.
- The format of the Annual Financial Report and Accounts appears to be unnecessarily complicated and in some respects not that useful or meaningful to the users of the financial reports.

Please refer to the attached schedules for further details regarding our most important audit findings.

We acknowledge that the Democratic Republic of Timor-Leste is still in its early years of operation and is still in the formulation process of policies and procedures. We further understand that this is a significant task for the new government especially as the level of international staff assistance continues to decline.

We are also pleased to note that a number of significant improvements have recently been made to the Government's accounting processes. In particular, we note the following issues arising out of the 2004 audit which have been addressed by the Government in the intervening period.

- Individual agencies are maintaining asset registers, although as detailed below, significant improvements can be made to these registers;
- The Payroll section has continued to improve their system of internal controls with respect to ensuring that payroll transactions are appropriately authorised;
- There has been a substantial improvement in the debt collection by Power and the installation of the prepaid meters has helped improve the collections.



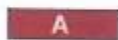
## MATTERS ARISING

The following schedules set out further details of issues arising from our audit. A number of the issues identified were also raised in the prior year. We have colour coded our priority ratings to enable major weaknesses to be easily identifiable. The key to the colour ratings is listed below the matters arising.

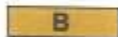
Schedule	Audit Issue	Rating	Issue Raised in Prior Year
<b>1</b>	<b>Timor Gap Revenue</b>		
	1.1 Insufficient audit function Timor Gap revenue	A	
	1.2 Inability to locate monthly returns	A	
<b>2</b>	<b>Domestic Revenue</b>		
	2.1 Agencies not reconciling revenue to Treasury revenue reports	A	
	2.2 Revenue not banked by some Agencies	A	
<b>3</b>	<b>Power Authority</b>		
	3.1 Integrity of PIMS Invoicing System	A	√
<b>4</b>	<b>Bank Reconciliations</b>		
	4.1 Outstanding reconciling items	B	
<b>5</b>	<b>Payroll</b>		
	5.1 No record of changes to payroll master file	B	
	5.2 No evidence of cash payments to employees in Dili	B	
	5.3 Payroll duplication process	C	
<b>6</b>	<b>Underutilised Salaries and Wages Budget</b>		
	6.1 Underutilised salaries and wages budget by Agencies	B	
<b>7</b>	<b>Asset Register</b>		
	7.1 Asset Register not maintained adequately	B	√
<b>8</b>	<b>Visit to Districts</b>		
	8.1 Maintenance of records in district finance offices	B	
	8.2 Retirement of district imprest by the Agencies	B	
<b>9</b>	<b>Procurement</b>		
	9.1 No CPVs for Multiple Agency Expenditure	B	√
	9.2 Carried forward liabilities due to delays in project execution	B	
<b>10</b>	<b>Investment of Funds</b>		
	10.1 Investment of funds held by the Banking and Payment Authority	B	



### Ratings



A major weakness that you must address soon.



An important matter that will significantly improve the control environment, the accounting system or the operations of the business.



A minor weakness that you should nevertheless address to improve the control environment, the accounting system or the operations of the business.





## **GENERAL**

The comments made above do not imply any lack of integrity or honesty on the part of the management committee and employees of the government. We have received comments on our management letter from the management and they are incorporated in this report.

As part of our audit procedures, we considered the Treasury's system of internal control to establish the level of our reliance on the system in determining the nature, timing and extent of other auditing procedures necessary to enable us to express our audit opinion. This work is not primarily directed towards the discovery of weaknesses or the detection of fraud or other irregularities and should not, therefore, be taken to assure that no other weaknesses exist. Accordingly, the comments in this letter refer only to those matters, which have come to our attention during the course of our normal audit work and do not attempt to indicate all possible improvements, which a special review might identify.

We wish to take this opportunity to thank you and your staff for the assistance given to us during the course of our audit.





## DETAIL SCHEDULES

### 1 Timor Gap Revenue

#### 1.1 Insufficient audit function Timor Gap revenue

**Issue:** The audit function relating to the tax revenue received from taxpayers operating in the Timor Sea area appears to be inadequate.

