SAINT HELENA AUDIT SERVICE
External Auditors

MANAGEMENT LETTER

FINANCIAL STATEMENTS 2012-13

To the Legislative Council of St Helena Government

29/10/2015

CONTENTS

INTRODUCTION

As the external auditor for Saint Helena Government, I am required by the Public Finance Ordinance to report to Legislative Council (LegCo) my findings from the audit of the financial statements of Saint Helena Government.

The purpose of this report is to summarise for LegCo the key issues arising from my audit of the Financial Statements for the year ended 31 March 2013 and report any material weaknesses in the accounting and internal controls that have come to my attention during the audit.

A draft of this letter was reported to the Financial Secretary and Executive Council for review prior to submission of the final report to the LegCo.

AUDIT OBJECTIVES

The main objective of the audit is to form an opinion as to whether the Financial Statements of Saint Helena Government present fairly the financial position of Government at 31 March 2013 and of its financial performance for the year, and confirm that the Financial Statements are prepared in accordance with the Public Finance Ordinance.

As part of my audit I carry out the following work:

- Examine, on a test basis, evidence relevant to the amounts and disclosures in the Financial Statements.
- Assess any significant estimates and judgements made by Saint Helena Government in the preparation of the Financial Statements.
- Assess whether the accounting policies are appropriate to Saint Helena Government's circumstances, consistently applied and adequately disclosed.
- Evaluate the overall adequacy of the presentation of information in the Financial Statements to ensure compliance with International Public Sector Accounting Standards (IPSAS).
- Report to you my opinion that
    - the accounts present fairly the financial position of the Government, as at the end of the financial year then ended; and
    - in all material respects the expenditure and income have been applied to the purposes intended and conform to the authorities which govern them; and
    - the accounts and financial statements have been prepared in accordance with all relevant laws and policies.
- Report to you such other information as I consider necessary or appropriate to assist you in your consideration of the Government's accounts for that financial year.
- Submit for your consideration an annual management letter on the audit.

My audit methodology for the collection of audit evidence is based on the Audit Manual of the St Helena Audit Service, which has been developed to reflect current international auditing standards. The methodology adopts a risk-based approach in accordance with International Standards on Auditing (UK & Ireland).

Although I am required under International Standards on Auditing to consider fraud when carrying out the audit, the purpose of my audit is not the detection of fraud. Responsibility for the prevention and detection of fraud rests with the Government who should not rely on the external audit function to discharge these responsibilities.

AUDITOR INDEPENDENCE

The audit engagement team has complied with relevant ethical requirements regarding independence. The following circumstances may present a perceived threat to the independence of the Saint Helena Audit Service:

- The audit of Saint Helena Government accounts for more than 50% of the annual fee income for the Saint Helena Audit Service.
- I am appointed by HM the Governor, with the approval of the Secretary of State, and my staff are appointed on the same terms and conditions of service as other public servants of Saint Helena Government.
- The budget for the Saint Helena Audit Service was approved as part of the Saint Helena Government's budget setting process for 2012/13. From 2013/14 the Audit Service has gained further autonomy by operating as a Special Fund, with budget approved by the Public Accounts Committee independently of the Executive.

The threats to independence in respect of the financial statements audit are reduced to an acceptable level through the protections enshrined in the Saint Helena Constitution, in which the Chief Auditor and staff of the Saint Helena Audit Service are not be subject to the direction or control of the Governor, the Executive Council or any other person or authority.

All my staff have completed declarations of interest, and where there is an identified conflict, appropriate safeguards are applied. Through these ethical policies and specific threat mitigation measures I am satisfied as to the independence and objectivity with which the audit is conducted.

CHANGES TO ACCOUNTS AND SIGNIFICANT MATTERS

FINANCIAL REPORTING FRAMEWORK

The financial statements for the year 2012/13 are the second year of reporting on an accruals basis using International Public Sector Accounting Standards (IPSAS). Consistent with the first time reporting in 2011/12 the preparation of financial statements for the second year has again proved to be technically challenging and resource intensive leading to a significant delay in statutory reporting. The matters reported in this management letter relate to the draft 2012/13 financial statements submitted for audit in March 2015.

The accounting policies set out in Note 1 explain that the financial statements are prepared in accordance with IPSAS with the exception of IPSAS 6 Consolidated and Separate Financial Statements. SHG has used certain transitional provisions available for periods subsequent to first-time reporting under IPSAS but there is no exemption in respect of IPSAS 6. Accordingly and consistent with the prior-year the audit report is qualified in respect of consolidated financial reporting.

CHANGES IN ACCOUNTING POLICY

Some changes in accounting policy have been applied in 2012/13 to provide improved compliance with IPSAS. These include the recognition under IPSAS 23 of income from non-exchange transactions in respect of the DfID funding of the St Helena Airport. These progressive changes are encouraged to move towards improved financial reporting and full IPSAS compliance.

The Bulk Fuel Installation (BFI) has no separate legal identity and accordingly remains an activity of Government. The BFI is now recognised as such in the 2012/13 financial statements of SHG.

These changes in accounting policy and correction of material errors which impact previous periods are applied in accordance with IPSAS 3 requiring the restatement of prior year comparatives on a consistent basis as explained in Note 2 to the financial statements.

OTHER LEGACY ISSUES

On 1 April 2011 Saint Helena Government changed its payments of benefits to a statutory basis for the first time with the introduction of Income Related Benefit (IRB) and Basic Island Pension (BIP) under the Social Security Ordinance 2010. Until the eligibility of all persons in receipt of IRB and BIP is verified there will remain a qualification over the benefits paid consistent with that raised in the 2011/12.

