

FINANCIAL MANAGEMENT ASSESSMENT

A. Project Description

1. Kiribati is highly exposed to the effects of sea level rise, storm surge, coastal erosion and saltwater intrusion. Between 2005 and 2015, 94% of households in Kiribati report having been impacted by environmental hazards. In this same period, 81% report having been impacted by rising sea levels.¹ Saltwater intrusion impacted just under half of all households. All of the other hazards (storm surges, floods, cyclones, and droughts) were reported more frequently in the outer islands.

2. In the outer islands, seaports (or shipping points) are in the form of narrow channels cut through the reef-flat, with docks in some islands. Navigational aids established to notify domestic vessels of hazards are mostly inaccurate, missing or damaged, and there are no suitable nautical charts covering any of the outer islands to permit safe navigation at the standard required by modern shipping. Domestic vessels travel to outer islands using local knowledge and unorthodox methods that are neither possible nor permitted by international shipping regulations.

3. The project will (i) conduct hydrographical surveys and maritime charting for four outer islands; (ii) provide aids to navigation, boat ramps, construction of modest sheds and jetties; (iii) rehabilitation of causeways; and (iv) institutional strengthening and capacity building support.

B. Financial Management System at the Ministry of Infrastructure and Sustainable Energy (MISE)

4. MISE is the implementing agency for the land transport infrastructure development and responsible for maintenance and coastal protection. The agency has not developed a masterplan for the sector it is responsible for and, as such, has no investment plans.

- (i) **Staffing.** MISE's accounting/finance unit does not have adequate staff numbers with the right training and qualifications. A senior accountant heads the unit which is composed of 6 accounting officers, 1 revenue collector, 1 payroll assistant, 1 maintenance fund assistant, 1 payables assistant, and 1 individual payments assistant. Only the senior accountant has some formal training. The others have no formal financial training.
- (ii) **Accounting software.** Microsoft Access is being used by the Accounting Unit to keep track of its transactions. It is not an accounting software and is not capable of generating financial reports. Report on financial transactions are sent to the Ministry of Finance and Economic Development (MFED) which uses Attachè, an accounting software which is used to consolidate the submissions.
- (iii) **Budget.** Annually, the Accounting Unit consolidates budget requests from all divisions within the Ministry based on key parameters prescribed by MFED; budget submissions are submitted and reviewed in MFED and is deliberated at the government committee level. Upon approval, warrants are issued to the

¹ R. Oakes et. al. 2016. *Kiribati: Climate change and migration - Relationships between household vulnerability, human mobility and climate change*. Report No. 20. Bonn: United Nations University Institute for Environment and Human Security (UNU-EHS).

https://collections.unu.edu/eserv/UNU:5903/Online_No_20_Kiribati_Report_161207.pdf

- ministries. MISE manages its utilization of the budget allocated to it. All revenues it generates are turned over to the MFED and is not utilized by MISE.
- (iv) **Reconciliation.** The Accounting Unit prepares monthly reconciliation of transactions utilizing the budget against the balances provided by MFED. It is necessary to ensure that figures are reconciled to have assurance that enough budget balance is available for budgeted and remaining expenditures. The reconciliation report and a financial report is submitted on a monthly basis to the Secretary.
 - (v) **Asset management.** MISE's accounting unit maintains an asset register of its office equipment, vehicles and machineries used to carry out its work; they do not depreciate assets and MISE's repairs and maintenance budget are not sufficient for regular maintenance of its assets. The budget is being used only for key repairs and when the asset breaks down.
 - (vi) **Records management.** MISE's records keeping and filing practices is not in good shape. Documents often gets lost that creates difficulties for external audit. It also means that funds are unaccounted for and there are possibilities of misuse.
 - (vii) **Revenues.** Their policy on rendering services for other government offices does not allow for appropriate remuneration, although MISE has established rates for private clients using their services; the revenues that are generated by the Ministry are turned over to the Treasury (under the MFED).
 - (viii) **Audits.** The Kiribati National Audit Office (KNAO) conducts the whole-of-government audit once a year and findings are discussed with the auditees. There is no internal audit unit within MISE. A person from the MFED occasionally visits and conducts random checks mainly of revenue items but in its current review structure does not comprise an audit of internal control processes.
 - (ix) **Conclusion.** MISE's financial management system is very weak on staffing, budgeting, asset management, records management, internal control, and audit. The financial management (FM) risk in MISE is assessed as "high".

C. Financial Management System at the Ministry for Communications, Transport and Tourism Development (MICTTD)

5. MICTTD's Marine Division is responsible for the regulation of domestic and international shipping, provision of aids to navigation, and search-and-rescue operations. A meeting was held with the accounting unit in MICTTD to assess the financial management capacity within the agency.