**Observation / Effect:** Currently the Timor Gap taxes paid by taxpayers are collected under a self assessment system. Whilst the existence of a self assessment tax system is not a problem in itself, the absence of tax audit on a regular basis raises concerns about the integrity of the information provided by taxpayers. At the moment, the only control in the Timor Gap revenue collection process is the checking of the calculations made by taxpayer in their tax assessment form by the recording officer. There does not appear to be any formal audit conducted on the Timor Sea Revenue.

The effect is that due to the inadequate controls in place the revenue collected by Agencies can not be easily verified. Hence the completeness of the Timor Gap revenue recorded can not be verified prior to it being recorded in the bank accounts of the Government.

We note that from 1 July 2005, the Timor Gap tax revenue is to come within the ambit of the Petroleum Fund of East Timor ("PFET"). This matter will remain relevant particularly as to the scope of the audit function of the PFET.

**Recommendation:** We recommend that tax audits are conducted on a regular basis particularly with the increase in the amount of revenue generated from this source. As the principle source of revenue (73%) a formal and structured audit process is warranted. The Timor Sea revenue unit advised that they had conducted audits of corporations with respect to the Withholding Tax returns, however there was no evidence sighted of any audit on the Business Tax returns of the corporations, which is the major source of revenue. Further, there are also only a few companies operating in the region which would make the audit reasonably simple.

**Management Response:** In addition to the regular checking of the calculations in the taxpayers' monthly forms and annual tax returns, Petroleum Tax Division has conducted some regular audits under the Law on Income Tax and also has conducted other audits to finalize some refund cases during the fiscal year 2004-2005. The audits were conducted for different type of tax obligations, such as special calculation of tax under Article 15 & 25, withholding tax and annual income tax. The verification audits regarding special tax calculation under Article 15 & 25 were conducted for two



taxpayers, which are ENSCO OFFSHORE INTERNATIONAL TIN-2000373 and DIAMOND OFFSHORE GENERAL COMPANY TIN-2000005. After the audit, Ensco's original refund claim for \$ 1,795,275.07 was finally reduced to \$ 699,439 which was subsequently refunded. An additional tax assessment of \$ 318,587.99 was raised on Diamond Offshore which was successfully collected after the audit. Another audit was conducted on withholding tax issue of TIDEWATER MARINE AUST PTY LTD TIN 2000542. After conducting the audit, Tidewater Marine's refund claim of \$ 118,132 were found correct, which were not refunded but the taxpayer were allowed to adjust the refund against its future tax liability.

The audits regarding the annual income tax returns were also conducted for McDERMOTT (AUST) PTY LTD TIN- 2000334 for the tax years 2000, 2001, 2002 and 2003, for HYDRO MARINE SERVICE INC TIN-2000327 for the tax years 2002, 2003 and 2004 and CGG AUSTRALIA PTY LTD TIN- 2000398 for the tax years 2002 and 2003. After the audit, the refund issues of McDERMOTT and HYDRO were settled and CGG's refund claimed was refused.

Petroleum Tax Division of the TLRS is committed to conduct audit on a regular basis but the resource constraints such as staff shortage (only two permanent staffs are working in this division), lack of professional skills and the location of the petroleum taxpayers (petroleum taxpayers are located in Australia, Singapore and other places abroad) require us to prioritize the work. Audit of all major operating companies would be time consuming and difficult process.

In addition to regularly administering the existing tax laws, advising and updating the taxpayers about the new laws and regulations, monitoring the tax payment and tax form lodgement obligations of the taxpayers, the Petroleum Tax Division is currently training its staff to improve their professional skills on tax audit procedures. We ensure that tax audit issue is a priority for the Petroleum Tax Division of the TLRS.

**Audit Conclusion:** We are please to note the Petroleum Tax Division of TLRS is committed to regular audits. We do emphasise the importance of a structured and regular audit function on the Timor Gap revenue.





## 1.2 Inability to locate monthly returns

**Issue:** The Timor Sea Revenue Service was unable to locate monthly returns for three of the companies operating in the region.

**Observation / Effect:** Although the Timor Sea tax revenue is collected on a self assessment basis, the revenue remitted by the taxpayer should be checked to the monthly return or remittance that is lodged by the taxpayer with the revenue service. We were unable to locate returns for the following companies operating in the Roxer Pty; Tideware Marine Australia Pty Ltd & Total Marine Services Ltd

**Recommendation:** As the principle source of revenue of the Government we recommend that all the revenue is checked to the monthly returns and other supporting documents relating to the taxpayer. After the revenue is checked to the returns, the documents should be properly maintained. It would also be appropriate to ensure that the revenue received is reconciled to the remittance advice or other information that is received from the taxpayer.