The financial statements for 2011/12 were further qualified because the financial statements recorded the cash payments made to pensioners of the unfunded defined benefit pension scheme rather than the current service cost. An actuarial report was obtained and adjustments made to achieve compliance with IPSAS 25 Employee Benefits and remove this qualification for 2012/13.

AUDIT OPINION

I base my opinion on the detailed audit work that we carried out in accordance with International Standards on Auditing. In my opinion, because of the significance of the matters described in the basis for qualified opinion paragraphs below, the financial statements do not present fairly the financial position of the Saint Helena Government as at 31 March 2013 and of its financial performance and cash flows for the year then ended in accordance with International Public Sector Accounting Standards.

The form of my proposed Independent Auditors Report is included in Appendix A.

ADVERSE OPINION RELATING TO NON CONSOLIDATION OF SUBSIDIARY BODIES

I have issued an adverse opinion on the financial statements because the Saint Helena Government has control, from an accounting perspective, either by direct shareholding (subsidies) or through appointment of board membership of several bodies. These bodies include the Bank of St Helena, Solomon & Company (St Helena) PLC, the St Helena Currency Fund, Enterprise St Helena, the St Helena Fisheries Corporation, the St Helena

National Trust, the St Helena News Media Service and St Helena Line Ltd. The accounts of these bodies have not been consolidated with those of the Saint Helena Government, as required by IPSAS 6, *Consolidated and Separate Financial Statements*.

I cannot accurately quantify the effects of these omissions on the Accounts (due to not having the necessary information to calculate the adjustments that would arise from aligning accounting policies, as required to provide a consolidated view). The expected impact is an understatement of net assets (approximately £12.4m) and financial performance (recalculated to exclude transactions internal to the group).

The Saint Helena Government has acknowledged in the accounting policies Note 1(a) that non-consolidation is not in compliance with IPSAS 6. Nonetheless this reserved statement of compliance does not meet the requirement of the standard.

QUALIFIED OPINION RELATING TO ELIGIBILITY OF SOCIAL BENEFIT PAYMENTS

I have qualified my opinion on the financial statements because the Saint Helena Government is responsible for the payment of Social Benefits, primarily through Income Related Benefit and Basic Island Pension. Payments of these two benefits in the year to 31 March 2013 were £1.839 million (£1.666m to 31 March 2012). I was unable to obtain sufficient appropriate audit evidence about the accuracy and eligibility of such payments because the Health and Social Welfare Directorate does not request or hold evidence of eligibility.

I was therefore unable to determine whether any adjustments to these amounts were necessary. My opinion is qualified in respect of this limitation of scope.

QUALIFIED OPINION RELATING TO INVENTORY HOLDINGS

I have qualified my opinion in respect to inventory holdings detailed in Note 11 with a carrying amount of £2.068m at 31 March 2013 (£1.954m at 31 March 2012).

The reported inventory excluded allocated stores with an estimated value of £1.127m at 31 March 2013 which had been held by the Infrastructure and Utilities Division and charged to expenditure on acquisition. IPSAS 12 requires that inventory is recognized as an asset and expensed when the stores are utilized and related revenue is realized. Accordingly reported net assets are understated to the extent of this allocated inventory.

The audit evidence available to me was limited because I did not observe the counting of the physical stock as at 31 March 2013. Owing to the nature of the Governments records, and inadequate stock taking arrangements, I was unable to obtain sufficient appropriate audit evidence regarding the stock quantities by using other audit procedures.

I was therefore unable to determine whether any adjustments to the reported amounts were necessary. My opinion is qualified in respect of these material uncertainties.

QUALIFIED OPINION DUE TO NON-CONFORMANCE WITH STATUTORY AUTHORITY

The Bulk Fuel Installation is an activity of Government undertaken without statutory cover through an Ordinance or Special Fund. Accordingly these transactions and balances are deemed to form part of the Consolidated Fund but expenditures and revenues in relation to the BFI are without estimate provision or legal authority under an appropriation ordinance.

My regularity opinion on whether expenditure and income have been applied to the purposes intended and conform to the statutory authorities which govern them is therefore qualified.

My regularity opinion is further qualified as the BFI reserve balance amounting to £3.796m at 31 March 2013 (£3.817m as restated 31 March 2012) is reported within Special Funds in the Statement of Financial Position and Note 21 rather than within Consolidated Fund.

EMPHASIS OF MATTER PARAGRAPH

I have included an emphasis of matter paragraph drawing attention to Note 25 which details the divestment of utility services to a controlled company Connect St Helena with effect from 1 April 2013. The transfer of these assets, revenues and expenditures represents a discontinued operation from the perspective of the separate financial statements of the Government of St Helena.

UNCORRECTED MISSTATEMENTS

In the course of our audit, I identified a number of misstatements. I requested the Financial Secretary to correct these misstatements and they were actioned where it was readily possible. In recognition of your governance responsibilities I have scheduled those material misstatements which have now been corrected in Appendix B.

The opinion and qualifications above highlight remaining areas of error or uncertainty which, in my opinion, would result in further material adjustments once further work quantified the full extent of the misstatements. They remain uncorrected. Their effects on the financial statements are described above and are detailed in Appendix C.

I have formally requested that all material misstatements are corrected.

