Madam Speaker, I rise to make a Statement on Government’s financial and performance reporting and the Adverse audit opinion received on the 2013/14 Entire Public Sector (“EPS”), Consolidated Financial Statements.

**Financial and Performance Reporting**

Madam Speaker, on 5th November 2015, the Acting Auditor General released two (2) Audit Reports, dated 25th September 2015, on the Financial and Performance Reporting of: (1) Ministries, Portfolios and Offices; and (2) of Statutory Authorities and Government Companies for the years ended 30 June 2013 and 2014. I will refer to these collectively as Public Sector Entities.

For the financial year ended 30 June 2014, the Auditor General reported that of the 42 Public Sector Entities which existed:

- 23 received unqualified or “clean” opinions; and
- 14 received qualified opinions.

Hence, of the 37 Public Sector Entities whose audits have been completed, none of those Entities received an Adverse opinion from the Auditor General.
The audits of the following five (5) Public Sector Entities are still ongoing:

- the Ministry of Education, Employment & Gender Affairs;
- the Ministry of Health, Sports, Youth and Culture;
- Cayman Islands Airports Authority;
- the Cayman Islands National Insurance Company; and
- the Tourism Attractions Board.

For the financial year ended 30th June 2015, the Acting Auditor General provided an update on the status of the 2014/15 audits and reported that as of 24 November 2015, of the 42 Public Sector Entities whose audits have been completed:

- 19 received unqualified or “clean” opinions; and
- 5 received qualified opinions.

Again, an Adverse opinion has not been issued with respect to any of the 2014/15 audits completed as at 24 November 2015.

The 2014/15 audits for 18 Public Sector Entities have not been completed as at 24 November 2015.

Madam Speaker, as you know, an unqualified or “clean” audit opinion is issued when the information contained in the financial statements of an entity can be relied upon because it represents fairly the financial position and performance of that entity.

A qualified opinion means that a portion of the financial statements cannot be relied upon, but the rest of the statements can be relied upon by the reader.

The Acting Auditor General reports that the Public Sector Entities continue to make improvement in the quality and timeliness of annual financial reporting. The financial statements of Public Sector Entities continue to show a greater degree of reliability and credibility and improvements have been made on accounting practices, supporting information and the presentation of information.

The Ministry of Finance will continue to provide guidance and support to individual Public Sector Entities to ensure further improvement of the quality of their financial statements.
Adverse Audit Opinion on the 2013/14 Entire Public Sector (EPS) Consolidated Financial Statements

Madam Speaker, the EPS consolidated financial statements are prepared by the Ministry of Finance. The consolidation exercise involves taking all of the financial statements of the Government’s 42 Public Sector Entities, consolidating the financial information and eliminating inter-agency transactions and balances.

The robustness of the consolidated financial statements for the EPS, is dependent upon the quality of information contained in the financial statements of individual Public Sector Entities.

If an individual Public Sector Entity is a significant entity within the EPS and that entity receives a Disclaimer of Opinion or an Adverse Opinion from the Auditor General, then the consolidated financial statements of the EPS will likely receive a Disclaimer of Opinion or Adverse Opinion from the Auditor General.

Madam Speaker, whilst 37 of the 42 Public Sector Entities have received Unqualified (or clean) and Qualified audit opinions on their 2013/14 financial statements, the Auditor General has issued an Adverse opinion on the 2013/14 EPS consolidated financial statements. This requires an explanation because the public will not readily understand how an Adverse opinion is issued on the EPS consolidated financial statements when 37 of the 42 Public Sector Entities have received either an Unqualified (or clean) or Qualified audit opinions.

The reasons for the Adverse opinions are not due to audit issues occurring in the underlying financial statements of Public Sector Entities. Instead, the Adverse opinion is due to the accounting treatment and decisions of “macro” issues that impact the EPS consolidated financial statements and not the underlying financial statements of individual Public Sector Entities.

The “macro” issues that have led to an Adverse opinion on the 2013/14 EPS consolidated financial statements include:

1. Material Omissions;
2. Property Plant and Equipment, Valuation and Completeness;
3. Erroneous Opening and Closing Balances;
4. Revenue and Related Receivables Completeness; and
5. Consolidation Integrity Issues.
Material Omissions

Madam Speaker, the Audit Office identified that both post-retirement benefits (health care and pension) and the accounting for the Public Service Pensions Board were not fully included in the EPS consolidated financial statements.

The post-retirement healthcare liabilities, of approximately $1.2 billion, were not included on the face of the primary statements in the 2013/14 EPS consolidated financial statements, but are referenced as disclosures in Notes to the financial statements.