**Management Response:** The Petroleum Tax Division of TLRS is regularly monitoring the tax payment and lodgment of monthly and yearly tax forms. The revenue received is also reconciled with the remittance forms and tax forms. Often the taxpayers are advised to explain any issue that arise from the reconciliation. Usually, we receive the copy of credit advice from BPA against every payment immediately but receive the tax forms after one or two months if the taxpayer sends the form through postal mail. This may be one reason why one or two monthly forms could not be located in ROXAR PTY LTD TIN- 2000599. However, ROXAR is now regular in sending its forms through postal mail. We have corresponded with TideWater Marine TIN- 2000542 several times to lodge the monthly forms regularly; it has started lodging the forms now but still not regular. Total Marine Services Pty Ltd TIN 2000408 was regularly lodging the monthly tax forms till March 2005. We will keep following up the issues with the taxpayers through e-mail. Since taxpayers are far away from Timor-Leste, it is not always possible to visit taxpayers frequently. However the audit issue is noted for compliances as much as possible.

**Audit Conclusion:** We note the attempts to improve the maintenance of documentation and will review the issue again at the next audit.



## 2 Domestic Revenue

### 2.1 Agencies not reconciling revenue to Treasury revenue reports

**Issue:** The monthly revenue reports that are sent out by Treasury to the individual Agencies are not being reconciled by all the Agencies to their individual revenue records.

**Observation / Effect:** Treasury produces monthly revenue statements that are sent to the Agencies for them to reconcile to their revenue records. From our visit to a number of Agencies, we noted there was no evidence that these reconciliations were performed by the Agencies other than in the Land and Property division of the Ministry of Justice and the Ministry of Health. This is a major weakness in the control system and has the following effects:

- Treasury does not know the exact amount of revenue collect and recorded by the Agencies;
- It gives rise to difficulties in ensuring that all monies collected have been properly recorded and banked;
- It gives rise to difficulties in ensuring that there is completeness in revenue collected.

**Recommendation:** We recommend that reconciliations should be carried out by the Agencies regularly, and preferably monthly. A report on the reconciliation performed by the Agencies should then be provided to Treasury. This will enhance the ability of management to detect error or fraud, and decrease the possibility of discrepancies occurring between the general ledger and the bank account. It will also ensure that all money collected by Agencies is banked.

**Management Response:** The Audit issue and recommendation are noted. Although regular reconciliation is being conducted by the agencies collecting major revenues of the Government, some departments mostly collecting smaller amount of revenues are not paying adequate attention on the subject. This will be taken up with the concerned agencies. Sometimes due to involvement of small amount as well as lack of awareness the agencies do not carry out the required reconciliation. As observed by the audit, the reconciliation is an important control mechanism and it should be regularly carried out by the agencies irrespective of the amount involved in it.

**Audit Conclusion:** We are satisfied that Treasury recognises the importance of the control mechanism and we will review it again at the next audit.





## 2.2 Revenue not banked by some Agencies

**Issue:** As with previous years there are still some Agencies that are not banking all the revenue received by the relevant Agency.

**Observation / Effect:** Judiciary collects revenue such as court fees which is not banked into the Treasury account. As observed in the previous year, some areas of the ministry does not bank all the revenue received into the Treasury account thereby constituting a breach of section 5 of the UNTAET regulation 2001/13 which prohibits holding public funds without authorisation by legislation or by the Head of the Central Fiscal Authority. This breach also has consequences on the completeness of revenue, given the Government's financial records are maintained on a cash basis and therefore it only records revenue when it is banked. The effect of such a breach is that the revenue recorded is understated.

**Recommendation:** We understand that there is proposed legislation to allow the retention of funds by the Judiciary. It is however recommended that until such time as the legislation is enacted, all revenue should continue to be banked into the Treasury account.

**Management Response:** In fact the legislation has been enacted and the Judiciary has not yet started complying with the legislation. The Audit issue and recommendation are noted. This will be brought to the notice of the Judiciary for necessary action.