SIGNIFICANT ISSUES ARISING FROM THE AUDIT

ACCOUNTING POLICIES, ACCOUNTING ESTIMATES AND FINANCIAL STATEMENT DISCLOSURES

The accounting policies disclosed are in accordance with IPSAS except for those recognized areas of non-compliance in terms of IPSAS 6 as described above. After making required adjustments the policies, practices and disclosures are compliant with IPSAS taking account of transitional provisions and are appropriate to the Saint Helena Government.

The inclusion of specific disclosures required by IPSAS 18 *Segmental Reporting,* IPSAS 20 *Related Party Disclosures* and IPSAS 24 *Presentation of Budget Information* was discussed with management. The required additional statements and note disclosures are now included in the financial statements.

The Financial Secretary has included a foreword to the financial statements. This responds positively to an audit recommendation made in the Management Letter for 2011/12. There is scope to develop the foreword in future periods by reference to the IPSAS Recommended Practice Guide 2 *Financial Statement Discussion and Analysis.* The foreword should complement the information in the financial statements and include:

- an overview of the operations and the environment in which it operates
- an analysis of the financial statements including significant changes and trends in financial position, financial performance and cash flows
- a description of the principal financial risks and uncertainties an explanation of their change in year and future mitigation strategies

SIGNIFICANT DIFFICULTIES ENCOUNTERED DURING THE AUDIT

Draft accounts for 2012/13 were first prepared on 13 January 2014 but by mutual agreement between Acting Chief Auditor and Financial Secretary the audit was suspended in May 2014 and the accounts returned.

Corporate Finance reworked the accounts to address the issues raised and presented a new edition of the financial statements and supporting schedules on 3 March 2015. These revised statements included comprehensive revisions and replaced in entirety the previous draft financial statements issued in January 2014 – all previous audit issues raised were set aside and the audit restarted with a clean sheet.

The 2012/13 financial statements are therefore being reported almost two-years behind the normal public reporting cycle. The late preparation of the accounts reflects the continued technical challenges encountered in preparing full IPSAS accruals accounts alongside the operational demands upon the professional accounting capacity within Corporate Finance.

The timely production and audit of public accounts is essential for good financial governance and public accountability. St Helena Government is in receipt of significant grant-in-aid and the audited accounts therefore serve to provide assurance to DFID and other international donors. The relevance of the public accounts to external stakeholders and parliamentary scrutiny processes are enhanced when public reporting occurs on a timely basis.

A collaborative programme in underway between Corporate Finance and the St Helena Audit Service to clear the backlog in the statutory reporting of the Financial Statements of Government in St Helena. This programme is designed to address the backlog such that the 2015/16 accounts will follow the expected reporting cycle of preparation and audit reporting within nine-months of financial year end.

SIGNIFICANT MATTERS ARISING FROM THE AUDIT THAT WERE DISCUSSED, OR SUBJECT TO CORRESPONDENCE WITH MANAGEMENT

Each of the issues leading to a modification of the opinion was discussed with management together with a range of other significant matters. These matters are summarized in the following sections.

NON CONSOLIDATION OF SUBSIDIARY BODIES

The lack of consolidated financial statements and when they might be prepared was discussed. Compliance with IPSAS 6, *Consolidated and Separate Financial Statements* presents a significant difficulty to SHG as it does to any other public sector bodies facing the same technical issue of consolidating the results of commercial activities with its own when those reporting components use different financial reporting frameworks.

Notwithstanding these technical challenges there are no transitional provisions applicable to IPSAS 6 and accordingly the qualification will remain a feature of the auditor’s report until the accounts of Government can be presented on a consolidated basis.

The subsidiary bodies which are regarded as controlled entities of SHG are detailed in Note 24 to the Financial Statements. Even where full consolidation is not achieved under IPSAS 6 the separate financial statements of Government should nonetheless account for the value of the investment held in the subsidiary bodies using the direct equity method.

ELIGIBILITY OF SOCIAL BENEFIT PAYMENTS

The current Social Security Ordinance is inadequate for continuing eligibility, case review and audit purposes. The Ordinance states an adjudication officer may only request information from potential beneficiaries for the purpose of determining an application. This does not allow for adequate checks and evidence gathering to support pre-existing claims.

The eligibility of benefits recipients can only be confirmed by making sure that evidence is obtained/retained for any new claims and when reviewing existing cases of Income Related Benefits and Basic Island Pension. It is recognized that the audit qualification will remain until the programmed review of all current claimants has been completed.

INCOME AND ASSET RECOGNITION FROM TRANSFER FUNDING

A number of accounting issues presented in terms of the recognition of revenues associated with aid transfers from donors and the associated assets where the aid transfers are of a capital nature. These issues are summarized in the following sections.

AIRPORT INFRASTRUCTURE

Income recognition was again discussed with respect to the requirements of IPSAS 23 *Revenue from non-exchange transactions*. In the 2011/12 accounts the aid funded transfers associated with the construction of the airport were recognized in reserves rather than in the Statement of Financial Performance as required by the IPSAS 23.

The IPSAS transitional provisions allow progressive application of the standard by asset class within a period of 3-years from first-time adoption. Accordingly the accounts for 2012/13 now recognize the DFID transfer funding for the airport construction as revenue within the Statement of Financial Performance with the associated asset under construction in the Statement of Financial Position. This progress is welcomed in terms of moving towards full adoption of IPSAS 23.

The basis of measurement of the value of the infrastructure asset was discussed with management. The value of milestone payments made under contract is used to recognize the transfer funding from DFID in the Statement of Financial Performance. This measure was initially used as a basis for estimating the work in progress value of the airport asset.

However, the contract provides for milestone payments to be made before the substantial completion of work on a particular area. Accordingly this measurement basis will significantly over-state the value of the completed work during contract delivery.