It was a policy decision of the Government to disclose details of the post-retirement healthcare liabilities and expenses in the Notes of the financial statements. This approach is similar to the accounting practices in countries such as the United States of America and Canada.

Such disclosure in the Notes to the financial statements is effectively adopting a modified version of International Public Sector Accounting Standards ("IPSAS"), No. 25.

The Ministry of Finance intends to present a Bill to the Legislative Assembly in 2016, to amend the Public Management and Finance Law in order to permit the use of a modified version of IPSAS 25.

Pension obligation liabilities, on the other hand Madam Speaker, have been stated on the face of the Government’s Balance Sheet for many years and further details relating thereto are provided in the Notes to the financial statements.

Madam Speaker, the Government is also exploring options to reduce the pension and post-retirement healthcare obligations such as: increasing the retirement age of Civil Servants from 60 to 65 years; introducing health insurance premium co-pay for Civil Servants; and reducing the current CI$5.0 million “cap” on the maximum lifetime medical benefits for Civil Servants. In the private sector, for the sake of comparison, with respect to supplemental benefit plans, the maximum lifetime medical benefits “cap” averages CI$2.5 million. The latter two points of co-pay and lifetime medical benefits are significant and changes thereto will require time for education and discussion with the Civil Service and time for persons to adjust their spending patterns. Consequently, it is expected that any such changes will not occur until 2018 and not for political expediency as speculated by some media outlets. If anyone knows of an approach that is more viable, more palatable and less inflammatory or financially damaging
to middle and low income Civil Servants, I am inviting them to make it known to all of us.

Madam Speaker, appointments to the Public Service Pensions Board are determined by statute, which the Government can amend and because of this degree of influence by Government, IPSAS would dictate that the Board’s assets, liabilities, revenues and expenses be included in the EPS consolidated financial statements.

However, any assets, liabilities, revenues and expenses of the Board are comingled with those of the three Public Sector Pension Plans (the “Plans”). The assets of the three Plans are for the direct benefit of current and retired Civil and Public Servants including Members of the Legislative Assembly. The Ministry of Finance is of the opinion that the assets of the Plans should not be included in the EPS consolidated financial statements because the money in those Plans belong to Civil Servants and retirees; the Cayman Islands Government via the Public Service Pensions Board only manages these funds. The treatment and decision to exclude such matters from the EPS consolidated financial statements is a very conservative and prudent approach that has been adopted.

The Audit Office disagrees with this treatment and is of the view that the Plans’ assets, liabilities and activities ought to be combined with those of Public Sector Entities. This disagreement is one of the factors that has led to an Adverse audit opinion being issued because the value of the assets in the Plans are significant, approximately $0.5 billion. The Ministry of Finance, therefore, is of the view that its prudent approach has, ironically, contributed to an Adverse opinion by the Auditor General’s Office.

Madam Speaker, the Government intends to review the Public Sector Pensions Law with the view of segregating the assets of the Public Service Pensions Board and those of the three Plans and, mandating separate reporting for each.

Property, Plant and Equipment, Valuation and Completeness

Madam Speaker, IPSAS requires that consistent accounting policies are applied across all entities in the EPS. However, not all of Government’s assets are reported at their revalued amounts, and most Statutory Authorities and Government Companies have yet to complete a revaluation of their fixed assets. Public Sector Entities with significant fixed assets, report such assets at cost as opposed to their revalued amounts.
The Ministry of Finance will ensure that fixed asset revaluations are conducted on a 5-year cycle similar to that of Central Government in order to ensure consistency of accounting policies across the EPS.

Additionally, the Audit Office is doubtful with respect to the completeness of both the inventory and value of the road network, which is currently valued at approximately $1.1 billion.

The Ministry of Finance has already engaged the National Roads Authority to compile a complete roads inventory for valuation.

Madam Speaker, it is envisaged that the roads inventory list will be completed by early 2016.

**Erroneous Opening and Closing Balances**

Madam Speaker, currently, the audit reports of Public Sector Entities are often completed after the 31st October each year which is the statutory deadline for the submission of the EPS consolidated financial statements. The EPS consolidated financial statements therefore are unable to reflect any material audit adjustments of these entities upon first submission to the Audit Office. An element of the improvement to Public Sector financial reporting has to be the completion of audit reports for Public Sector Entities by, or before, their statutory deadline dates.

It is envisaged that the Audit Office will complete all of its audits within the legislated two-month timeframe for entity audits (i.e. by the 31st October each year), and any audit adjustments will then be reflected in the EPS consolidated financial statements.