**Audit Conclusion:** Satisfactory.



### 3 Power Authority

#### 3.1 Integrity of PIMS Invoicing System

**Issue:** As we noted with the previous year audit, the Electricity Service of Timor Leste (Power) had not addressed the issue with its billing and invoicing system (PIMS). The PIMS system also cannot be relied upon to determine the amount of outstanding debtors.

**Observation / Effect:** The billing reports generated from the PIMS does not appear to be reliable, due to apparent inaccuracies in the PIMS system, however, the level of accounts receivable cannot be estimated with any confidence, nor are we able to quantify the errors. We were unable to verify the balance of outstanding power invoices. Also, it is not possible to determine whether the government is collecting all the power revenue that it is entitled to.

**Recommendation:** We acknowledge that Treasury and Power are aware of the problems associated with the Power Authority. We understand that a complete review and update of the PIMS system is in progress and that a contractor was engaged to undertake the project in the last financial year.

We strongly recommend that this issue be addressed at the earliest to ensure that the parameters of the system can enable the calculation of accurate information.

We further recommend that a formalised debt collection policy be put in place to ensure that payments are received on a regular basis, also to identify and limit potential bad debts.

**Management Response:** The new billing system will be operational with effect from 1<sup>st</sup> December and this will include reports such as the 'balance outstanding power invoice' based on the data-input after 1<sup>st</sup> December. EDTL is working to put in place a formalized debt collection policy. It is expected that the process will be finalized before the end of 3<sup>rd</sup> quarter of the fiscal year 2005-06.

**Audit Conclusion:** We are pleased that action is being taken but note that this has been an issue since 2003 audit. This will be reviewed again at the next audit.



#### 4 Bank Reconciliations

##### 4.1 Outstanding reconciling items

**Issue:** The outstanding reconciling items in the bank reconciliations need to be followed up on a regular basis.

**Observation / Effect:** Our review of the monthly bank reconciliations performed during the financial year noted a large number of reconciling items remained unreconciled during the year. Despite the fact that these were not all material amounts, the existence of a large number of reconciling items could indicate that they are not being regularly followed up and analysed for correction. We did note that in the bank reconciliation for July/August 2005 most of the reconciling items had been cleared.

**Recommendation:** We recommend that the reconciling items, particularly those that have been outstanding from previous periods are reviewed regularly. The process that was undertaken in the July/August 2005 reconciliation should be continued throughout the year.

**Management Response:** The Treasury conducts bank reconciliation on a regular basis. As a part of continuous process of 'bank reconciliation', necessary review and actions are also being taken to clear the outstanding items. At any particular point of time there will always be a considerable number of outstanding items due to, for example, late encashment of cheques by the recipient, reporting of collection of revenues made by the banks, etc. Such pipe-line items are cleared on a regular continuous basis as and when necessary information is received from the banks or the agencies. Audit has also observed, during July/August 2005 most of the outstanding reconciling items pertaining to the last fiscal year, have been cleared. In spite of all the actions there may still be some old outstanding items, for example, non-encashment of some old cheques or some kind of misclassification of expenditure or revenue, etc. Actions on such cases can be taken only on receipt of proper certification by the concerned bank. The banks are requested from time to time to provide such certificates. Reconciliation is an important control issue and it is expected that the audit would also review the entire process during the next audit.

**Audit Conclusion:** The issue will be reviewed at the next audit.





## 5 Payroll

### 5.1 No record of changes to payroll master file

**Issue:** There is a risk that changes may be made to the payroll master file with respect to contracts and new staff without proper authorisation.

**Observation / Effect:** The payroll staff have authorisation to make changes to the employee's master file and to create new employees. Although it appears that procedures in place to minimize the risk seem to be working, there is no final report detailing all the changes made in the master file of the employees that could be reviewed by the supervisor. Monthly reports that list changes to the master file are not being generated and maintained.

**Recommendation:** We strongly recommend that procedures be implemented for the review of changes to the payroll master file on a regular basis. This will help ensure that all new data and changes to the payroll details are authorised.

**Management Response:** The Payroll system CHRIS has an in-built security control feature. The authorized person can only log into the system. The head of the payroll unit is responsible in providing access to the authorized staff in the payroll unit. The creation and editing of the civil servant's record are carried out in the system only by the authorized official of the payroll unit on the basis of approved documents received from the concerned department and endorsed by the department of Human Resources and Public Employment.