IPSAS 17 *Property Plant and Equipment* requires the infrastructure asset to be recognized at fair-value in the Statement of Financial Performance and Note 13. A technical assessment of earned-value has been applied to measure fair value for recognition of the airport asset rather than payments made under contract and a material adjustment made. The difference between these two measurement bases represents a contract pre-payment as disclosed in Note 12. These measurements will converge as the construction phase-1 nears completion and the value of the pre-payment will reduce.

> ***Recommendation 1*** *Measurements of earned value should be prepared for subsequent accounting dates to facilitate the appropriate recognition of transferred assets at fair value in accordance with IPSAS 17.*

OTHER DEVELOPMENT AID

Aside from the airport infrastructure SHG receives development aid from a range of donors for a variety of purposes. These aid funds are often covered through a bilateral agreement with the donor in the form of a Memorandum of Understanding (MOU). The MOU places restrictions on St Helena earmarking the aid funds for particular purposes. These funds are often drawn in advance of their application and in other cases in arrears on a claims basis.

A particularly complex issue has arisen with the accounting for EDF monies which are received by SHG from the EU and administered on behalf of St Helena, Tristan da Cunha and Ascension Island. This has caused revenues to be recognized in the wrong accounting period and for funding not necessarily intended for St Helena.

SHG had accounted for this grant funding as revenue on an unrestricted basis in the Statement of Financial Performance without recognition of accruals. The required treatment under IPSAS 23 is to recognize the revenue only to the extent that there is no restriction or liability arising which, in most cases, means matching the revenue recognition with the associated programme expenditure. Any difference will be held as a liability to repayable to either the donor or other beneficiary.

SHG have made required adjustments to the DFID funding but have elected to take benefit of the IPSAS 23 transitional provisions in respect of EDF funding which allow a period of up to three years before a change in accounting policy is required.

Finally, whilst the DFID requires an Annual Audited Statement to be made in respect of each project requiring separate review procedures by the Chief Auditor there is no similar process currently applied to EDF funding provided by the European Commission. The statutory audit of the SHG financial statements will not in itself provide the level of assurance required by the EU as donor.

> ***Recommendation 2*** *A separate review engagement should be commissioned in respect of EDF funded infrastructure in order to give specific assurance that the grant funds have been applied for the purposes intended.*

ASSET VALUATIONS

ROAD INFRASTRUCTURE

Transitional exemptions were adopted in 2011/12 in respect of the non-recognition of certain classes of assets including land and buildings and the roads network. However these transitional provisions do not obviate the need to recognize subsequent capital expenditure within these asset classes. Corporate Finance team will need to ensure accounting policies are suitably designed and applied for the recurrent and capital aspects of road network infrastructure and that maintenance and improvement works are suitably differentiated.

RMS ST HELENA

The RMS St Helena was initially recognized at its estimated residual value plus the capital expenditure incurred since, with just that expenditure to be depreciated over its short remaining useful life. SHG has chosen to apply the IPSAS 17 transitional exception to this asset class and remove the opening carrying value of the RMS St Helena. The relevant adjustments have been made to the Financial Statements.

BULK FUEL INSTALLATION

The BFI Agency Ordinance 2003 although enacted is not used to administer the BFI. Rather the BFI is managed on behalf of SHG by Solomon & Company (St Helena) PLC under a 2006 Management Agreement. Since the BFI has no separate legal identity, the operations and financial affairs of the BFI remain an activity of SHG. Accordingly the BFI financial results are incorporated within the financial statements of SHG.

The incorporation of the results of the BFI within the financial statements is necessary but material adjustments were required to ensure BFI revenues and expenditures and associated fuel duties were properly presented. Furthermore the infrastructure assets of the BFI required adjustment to present these within the correct asset class within Note 13 Property Plant and Equipment.

Finally the BFI reserve balance and movements are reported within Special Funds albeit there is no special fund held in respect of this undertaking. The BFI should therefore form part of the Consolidated Fund. Accordingly the balance on Consolidated Fund and Special Funds and the movements in the Reserves Note 21 are misstated in respect of the BFI classification.

A qualification of the regularity opinion arises as the expenditures of the BFI were made without the authority of an Appropriation Ordinance.

> ***Recommendation 3*** *A Special Fund should be established to account for the operations of the BFI and therefore eliminate the need for statutory authorization of these transactions under an Appropriation Ordinance.*

CONSOLIDATED FUND AND RESERVES

The reserves of St Helena Government are presented in Note 21. There is statutory authority for Government to maintain only two forms of reserve funds:

- **The consolidated fund** – this is the primary government fund in which all revenues are received and all expenditures are made save for those separately provided in law
- **The special funds** – these funds are established by order and enable individual projects and trading activities to be accounted for separate to the Consolidated Fund

The reserves statement in Note 21 required material adjustment to properly present the reserves of Government. Aside from the Bulk Fuel Installation referred to above there are three other reserves in the draft presentation which were shown separately from the Consolidated Fund but in reality formed part of the Consolidated Fund. The following table shows the draft presentation of these reserves and the final presentation after required adjustments.

Draft presentation	Final presentation
Capital Reserve– this hybrid reserve represents the negative balance arising from the unfunded liability on the defined benefits pension scheme offset by the positive fund balance created upon initial recognition of capital assets within the Statement of Financial Position.	This reserve has been separated into the two components being the **Pension Reserve** and the **Capital Reserve**. The presentation has been changed to properly represent these reserves as forming part of the Consolidated Fund.
Capital Grant Reserve– this reserve represents the capital grant reserve associated primarily with the BFI grant funded assets accounted for under FRSSE.	This reserve has now been eliminated to **Consolidated Fund** upon consolidation of the BFI as required under IPSAS.