- (i) **Staffing.** The Marine Division's accounting unit is headed by a senior accountant supervising 1 accountant and 4 account officers.
- (ii) **Accounting software.** Microsoft Access is being used by the Accounting Unit to keep track of its transactions. They do not prepare financial statements but simply a statement of expenditures against utilization of the allocated budget. Microsoft Access is not an accounting software and not capable of generating financial reports. The reports are sent to the MFED which uses Attachè, an accounting software to consolidate the submissions.
- (iii) **Budget.** Annually, the Accounting Unit consolidates budget requests from all divisions of the Ministry based on key parameters prescribed by MFED. The budget submissions are submitted and reviewed in MFED and is deliberated at the government committee level. Upon approval, warrants are issued to the ministries. MICTTD manages its utilization of the budget allocated. MICTTD

uses Microsoft Access to record their transactions against the warranty issued. Most expenditures relate only to their day-to-day recurrent charges.

- (iv) **Revenues.** The revenues that are generated by the ministry are turned over to the Treasury (under the MFED).
- (v) **Reconciliation.** Unlike MISE, the senior accountant in MICTTD conducts a weekly reconciliation of their warrant balances as there have been instances of double posting in the MFED's records.
- (vi) **Asset management.** MICTTD has an asset register which only accounts for office equipment, vehicles and the heavy equipment under MICTTD. They do not depreciate their assets and have provided minimal budget for repair and maintenance.
- (vii) **Records management.** The Senior Accountant ensures that records keeping and filing in the ministry is done well. The records are updated weekly as a basis for the reconciliation.
- (viii) **Audits.** KNAO conducts the whole-of-government audit once a year and findings are discussed with the auditees. There is no internal audit unit within MISE. A person from the MFED occasionally visits and conducts random checks mainly of revenue items but in its current review structure does not comprise an audit of internal control processes.
- (ix) **Conclusion.** The MICTTD accounting unit overall has weaknesses relating to staffing, budgeting, asset management, internal control, and audit, and FM risk is assessed as "high".

D. Financial Management System at the Kiribati Fiduciary Services Unit (KFSU)

6. The KFSU was created to handle financial aspects of project management for donor-funded projects. It is based in the MFED to allow for proper oversight by the Secretary of Finance.

7. The KFSU was initially created with 7 positions:

- (i) 1 KFSU Manager
- (ii) 1 Procurement Specialist
- (iii) 4 Accountants
- (iv) 1 Recording/Administrative Assistant

8. The KFSU performs the financial and contract management aspects of project administration for all donor-funded projects while the corresponding implementation units (PIU) handle day-to-day implementation. The KFSU has worked satisfactorily since its creation in 2011 and has been familiar with the different requirements of the donors. While there are reports of inefficiencies like delays in disbursements, these are considered minor as audit reports are unqualified and no lingering issues are noted.

9. A key risk for KFSU relates to the sustained funding for the unit. Each project funded by donors provide funding for the KFSU but as projects are completed, funds dwindle and some of the KFSU staff has moved out when their contracts are not renewed. Currently, only two accountants are left in KFSU whose contracts are expiring in December 2019. The KFSU is being funded by various donors. The World Bank's Project Preparation Advance (PPA) will continue to provide funding for the existing accountants in KFSU until June 2020. Afterward, the project will include funds to support the KFSU during its implementation.

10. Reported delays relate to unavailability of signatories, and unexpected volume of transactions. The shortage of staff in recent months also contributed to the delays when the

two accountants have to do most of the tasks including advertising for consultants which could have been the responsibility of the procurement person.

E. Financial Management Arrangements

11. Separate books of accounts and bank accounts for the project will be maintained by the KFSU designated accountant in coordination with the Project Manager under the overall supervision of MFED. The financial reporting requirements for this project will follow the requirements of the World Bank (WB) in terms of the 6-monthly Interim Financial Report, and financial inputs into the Asian Development Bank's (ADB) quarterly progress report. The financial statements for the project, which will cover funding from both the WB and ADB, will be prepared 2 months after the closing of the books of accounts in December and will be submitted to KNAO for audit. Audit reports will be submitted to WB and ADB on or before 6 months after the end of calendar year. Only audited project financial statements will be required under the project. The audit reports will be reviewed and disclosed to the public through the WB/ADB websites.

F. Disbursement Procedures

12. Direct payment, reimbursement, and advance account disbursement procedures will generally be used for the project. However, only direct payment and reimbursement will be applied for the ADB-financed components. The World Bank will also manage their funds separately. The KFSU is familiar with these disbursement procedures which have been used in most ADB- and World Bank-financed projects.

G. Suggested Covenant

13. A covenant to ensure that the government (as represented by MFED) will initiate the process of developing an asset management policy for the country to fully account for state assets, when they were constructed/rehabilitated, current valuation, the agency responsible, estimating, requesting and allocating the annual budget and undertaking the necessary repair and maintenance would help ensure the sustainability of the investments. At fact-finding, however, the project team was informed that the government, through MFED, has initiated the development of an Asset Management Information System which aims to account for all government assets that will form the basis for requesting and allocating budgets for repair and maintenance.