As such it may be observed that every change in the payroll data is carried out by the officials duly authorized to do so. Due to the functional requirement the task has been delegated with proper authorization for processing the monthly payroll of the individual agencies. In fact the regular control mechanism and the reconciliation process at present, are with the respective agencies, not with any central body or agency. However, as observed by the audit, the issue will be taken up with the vendor of CHRIS so that a consolidated report is also generated from the system, which will then be reviewed by the head of payroll unit

**Audit Conclusion:** Satisfactory





## 5.2 No evidence of cash payments to employees in Dili

**Issue:** Treasury does not maintain any evidence of the salary payments made to the Dili District employees where such payments are made in cash.

**Observation / Effect:** Those Dili District's employees that are paid their salaries in cash receive their payments at the Banking and Payment Authority ("BPA"). The BPA keeps the supporting documentation (payslip) of these transactions. Should there be any dispute or complaints about the cash payments made to the employee, the payroll department will have no evidence that such payment was made.

**Recommendation:** It is recommended that the Treasury payroll department implement procedures to maintain evidence of the payments made to employees, particularly where such payments are made in cash. Such evidence will assist the Treasury should there be any dispute or complaint by an employee in relation to the payment of salaries.

**Management Response:** At present the list of the civil servants to be paid their 'salary and wages' in cash is provided with the Banking and Payment Authority (BPA) which is the official banker as well as the cashier of the Government. As proof of disbursement of such 'salary and wages' all the documents are kept by them and a report to the effect is sent to the payroll unit. Should there be any dispute or complain from any civil servant, the BPA would be asked to provide necessary proof of payment in response to such complain. So far, however, such incidence has not taken place. Accordingly, neither any functional nor any administrative problem is envisaged. Since the cash payment has taken place at the counter of the BPA, the original document of disbursement will be kept by the BPA. At best the BPA may be requested to provide the payroll unit with the copies of these documents, although this will result in additional work with the BPA and additional papers with the payroll unit.

**Audit Conclusion:** It is important that adequate documentation is maintained as evidence of the payment of wages. If it is decided that only BPA is to maintain the documentation, there should be clear agreement between Treasury and BPA to the effect.



### 5.3 Payroll duplication process

<b>Issue:</b>	The Salary Payments report generated by CHRIS (Payroll System) each month is sorted and arranged before being sent to Banking and Payment Authority ("BPA").
<b>Observation / Effect:</b>	This represents a duplication of tasks and increases the risk that the output of the system may be manipulated.
<b>Recommendation:</b>	We would recommend that the CHRIS software reporting system be amended to ensure that the CHRIS system reports are not manipulated before they are sent to BPA. Adjustments should be authorised and made through the system.
<b>Management Response:</b>	It may be observed that the payroll is processed agency and program wise. Afterwards further 'sorting' is required for arranging the different modes of payment like cash, transfers etc. At the end, the control totals are checked and also reconciled with the system data base. Such duplication of task is unavoidable. However, the issue and recommendation of the Audit are noted and the matter will be taken up with the vendor of CHRIS for generation of additional reports in this regard.
<b>Audit Conclusion:</b>	Satisfactory



## 6 Underutilised Salaries and Wages Budget

### 6.1 Underutilised salaries and wages budget by Agencies

**Issue:** The salary and wages expenditure is substantially below budget for most Agencies.

**Observation / Effect:** The overall payroll budget for the financial year was \$28.2 million compared to the actual expenditure of \$25.4 representing an under expenditure of approximately \$2.8 million.

While the under utilisation of the payroll budget could indicate expenditure restraint, it is important that the key positions are filled particularly in Agencies such as Finance to ensure there are adequate controls operating in the relevant Agencies.

**Recommendation:** It is recommended that the Agencies ensure that all the key positions are filled to make sure they are operating adequately and that adequate controls are in place. Alternately the budget should be carefully reviewed in order to assess whether it correctly reflects the funding requirements of the relevant Agencies.

**Management Response:** It is agreed that all the key positions should be filled in order to provide an efficient and effective public service. Accordingly, these posts are being filled as and when the suitable candidates are available. This is also evident from the staffing profiles of last few years. The Government does not find it appropriate to fill such key posts with the candidates who are not found to be suitable as it would not serve the purpose of achieving the efficient and effective public service. However, in some cases wherever possible, the Government has appointed staff on 'acting' basis.