Draft presentation	Final presentation
Donated Assets Reserve– this reserve was established to represent the assets acquired principally through the DFID funded airport project.	The presentation has been changed to separate the **Airport Infrastructure Reserve** from the **Donated Asset Reserve** and properly present these as forming part of the **Consolidated Fund**.

INVENTORY

Inventory in Note 11 comprises a wide range of stocks and stores required for activities of Government and totalling some £2.068m at 31 March 2013 (£1.954m at 31 March 2012).

Excluded from this inventory was the allocated stock held by the utilities division with an estimated value of £1.127m but not recognized in the financial ledger. These stocks formed part of the assets and inventory subsequently transferred to Connect St Helena. A material misstatement remains from the non-recognition of these stocks giving rise to an audit qualification.

In the absence of independent audit scrutiny the departmental stocktaking arrangements at 31 March 2013 were not deemed sufficiently reliable to confirm existence and valuation of inventories. Accordingly there is a limitation of audit scope arising which is reflected as a qualification in the audit report.

CLASSIFICATION OF INVESTMENTS

In the Statement of Financial Position certificates of deposit held with Crown Agent Investment Managers amounting to £6.400m at 31 March 2013 (£8.312m at 31 March 2012) were initially classified within cash and cash-equivalents in Note 8. These have now been disclosed in Note 9 as investments to reflect the fixed-term nature of these holdings.

CLASSIFICATION OF EXPENDITURE

In the Statement of Financial Performance the expenditures of Government are shown according to a functional analysis as required by IPSAS. Included within the General Public Service line was the expenditure on Technical Cooperation amounting to £4.090m and depreciation of £2.237m. These amounts have now been reclassified by function.

Note 4 provides an analysis of expenditure by nature of the expense. Material adjustments have been made to ensure this Note presents fairly in accordance with IPSAS requirements.

LOSSES AND WRITE OFFS

Losses and write-offs were discussed with management. An advance payment of £55,495 had been made in a prior year in respect of an order for an ambulance but the supplier subsequently defaulted and accordingly the pre-payment previously held as an asset was written-off in year.

The Financial Regulations state that the Governor may, subject to obtaining prior approval from the Secretary of State for amounts exceeding £50,000, authorise the Financial Secretary to write-off a loss of assets. ExCo and DfID were clearly informed but the required authorization from the Secretary of State was not available to support the write-off.

INTERNAL RECHARGES

The accounting for internal recharges was discussed. Management had eliminated these internal recharges but we required additional information to validate these journal entries amounting to £986,000and further adjustments were then effected. Adjustments were also required to also eliminate the internally generated trading surplus of £342,000 associated with these recharges.

OTHER MATTERSARISING FROM THE AUDIT THATARE SIGNIFICANT TO THE OVERSIGHT OF THE FINANCIAL REPORTING PROCESS

DISCONTINUED OPERATIONS

Events after the reporting date in Note 25 details the divestment of utility services to a controlled company Connect St Helena with effect from 1 April 2013. The transfer of these assets, revenues and expenditures represents a discontinued operation from the perspective of the separate financial statements of the Government of St Helena and requires disclosure under IPSAS 1.106. An emphasis of matter has been included in the auditor’s report to underline the significance of this transfer to the reader of the financial statements.

EXPENDITURE WITHOUT AUTHORITY

The Statement of Budgetary Performance and related Note 5 reports departmental expenditure and revenue at output level compared with the budget estimate. Expenditure exceeding the limit of the approved estimate requires authority of a supplementary appropriation. These excess votes have previously been authorized by supplementary appropriation with the exception of two items:

- **Bulk Fuel Installation**– the transactions of the BFI form part of the Consolidated Fund but were not included within the budget estimates and are therefore without the authority of an Appropriation Ordinance.
- **Pensions and Gratuities** – the Pensions Ordinance permits the payment of pensions from the Consolidated Fund which provides the necessary lawful authority notwithstanding any appropriation Ordinance.

PENSION DEFICIT

The Government has a defined benefits pension scheme (DBPS) which is explained in accounting policies Note 1(i). The DBPS was closed to new members on 31 March 2010 with eligible employees joining after 1 April 2010 being enrolled into the new defined contribution pension scheme (DCPS).

The DBPS is unfunded and Note 18 to the accounts reports the pension liability amounting to £38.279m at 31 March 2013 (£35.200m at 31 March 2012) with no corresponding assets. Accordingly pensions in payment under the DBPS will continue to fall upon the Consolidated Fund on a pay-as-you-go basis.

WRITTEN REPRESENTATIONS

Written representations were requested and received from the Financial Secretary in line with those required by Auditing Standards.

GOING CONCERN

The annual recurrent spend by St Helena Government is 57% (£20.534m of £36.011m) funded from direct grant from the Department for International Development (DfID). These figures exclude internally generated income, which was included in the workings that set future targets for DfID income dependency reducing to 50% by 2014/15.

I have considered Saint Helena Government's assessment that the organisation is a going concern. I am satisfied that this assessment is appropriate based on discussions with the Financial Secretary, a review of budgets, the Development Assistance Planning Mission Aide Memoir of 22 February 2012 and the assumption that that Department for International Development will continue to provide grant-in-aid necessary to meet the reasonable needs of the Island.