**Revenue and Related Receivables Completeness**

Madam Speaker, the Audit Office reported that there is no system in place to ensure that the Government is collecting and reporting all revenues and related receivables.

The Ministry of Finance intends to conduct a review of Government revenue items to determine which items can be assessed for completeness. Going forward, revenue completeness should then be assessed by respective agencies at the end of each quarterly report to Cabinet.
Consolidation Integrity Issues

Madam Speaker, the Auditor General found that there was no formal reconciliation of inter-agency transactions and balances between Public Sector Entities. The Ministry of Finance currently makes judgments and elimination entries for thousands of inter-agency transactions. This approach is not robust enough to ensure that all inter-agency transactions are fully eliminated. It is agreed that Public Sector Entities should confirm and agree inter-agency transactions and balances amongst themselves. Implications of not doing so could be that receivables, payables, revenues and expenses are overstated or understated in the financial statements.

Going forward, Public Sector Entities will now be required to confirm and agree inter-agency charges. Transactions that are not substantiated will be written-off. The Audit Office will undoubtedly find that in auditing the 2014/15 financial year disagreements of inter-agency transactions are substantially reduced. This is another example of progress being made.

The Ministry of Finance will also implement the inter-agency module, known as Advanced Global Inter-company System ("AGIS"), in the Government’s financial reporting system by 30th June 2016.

The use of AGIS will reduce inter-agency transaction mismatches as these transactions will require agreement by both counterparties prior to recognition in their respective ledgers.

Madam Speaker, it is also intended that the Law will be amended further in 2016 to strengthen the powers of the Ministry of Finance in order to enforce compliance with the Law and Financial Regulations, to hold Chief Officers accountable and prescribe sanctions which are proposed with the objective of achieving an improved quality of information and timeliness of reporting, particularly as it relates to the consolidation of the EPS consolidated financial statements.

It is intended that finance functions will be centralised within the Ministry of Finance to improve compliance with the Law and consistency in the application of Generally Accepted Accounting Principles ("GAAP"). Currently, each Ministry, Portfolio and Office has its own separate Chief Financial Officer and finance function. Suffice it to say, the Audit Office has said what it thinks of the decentralised approach every time they have issued an opinion on the Government’s financial and performance reporting.
The Ministry of Finance will produce a Public Finance Manual, which is in accordance with best practices and GAAP. The Manual will be disseminated to all Public Sector Entities and will serve to improve the consistency in the application of GAAP. It is expected that the Manual will be completed 30th April 2016.

**Conclusion**

Madam Speaker, the Ministry of Finance, with the support of the Government, is taking steps to address the matters that have led to an Adverse audit opinion being issued with respect to the 2013/14 EPS consolidated financial statements.

It should be noted that the Adverse opinion on the 2013/14 EPS consolidated financial statements is the first audit opinion that has been issued on the EPS since the Law was introduced in 2004. Prior to the 2013/14 EPS consolidated financial statements, such earlier years were given a “disclaimer” of opinion by the Auditor General’s Office, which meant that it was not possible to reach an opinion on the consolidated financial statements for the years prior to 2013/14.

An Adverse opinion is not the opinion the Government desires to receive. However, the Government sees this as a significant attestation that its financial performance has improved and evidence exists to substantiate this improvement. The Government intends to use this opportunity to address the issues that caused the issuance of an Adverse opinion and, aims to achieve greater accountability and transparency.

Addressing the qualification factors will be done via further changes proposed to the Law in 2016 and, by administrative means such as the Ministry of Finance providing enhanced guidance in required areas, and restarting meetings with Chief Financial Officers on a monthly basis.

I trust that having outlined the reasons for an Adverse audit opinion being issued, it is realised that Public Sector accounting treatments in the Cayman Islands are not significantly different from those adopted in more advanced economies, such as the USA and Canada.

It is also important to note that these audit issues are policy-related factors whilst the underlying individual accounting agencies that make-up central Government, increasingly are receiving unqualified or clean audit opinions – signifying a material improvement in their financial evidence and retention of records.
Madam Speaker, the following illustrates that significant improvement has been achieved with respect to the audit opinions issued on the 2014/15 financial statements, as of 24 November 2015:

- Eight (8) Central Government Agencies received an Unqualified (or clean) audit opinion;
- Two (2) Central Government Agencies received a Qualified audit opinion; and
- The audits of six (6) Central Government Agencies were ongoing (as of 24 November 2015).

Nonetheless, the factors leading to an Adverse opinion on the 2013/14 EPS consolidated financial statements, will be addressed effectively and decisively.

Thank you, Madam Speaker.