In the beginning of the year the budget for the 'salaries and wages' is prepared on the basis of the 'staffing profile' of the respective agencies, not on the basis of the posts actually filled-in. It is not feasible to approach the Parliament frequently for supplementary appropriation. As a result the provision in the budget of 'salary & wages' is found to be more than the actual need. However, the point raised in this issue is noted and necessary actions will be taken, as far as possible, during the mid-year or supplementary 'budget proposal' to revise the budget of the 'salary and wages' so that the underutilized amount in this category is reduced.

**Audit Conclusion:** Satisfactory.





## 7 Asset Register

### 7.1 Asset register not maintained adequately

**Issue:**

The full listing of assets of the Government of Timor-Leste is yet to be completed and again this year no complete physical verification of the assets of the Government was undertaken. Asset registers require additional work to ensure they are as free of discrepancies, as complete, and secure as possible.

**Observation /  
Effect:**

This issue was identified in the previous year and continues to be an issue this year. In particular the following issues are outlined in regards to assets held by the Government:

- The detailed listing of assets has not been completed to include all assets purchased or donated to the Government;
- Land and Buildings and infrastructure assets have not been recorded or valued;
- The detailed listing of assets is maintained on an Excel spreadsheet, without adequate backup or procedures to maintain the security of the register;
- In some cases new assets are not being assigned asset identification numbers;
- Our audit of the available listing highlighted a number of errors in either the description, serial number, cost or location of the assets;
- Most Government Agencies have prepared detailed listings of assets, however these listings have not been reconciled to actual purchases of assets for the year;
- Individual Agency asset listings have not been crosschecked to the full listing of assets;
- No regular check/count of assets had occurred; and
- The condition of the asset should be reassessed and the register updated to reflect the current condition.

If assets are not recorded on a detailed asset register and identified by way of an asset number the risk of assets disappearing increases. Furthermore if the Government adopts accrual accounting it will prove to be a very time consuming task to compile a detailed listing of all assets. We understand that the asset register is being updated and that when the register is completed the details will be downloaded into Freebalance asset module.

**Recommendation:**

We refer to the management letter issue raised in the previous year and recommend that a full physical verification of all assets be undertaken prior to the listing being downloaded into Freebalance. Asset registers should be maintained for all Agencies and regular counts of assets should be undertaken to ensure that the asset still exists and is in good working order.





**Management  
Response:**

The National Assets Management Unit could not complete physical identification of all the Government assets during the last fiscal year, mainly due to the fact that several donated assets from different sources kept on being received by various departments of the Government. The physical identification of the assets in the districts is likely to be completed soon and thereafter that will be followed at the national level. After the physical verification and identification process is complete, the Asset Register will be completed both for the assets purchased and donated.

Regarding the Land and Property assets, an appropriate system as well as the format of the data base is being worked out. The appropriate mechanism is being worked out in consultation with the Land and Property Division of the Government.

The National Assets Management Unit is still maintaining the detailed listing of assets on the Excel Spreadsheet, but the backup is taken in the server. Once the data base is finalized with proper identification and verification, the data base will be uploaded in the Free Balance system.

At present all the new assets are assigned barcodes on its arrival.

Some errors in respect of serial no., cost, location of the assets etc. are caused by various departments of the Government. They are being reconciled from time to time. The National Assets Management Unit will also be conducting workshops for the logistic officers of various departments towards elimination of such errors and awareness of assets management procedures as well as that of the appropriate data base.

As mentioned above the physical identification of the assets in the districts is likely to be completed soon and thereafter that will also be followed at the national level. During this process of identification, verification as well as condition of assets will also be assessed and the Asset Register will, accordingly, be updated.

**Audit Conclusion:** The issue will be reviewed at the next audit.



## 8 Visit to Districts

As part of our audit procedures we conducted field visits to the districts of Liquica, Bobonaro, Suai, Aileu and Manatuto and observed a number of issues with respect to the accounting records and financial procedures.

### 8.1 Maintenance of records in district finance offices

**Issue:** From our visits to five districts it was observed that financial records were not maintained or updated in District Finance Offices in accordance with procedures laid down in the Treasury Manual and Expenditure Procedures.