ANNUAL GOVERNANCE STATEMENT

Consistent with best public sector practice SHG has prepared an Annual Governance Statement (AGS) for 2012/13 for publication with the Financial Statements. As Chief Auditor I am obliged to review the AGS to and consider whether it conforms to proper practice and the reported content is not inconsistent with my knowledge of the entity.

The publication of an AGS represents a voluntary disclosure and accordingly there is currently no regulatory basis requiring publication with the accounts of Saint Helena Government or prescribing its form. In the absence of specific regulation the form has been reviewed in comparison with the model framework published by CIPFA.

The following issues were identified and discussed with management:

- There was no Code of Governance published by SHG and accordingly there is no express statement of compliance in the AGS as envisaged by the model statement.
- There was no explicit statement which says that the governance framework has been in place for the year and up to the date of approval of the statement of accounts.

Modifications were made by management such that the AGS conforms to proper practice and the reported content is consistent with the financial statements and my audit understanding of SHG in the period under report.

> ***Recommendation 4*** *A Code of Governance should be developed with reference to the CIPFA/IFAC International Framework on Good Governance in the Public Sector and adopted as a standard against which compliance may then be measured in the AGS.*

INTERNAL CONTROLS

In accordance with International Standards on Auditing (UK & Ireland) I have included a summary of matters which arose during the course of my audit and which I consider should be brought to the attention of Council.

The matters described in this section came to my attention during the normal course of my audit, the purpose of which was to express an opinion on the financial statements. The audit included consideration of internal control relevant to the preparation 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 internal control.

Overall responsibility for maintaining adequate financial reporting systems and systems of internal control, as well as for the prevention and detection of fraud, irregularities, and other errors, rests with the Accounting Officers.

FOLLOW-UP OF PREVIOUS ISSUES

Five audit recommendations were made in the Management Letter for 2011/12. The current status of these items is summarized in the table of below.

Recommendation	Follow-up status
1. Identification of an appropriate body for external auditor reporting to those charged with governance under ISA 260	**Closed** – Executive Council provides a suitable forum for the auditors reporting to those charged with governance
2. Introduction of accruals budgeting	**Pending** – Financial Secretary has given a commitment to PAC that accruals based budgeting will be introduced with effect from financial year 2017/18
3. Foreword to be included with the published financial statements	**Actioned** – Foreword by Financial Secretary now included within the published financial statements for 2012/13
4. Advance funding of the airport contract	**Superseded** – the airport contract has been reviewed and is the subject of a separate audit report with recommendations
5. An audit is required of the Defined Contribution Pension Scheme	**Actioned** – a financial statement has been prepared for the DCPS pension scheme and submitted for audit

Overall am satisfied that appropriate progress has been made in respect of these previous audit recommendations.

NEW ISSUES RAISED THIS YEAR

The new matters now reported in Appendix D are limited to those deficiencies that I consider to be of sufficient importance to merit being reported to Council. Less significant matters will be reported to the Financial Secretary in a separate Final Accounts Memorandum.

I have noted in the Appendix the actions proposed by management in regard to the recommendations made in this letter.

CONCLUDING REMARKS

I acknowledge and thank the Saint Helena Government, and in particular the Corporate Finance team, for their assistance and co-operation given to the Audit Service during the course of the statutory audit.

Phil Sharman
Chief Auditor
St Helena Audit Service

29 October 2015

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SAINT HELENA GOVERNMENT

I have audited the financial statements of the Saint Helena Government for the year ended 31 March 2013 under the Public Finance Ordinance 2010. The Saint Helena Government financial statements comprise the Statement of Financial Performance, the Statement of Financial Position, the Statement of Changes in Net Assets, the Statement of Cash Flows, the Statement of Comparison of Budget and Actual Amounts, and the related notes.

Respective responsibilities of the Financial Secretary and the Chief Auditor

The Financial Secretary is responsible for preparing the financial statements in accordance with International Public Sector Accounting Standards and being satisfied that they present fairly the financial position, financial performance, and cash flows of the Saint Helena Government. My responsibility is to audit and express an opinion on the financial statements in accordance with applicable legal and regulatory requirements and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Auditing Practices Board (APB) Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the government's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Financial Secretary; and the overall presentation of the financial statements.

I also assess whether the accounts and financial statements have been prepared in accordance with all relevant laws and policies; and whether in material respects the expenditure and income have been applied to the purposes intended and conform to the authorities which govern them.

I read all the financial and non-financial information published with the financial statements to identify material inconsistencies with the audited financial statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my adverse audit opinion.

Basis for adverse opinion

Non-consolidation of subsidiary bodies

The Saint Helena Government has control, from an accounting perspective, either by direct shareholding (subsidiaries) or through appointment of board membership of several bodies. These bodies include the Bank of St Helena, Solomon & Company (St Helena) PLC, Enterprise St Helena, the St Helena Fisheries Corporation, the St Helena National Trust, the St Helena News Media Service and the St Helena Line Ltd. The accounts of these bodies have not been consolidated with those of the Saint Helena Government as required by IPSAS 6, *Consolidated and Separate Financial Statements*.

I cannot accurately quantify the effects of these omissions on the Accounts (due to not having the necessary information to calculate the adjustments that would arise from aligning accounting policies, as required to provide a consolidated view). The expected impact is an understatement of net assets (approximately £12.4m) and financial performance (recalculated to exclude transactions internal to the group).

The Saint Helena Government has acknowledged in the accounting policies Note 1(a) that non consolidation is not in compliance with IPSAS 6.