Table 1: Financial Management, Internal Control, and Risk Assessment

Risk	Risk Assessment	Mitigation Measures	Timeframe/ Responsibility
A. INHERENT RISKS			
1. Country Specific Risks – Kiribati has no nationwide asset management policy	Substantial	Ministries do not provide for sufficient budgets for operation and maintenance of assets under their responsibility. Assistance will be required for the country to conduct an inventory of its state assets and develop a policy for asset registry, valuation, depreciation and maintenance. An AMIS is being implemented by MFED to cover all government assets.	MFED/During project implementation
2. Country specific Risks – KNAO generally conducts the audits for all foreign-funded projects. Given the increase in workload, KNAO may reach a point where its staff may not be able to cope with its audit program	Moderate	Increased workload may affect the quality of audits and may not allow for meaningful audit processes. Consider financing audits under project funds and for audits to be conducted by independent professional auditors.	KNAO Year 2020
3. Entity specific risks – KFSU, currently donor-funded, may not receive adequate funding for its efficient operation	Substantial	KFSU is a central unit under MFED handling the financial management aspects of donor-funded projects. Staff has gained proficiency with the requirements of the donors and have functioned well in the past 8 years. Due to inadequate funding, the KFSU Manager, the procurement specialist and 3 accountants have left. Only 2 accountants were left managing both financial and procurement aspects of 7 projects they administer. Consider setting aside funding from every project approved together with an assessment of the KFSU workload.	MFED/KFSU Year 2020
4. Entity specific risks – capacity building from intended mentoring services to be done by consultants in donor-funded projects are not effective	Moderate	Almost all foreign-funded projects include aspects to build capacity but no assessment is being done during project reviews or after to assess if knowledge is indeed being/was transferred. Specific indicators (not only in terms of number of staff trained) should be set in the DMF to monitor capacity building. MFED, MICTTD, MISE, KFSU and OIIU staff will also be trained in ADB's disbursement procedures.	MFED Year 2020
5. Limited internal audit support to implementing agencies	Substantial	In the absence of internal audit units in the implementing agencies, MFED should consider a more formal arrangement to lend internal audit support to MICTTD and MISE	MFED
Overall Inherent Risk	Substantial		
B. PROJECT RISKS			
1. Delays in processing payments may be encountered which could impact overall project implementation	Substantial	The constraint would be due to the reduced staffing in the KFSU. An accountant per project may not be the right approach since the specific project may not require full time support of the accountant. A pool of funds for the fully staffed KFSU may be considered.	MFED/KFSU Starting Year 2020
2. Poor filing practices will affect the preparation of financial statements and the auditor's opinion on it	Substantial	KFSU staff has been briefed on the new FM requirements on the timely submission of APFS: that complete submission is required as per financing agreement and, unqualified opinion, as much as possible.	KFSU; starting Year 2020

Risk	Risk Assessment	Mitigation Measures	Timeframe/ Responsibility
3. There is weak oversight of the KFSU by MFED	Substantial	The KFSU was based in the MFED for appropriate oversight but it appears that the MFED has not done sufficient oversight. The KFSU is also being funded by donor funds and donors do their own supervision. The departure of staff including the KFSU manager was not addressed by MFED.	MFED; during country programming
4. The absence of an asset management policy at the state level will affect the sustainability of new investments	Substantial	The project will assist the government in utilizing AMIS to maintain the proposed facilities after project completion.	MFED; during country programming
Overall Project Risk	Substantial		
OVERALL FM RISK	Substantial		

AMIS = Asset Management Information System; APFS = audited project financial statement; FM = financial management; KFSU = Kiribati Fiduciary Services Unit; KNAO = Kiribati National Audit Office; MFED = Ministry of Finance and Economic Development; MICTTD = Ministry of Information, Communication, Transport and Tourism Development; MISE = Ministry of Infrastructure and Sustainable Energy; OIIU = outer islands implementation unit.

Sources: Asian Development Bank and the World Bank.

Table 2: Financial Management Action Plan

Weaknesses	Mitigating Action	Responsibility / Timing
1. The absence of an asset management policy will undermine the sustainability of infrastructure investments.	The government has initiated the formulation of an assets management policy which will include an inventory of state assets with details, assigned caretaker agency who will be responsible for requesting budgets for repair and maintenance.	Infrastructure government agencies and MFED; starting next budget cycle.
2. MFED will provide increased support to undertake internal audit function in MISE and MICTTD.	MFED currently provides support to these ministries through an occasional visit of an internal auditor but only to check on revenues. MFED, MISE, and MICTTD should agree on a periodic and more frequent schedule of visit from the internal auditor to conduct checks of internal control.	Infrastructure government agencies and MFED; on an agreed start date within the year.
3. MFED will provide increased oversight for the efficient functioning of the KFSU.	MFED will define a more stringent oversight of the KFSU which may include monthly meetings to resolve issues.	MFED, immediately
4. Capacity and institution building components of project management should be carefully designed. It appears that mentoring teams do not work with government agencies for proper knowledge transfer.	Consulting contracts will include indicators that not only refer to the number of staff trained without assessment of how much knowledge were truly assimilated.	ADB/WB

ADB = Asian Development Bank; KFSU = Kiribati Fiduciary Services Unit; MFED = Ministry of Finance and Economic Development; MICTTD = Ministry of Information, Communication, Transport and Tourism Development; MISE = Ministry of Infrastructure and Sustainable Energy; WB = World Bank.

Sources: Asian Development Bank and the World Bank.