**Observation / Effect:** It was observed from our visits to the districts that the District Offices are not maintaining/updating records. These are:

- The format of Cash Books was not as per format laid down;
- Cashbooks are not sequentially numbered;
- Despite instructions issued by Treasury the District Finance Offices are updating the electronic cash books regularly while updating of Manual Cash Books receives less priority;
- Periodical Cash Verification not conducted regularly by District Administrator and District Finance Officer as prescribed in the instructions issued by the Treasury;
- Delay in depositing Cash Revenues collected by District Finance Offices;
- Payment Vouchers in the format designed by Treasury are not followed properly in the districts.

These represent a breakdown in the financial recording procedures and could affect the accuracy of the financial reporting.

**Recommendation:** It is recommended that the District Finance Offices adhere to the relevant procedures laid down in the Treasury Procedures Manual, Expenditure Procedures and instructions as issued by Treasury.



**Management  
Response:**

This issue has also been observed by the treasury. A continuous attempt by the international advisors has been there for the last 4-5 years in this regard. In addition there had been number of seminar/workshops conducted in Dili as well as in the Districts. Recently in August 2005 there was a three-day workshop held by the Treasury officials in Dili. This workshop was attended not only by the District Finance Officers but also by the District Administrators and the concerned Agency Officials. During the workshop adherence of all the provisions in the existing manuals, procedures, administrative instructions was emphasized and that had also been followed by number of practical exercises, particularly towards proper maintenance of the cash book. It is expected that with these continuous attempts, the standard and quality of maintenance of records in the district finance offices will further improve in near future. The District Finance Officers/District Administrators, during the recent workshop, have again been instructed/reminded specifically for discontinuation of electronic cash book, regular verification of cash, observing the proper format of cash book, payment vouchers, etc.

In the Districts, where there is no bank branch nearby, it may not always be feasible to deposit the small amount of revenue collected into the bank on daily basis. However the revenue officers/district finance officers are always instructed/advised to deposit the government revenue into the bank at the earliest and within the reasonable period of time. With the opening of bank branches in the districts this problem is likely to be eliminated in the near future.

Further, all the concerned officials in the districts, will be appraised of the issue and recommendation made by the Audit in these regard.

**Audit Conclusion:** We accept that action is being taken to address these issues.





## 8.2 Retirement of district imprest by the Agencies

**Issue:** Agencies are not adhering to proper laid down procedures while submitting the retirement documents against District Imprest and its settlement.

**Observation / Effect:** It was observed in checking the documents in District Finance Offices that Agencies are not submitting proper retirements leading to delay in settlement of the district imprest. Following instances were noted:

- Delay in submission of retirement documents to District Finance Offices;
- Expenditure incurred is not in order as per-sub allocated budget and the guidelines issued; this at times leads to excess/misclassified expenditure which is not acceptable to Treasury leading into delay in settlement of district imprest;
- Supporting documents not in proper format; and
- Instances of "withheld Items" at the end of financial year.

**Recommendation:** It is recommended that while issuing sub-allocation for the district operations, the Agencies should sub-allocate budget item-wise as approved in the budget document. Accordingly, while issuing the district imprest, the items in the budget of the Agencies would stand committed. The retirement could be checked against committed items.

**Management Response:** The Audit has very rightly pointed out the issue involving retirement of the imprest amount by the Agencies. This has also been observed by the Treasury. From time to time the international advisors as well as the district finance officers had brought such irregular retirements to the attention of the Agency officials at the Districts. The Treasury has also taken up such cases with Agencies at the national level. Without prior commitment of fund the Agencies at the national level are not in a position to control the expenditure at the district level. The issue and recommendation of the Audit have been noted and this will further be pursued with the Agencies both at the national and district level.

**Audit Conclusion:** Satisfactory.





## 9 Procurement

### 9.1 No CPVs for Multiple Agency Expenditure

**Issue:** Commitment and Payment Vouchers (CPVs) have not been issued for payments relating to multiple agency expenditure for mobile telephone costs, maintenance of photocopiers, custom broker agent fees and advertisement costs.

**Observation / Effect:** During our review of expenditure, we noted that for mobile telephone costs, maintenance of photocopiers, custom broker agent fees and advertisement costs, Commitment and Payment Vouchers (CPVs) had not been raised.