Eligibility of social benefit payments

Saint Helena Government is responsible for the payment of Social Benefits, primarily through Income Related Benefit and Basic Island Pension. Payments of these two benefits in the year to 31 March 2013 were £1.839 million (£1.666m to 31 March 2012). I was unable to obtain sufficient appropriate audit evidence about the accuracy and eligibility of such payments because the Health and Social Welfare Directorate does not request or hold evidence of eligibility. I was therefore unable to determine whether any adjustments to these amounts were necessary.

Inventory holdings

The reported inventory in Note 11 amounting to £2.068m at 31 March 2013 (£1.954m as restated 31 March 2012) excluded allocated stores with an estimated value of £1.127m at 31 March 2013 which had been held by the Infrastructure and Utilities Division and charged to expenditure on acquisition. IPSAS 12 requires that inventory is recognized as an asset and expensed when the stores are utilized and related revenue is realized. Accordingly reported net assets are understated to the extent of this allocated inventory.

The audit evidence available to me was limited because I did not observe the counting of the physical stock as at 31 March 2013. Owing to the nature of the Governments records, and inadequate stock taking arrangements, I was unable to obtain sufficient appropriate audit evidence regarding the stock quantities by using other audit procedures.

Basis for qualified regularity opinion

The Bulk Fuel Installation (BFI) is an activity of Government undertaken without statutory cover through an Ordinance or Special Fund. Accordingly these transactions and balances are deemed to form part of the Consolidated Fund but expenditures and revenues in relation to the BFI are without estimate provision or legal authority under an Appropriation Ordinance.

My regularity opinion is further qualified as the BFI reserve balance amounting to £3.796m at 31 March 2013 (£3.817m as restated 31 March 2012) is unlawfully reported within Special Funds in the Statement of Financial Position and Note 21 rather than within Consolidated Fund.

Adverse opinion on the financial statements

In my opinion, because of the significance of the matters described in the basis of adverse opinion paragraphs, the financial statements do not present fairly the financial position of Saint Helena Government and its subsidiaries as at 31 March 2013, and their financial performance and cash flows for the year then ended in accordance with International Public Sector Accounting Standards.

Qualified opinion on regularity

Except for the incurrence of expenditure without authority in respect of the Bulk Fuel Installation and the unlawful classification of its reserve, as described in the basis for qualified regularity opinion paragraphs, in my opinion:

- in all material respects the expenditure and income have been applied to the purposes intended and conform to the authorities which govern them; and
- the accounts and financial statements have been prepared in accordance with all relevant laws and policies.

Emphasis of matter – divestment of utility services

In forming my opinion on the financial statements, which is modified, I have considered the adequacy of the disclosures made in Note 25 to the financial statements concerning the divestment of utility services to a controlled company Connect St Helena with effect from 1 April 2013. The transfer of these assets, revenues and expenditures represents a discontinued operation from the perspective of the separate financial statements of the Government of St Helena.

Phil Sharman CPFA CA
Chief Auditor for St Helena

29 October 2015

St Helena Audit Service, Jamestown, St Helena

SCHEDULE OF MATERIAL ADJUSTMENTS APPENDIX B

I identified the following misstatements during my audit and management have adjusted the financial statements to correct these errors. The table does not repeat the restatements of prior year figures already presented in Note 2 to the financial statements.

Table 1: **Material adjustments to the primary financial statements**

Adjusted misstatement	**Statement of Financial Performance**		**Statement of Financial Position**	
	Dr £000	**Cr £000**	**Dr £000**	**Cr £000**
Description	***Value***		***Value***	
Recognition of DFID development aid in line with IPSAS 23 requirements				
Income in Advance			205	
Revenue: DFID Development Aid	427			
Accrued Income: Other				632
Recognition of DFID airport asset on earned value basis				
Revenue: DFID Airport Funding	5,388			
Prepayments			17,452	
Assets Under Construction				22,840
Reallocation of customs duty on external fuel sales				
Revenue: Income Received	508			
Revenue: Taxation		508		
Reversal of expenditure debited directly to reserves				
Consolidated Fund			800	
Expenditure: General Public Service		800		
Recognition of actuarial cost the defined benefit pension scheme				
Expenditure: Public Sector Pensions	791			
Consolidated Fund				791
Reallocation of depreciation charge and TC salaries to directorates				
Expenditure: Infrastructure and Utilities	2,274			
Expenditure: Various Directorates	1,355			
Expenditure: General Public Service		3,629		

Adjusted misstatement	Statement of Financial Performance		Statement of Financial Position	
	Dr £000	**Cr £000**	**Dr £000**	**Cr £000**
Description	***Value***		***Value***	
Reclassification of funds invested with Crown Agents				
Current Asset Investments			6,400	
Cash and Cash Equivalents				6,400
Transfer between reserves to reflect DFID funded fixed asset additions and completed assets under construction				
Special Funds			4,289	
Consolidated fund				4,289
Reversal of previous adjustment to eliminate expenditure from trading accounts				
Special Funds			1,204	
Consolidated Fund				1,204

Table 2: **Material adjustments to financial note disclosures**

Description of correction	Note affected	Value of the error £000
Proper presentation of prior year adjustments in respect of errors and changes in accounting policies	Note 2 Restatement of prior year figures	Various
Reclassification of expenditure by category to correctly classify LTTC employee costs	Note 4 Expenditure by category	2,193
Disclosure of changes between original budget and final budget estimates/ explanation of material variances/ and reconciliation to primary statements	Note 5 Comparison of budget and actual amounts	Various
Amendment of the segmental reporting note to show inter-segment revenue and capital expenditure	Note 6 Segmental reporting	2,299 and 59,455
Disclosure of inventories recognised as an expense in year	Note 11 Inventories	811
Disclosure of nature and extent of risks arising from financial instruments	Note 20 Financial Instruments	Narrative
Reclassification of Special Funds and reserves forming part of the Consolidated Fund	Note 21 Reserves	Various
Disclosure of movements in working capital for cash flow statement	Note 22 Movements in working capital	1,137
Improved disclosures of related party transactions	Note 23 Related party transactions	Narrative
Amendment to infrastructure assets transferred to Connect St Helena	Note 25 Events after the reporting date	3,178

I identified the following misstatements during my audit which remain unadjusted in the financial statements.

Table 3: **Uncorrected misstatements in the main financial statements**

Misstatement	**Statement of Financial Performance**		**Statement of Financial Position**	
	Dr £000	**Cr £000**	**Dr £000**	**Cr £000**
Description	***Value***		***Value***	
Non-consolidation of subsidiaries disclosed in Note 23 with pervasive effect on group financial statements	Un-quantified	Un-quantified	Un-quantified	Un-quantified
BFI reserve reported within Special Funds not Consolidated Fund Special Funds Consolidated Fund			 3,796	 3,796
Unallocated stores not recognised as inventory in Note 11 Inventory Consolidated Fund	Un-quantified	Un-quantified	 1,127	 1,127
DFID deferred grant income not recognised in year Income in Advance: Other Revenue: DFID Development Aid		 244	 244	
Aggregate soft error projections from audit testing affecting: Depreciation expense/ leave accrual/ other accruals/ pre-payments/ cash	104	 186	186	 104

RECOMMENDATIONS TO MANAGEMENT APPENDIX D

No	Observation	Recommendation	Priority	Response& timescale
1	**Transferred asset valuation** The value of milestone payments will consistently over-state the value of the completed work at any point in time. Accordingly a technical assessment has been made of earned value of the airport infrastructure at the accounting date.	Measurements of earned value should be prepared for subsequent accounting dates to facilitate the appropriate recognition of transferred assets at fair value in accordance with IPSAS 17.	H	**Corporate Finance:** Corporate Finance will discuss the matter with Halcrow and make the necessary adjustments in future statements. **By end of December 2015**
2	**EDF audit certification** The bilateral funding agreement for the EDF-10 infrastructure funding provides that the accounts of the St Helena Government are audited and this will include an audit of the Development Fund. The statutory audit of the SHG financial statements will not in itself provide the level of assurance required by the EU as donor.	A separate review engagement should be commissioned in respect of EDF funded infrastructure in order to give specific assurance that the grant funds have been applied for the purposes intended.	M	**Corporate Finance:** Corporate Finance will approach EDF and request clarity on the audit procedures to be followed and share this with SHAS. **By end of December 2015**
3	**Bulk Fuel Installation** The Bulk Fuel Installation is an activity of Government undertaken without statutory cover through an Ordinance or Special Fund. Accordingly expenditures and revenues in relation to the BFI are without budget estimate provision or legal authority under an appropriation ordinance.	A Special Fund should be established to account for the operations of the BFI and therefore eliminate the need for statutory authorization of these transactions under an Appropriation Ordinance.	H	**Corporate Finance:** Special Fund to be implemented. **By end of November 2015**

No	Observation	Recommendation	Priority	Response& timescale
4	**Code of Governance** There is no Code of Governance published by SHG and accordingly there is no express statement of compliance as envisaged by the model Annual Governance Statement.	A Code of Governance should be developed with reference to the CIPFA/IFAC International Framework on Good Governance in the Public Sector and adopted as a standard against which compliance may then be measured in the AGS.	M	**Corporate Support:** To be reviewed and implemented in time for 2016/17 reporting. **By end of March 2016**
5	**Inventory management** Year end stock observation procedures (as compiled by the SHG finance directorate) were not observed by all SHG directorates. In particular no year-end stock observation took place for inventories classified as unallocated stores, amounting to £405k, resulting in a material uncertainty over the accuracy or valuation of these stores.	Measures should be implemented to ensure that stock counts are performed on all material balances within the total inventory – where a full inventory count is not feasible (either due to resource constraints or materiality), it performs an alternate exercise to obtain assurance over year-end inventory.	M	**Corporate Finance:** Year-end stock procedures to be further reviewed and discussed with Accounting Officers to ensure full compliance at year end. **By end of February 2016.**

DEFINITION OF PRIORITIES	
HIGH	Immediate risk of error, loss of cash or other assets or significant non-compliance with relevant Ordinances or regulations. Action should be taken on these within 2 months.
MEDIUM	Issues identified which would improve the quality of financial reporting and/or internal control systems. Action should be taken on these within 6 months, or by the end of the next financial reporting period, whichever is the earliest.

RELATED PARTIES & GROUPS APPENDIX E

As explained in the paragraph on the adverse opinion relating to non-consolidating group entities, the financial statements fail to include group entities as required by IPSAS 6, *Consolidated and Separate Financial Statements*. The group entities that should have been consolidated are:

- Bank of St Helena
- Solomon & Company (St Helena) PLC
- St Helena Currency Fund
- Enterprise St Helena
- St Helena Fisheries Corporation
- St Helena National Trust
- St Helena News Media Service
- St Helena Line Ltd

The lack of consolidation means that I am unable to express an opinion on the internal control arrangements of group entities. I have not carried out such audit work on the group entities which we act for, nor communicated with other component auditors. All the group entities received unqualified audit opinions for the period ended 31 March 2013.