The ETTA Manual stipulates that for all expenditure items, the following procedure applies:

- a CPV is opened;
- the Procurement Unit issues a purchase order;
- a Sales Order is received from the supplier;
- goods/services and an invoice are received from the supplier.

We found that expenditures regarding mobile telephones, maintenance of photocopiers, custom broker agent and advertisement, goods/services and invoices had been received from respective suppliers but no CPV had been opened.

The absence of strict adherence to ETTA Manual procedures on Expenditure will give rise to a risk of unauthorised expenditure and loss to the Government.

**Recommendation:** We recommend that strict adherence to the ETTA Manual with regard to Expenditure be enforced and controls be introduced to this effect.

**Management Response:** The issue and recommendation of the Audit have been noted. Such system of multiple agency expenditure was inherited from the UNTAET. The Government has been taking necessary actions to discontinue occurrence of such multiple agency expenditure. During the last fiscal year two major expenditure items falling under such system were discontinued. During this fiscal year actions are being taken to discontinue the remaining minor items of multiple agency expenditure also.

**Audit Conclusion:** The issue will be reviewed at the next audit.



## 9.2 Carried forward liabilities due to delays in project execution

**Issue:** Carried forward liabilities due to delays in the point of commitment and actual execution.

**Observation / Effect:** It was noted that \$4,233,605 of carried forward liabilities refers to commitments incurred in previous financial years. After discussions with Procurement, this is due to:

- Inadequate documentation for processing tendering such as feasibility study reports, design and specifications and estimations on the basis of the commitment of funds.
- Project implementation and contractors not being monitored adequately.

Delays in implementation of projects increase the likelihood that funds are not used for the purpose that they were committed. Lack of control and monitoring of projects and contractors may lead to cost escalation.

**Recommendation:** Project implementation should not be delayed due to inadequate documentation. At the time of committing the funds, agencies should have all documents. Projects and contractors should be monitored more carefully to avoid time escalation that could lead to costs escalation.

**Management Response:** The issue and recommendation of the Audit have been noted. Although such lack of documentation or delays are not observed in every project, but in the case of some projects the observations made by the Audit are found to be correct. This will be taken up with all the Agencies so that they take necessary actions towards required documentations and appropriate supervision/monitoring during inception and implementation of each project.

**Audit Conclusion:** The issue will be reviewed at the next audit.



## 10 Investment of Funds

### 10.1 Investment of funds held by the Banking and Payment Authority

**Issue:** The Government funds held in the Banking and Payment Authority ("BPA") accounts constituting 95% of the total assets of the Government of Timor-Leste are all held in US currency.

**Observation / Effect:** Of the total assets of the Government of Timor-Leste of \$358,146 million, the amount of \$340,681million (95%) represents cash or investments held in BPA. It appears that all of the funds are held in US currency.

Although it would appear that it is the responsibility of the BPA to determine how and where funds are to be held and invested, it could be considered an exposure risk to currency exchange fluctuations if all the funds are held in one currency. Also given the relative value of the funds held by the BPA it could be expected that they would have in place a currency exchange risk management policy. We understand that to some extent this will be addressed with the commencement of the Petroleum Fund.

**Recommendation:** It is recommended that the Treasury should raise the issue with BPA and obtain confirmation that they have in place an adequate currency exchange risk management policy.

**Management Response:** The Consolidated Fund account held at the Banking and Payment Authority (BPA) is denominated in United States Dollars, the official currency of Timor-Leste. As such the balance in the account is not exposed to exchange fluctuations of other currencies.

The Banking and Payment Authority (BPA) has a currency exchange risk management policy in place, whereby the BPA's assets and liabilities are all denominated in United States Dollars, aside from some balances held at correspondent banks for payment settlement purposes.

To the extent that the Banking and Payment Authority (BPA) may change its reserve management policy to include investments in currencies other than the United States Dollars, gains and losses resulting from such activities would be solely for the account of the BPA unless the transactions were undertaken on behalf of a customer. Accordingly, it is observed that the balance in the Consolidated Fund account is not exposed to currency risks of the nature mentioned in this issue.

The creation of the Petroleum Fund would not result in changes in these principles.

**Audit Conclusion** We are satisfied Treasury is aware of the issues.