



Must be communicated to those charged with governance

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We require management to acknowledge in writing its responsibility for putting in place sufficient internal controls to prevent and detect fraud. We also require management to disclose to us:

- The results of their assessment of the risk that the financial statements may be materially misstated as a result of fraud;
 - Their knowledge of fraud or suspected fraud affecting the entity involving management, employees or others; and
 - Their knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.
- MSACS have made this information available to us. Our audit has concluded that the risk of material misstatement arising from fraud is relatively high.

Reliance on Internal Audit and Other Assurances

The internal audit had not commenced as the appointment had been delayed. As explained, at some of the units / NGO's / Peripheral units, the audit had been completed but the report for the same was not available for our perusal. Hence, we are unable to comment upon the same.

Effectiveness of Communications

SA 260 requires us to review the effectiveness of communications between the auditors and those charged with governance. Throughout our audit, we tried to ensure that communications were effective. Due to ineffective working of Executive Committee, there was no interaction those charged with governance. However, we presented our audit strategy and the findings to the Project Director and the Head of Finance. The audit team also had regular meetings with the finance staff at MSACS, which ensured that all issues arising were raised at the earliest possibility, resulting in swift resolutions. Overall, communications between us and MSACS have operated effectively throughout the field work of audit but not with those charged with governance.

Material Weaknesses in Internal Control

A material weakness in the accounting and internal control systems is a deficiency in design or operation which could adversely affect the audited entity's ability to record, process, summarize and report financial and other relevant data and which might result in a material misstatement in the financial statements.

As external auditors, we will only formally communicate those audit matters that have come to our attention as a result of the performance of the audit.





MANAGEMENT LETTER

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To:
The Governing Board,
Maharashtra State AIDS Control Society,
Wadala, Mumbai 400 031

Re: Statutory Audit for the Financial Year 2012-13

Dear Sir,

Purpose, Responsibilities and Scope

The purpose of this Management Letter (the letter) is to summarize the key issues arising from the audit work that we have carried out as Statutory Auditors for financial year 2012-13 at Maharashtra State AIDS Control Society (MSACS).

Although this letter is addressed to the Governing Body of MSACS ('you') as it is your responsibility to ensure that arrangements are in place for the conduct of MSACS' business and to safeguard and properly account for public money, it is also intended to communicate those key issues to key external stakeholders, including members of the public.

MSACS is solely responsible:

- a) to establish and maintain a system of internal controls by putting into place appropriate arrangements to ensure the proper conduct of its financial affairs which includes documenting the system, communicating system requirements to employees, and assuring that the system is functioning as prescribed and is modified, as appropriate, for changes in conditions;
- b) to monitor their adequacy and effectiveness in practice, including:
 - ensuring its financial standing is soundly based;
 - the development, implementation and monitoring of adequate systems of internal control;
 - ensuring its affairs are managed in accordance with proper standards of financial conduct and to prevent and detect fraud and corruption; and
 - ensuring its financial affairs are conducted in accordance with the laws and relevant regulations applicable to the entity
- c) to ensure that arrangements are in place for the conduct of its business and to safeguard and properly account for public money; and
- d) to provide us with the necessary information, explanations and documents relating to the audit

Statutory Auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively





Overall audit approach

A comprehensive audit approach which integrates financial, compliance and value added aspects has been followed in performing the audit, with a view to providing you with an independent external audit service with an emphasis on promoting accountability, good governance and the effective, economic and efficient attainment of your goals. In addressing the financial and compliance aspects of the audit, primarily, a risk-based approach has been adopted to ensure that audit resources are clearly focused.

We collect information by interaction with your staff and review key documents to improve our understanding of your business and operations. This enables us to form a preliminary view of the strengths and weaknesses of the overall control environment. We also review the information systems controls and the controls operating over specific account balances. We use this information to identify the material risk areas. We then review judgmentally selected activities within the scope advised to us for management controls and test their operation in order to determine those on which we can place reliance, and those where we need to direct more audit effort.

We review accounting systems and management controls operated by MSACS only to the extent we consider necessary for the effective performance of the audit. The results of all these aspects of the audit are brought together and evaluated to consider the impact on our audit opinion.

The types of controls we expect to be in place are:

- i) up-to-date procedure notes, so that staff are aware of the procedures they should be following
- ii) segregation or separation of duties, so that staff act as checks on each other's actions
- iii) reconciliations between financial records and other records held, to confirm the accuracy of the financial records
- iv) access to records is limited to those who require it
- v) effective review of exception reports and other management information
- vi) effective supervision, so that any problems are promptly identified and addressed.

Audit of the accounts and accounting issues

We received a set of draft financial statements for the audit and issued a qualified opinion on the financial statements of MSACS within the submission deadline set by National AIDS Control Organisation (NACO). The draft statements were supported by working papers except for certain information and clarifications and replies to our observations which were provided subsequent to audit field work. We identified a few adjustments to the accounts which you agreed to amend.





- to maintain records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the entity;
- b) to provide management with reasonable, but not absolute assurance that transactions (including receipts and expenditures) are executed in accordance with management's authorization and recorded properly as necessary to permit the preparation of the financial statements in accordance with generally accepted accounting principles; and
 - c) to provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the entity's assets that could have a material effect on the financial statements. Because of inherent limitations in any internal control structure, errors, irregularities or misstatements may nevertheless occur and not detected. Also, projections of any evaluation of effectiveness of the structure to future periods are subject to the risk that controls and procedures may become inadequate because of changes in conditions or that the degree of compliance or that the effectiveness of the design and operation of controls with the policies and procedures may deteriorate. Furthermore, the projection of any conclusions, based on our finding to future periods is subject to the risk that changes may alter the validity of such conclusions.

In planning and performing our work, we considered MSACS' internal control over financial reporting by obtaining an understanding of the design effectiveness of MSACS' internal control, determining whether controls had been placed in operation, assessing control risk, and performing tests of MSACS' controls as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements but not to express an opinion on the effectiveness of MSACS' internal control over financial reporting.

We limited our internal control testing to those controls necessary to achieve the objectives described above. We did not test all internal controls relevant to operating objectives such as those controls relevant to ensuring efficient operations.

Our consideration of internal control over financial reporting was for the limited purposes described in the preceding paragraphs and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses.

We identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies in respect of which corrective action is yet to be fully addressed by you. Our audit opinion for this year also refers to certain deficiencies in internal control system.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles (GAAP) such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiencies described below to be significant deficiencies in internal control over financial reporting.





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A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will occur. Material weaknesses may be identified by the auditor in performing the internal control audit. Material weaknesses could not be identified by the auditor in performing the internal control audit that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses.

While some improvements were noticed because you have strengthened your performance management arrangements and embedded changes, there is still scope for you to strengthen your arrangements and our report and further collaboration with you is intended to maintain the momentum of improvement. In future, you will need to comply with both the current regulatory framework for and the requirements of donors/funding agencies. In this context, it is vital that you ensure that core systems of financial control and governance are robust.

Audit Findings

Our findings in respect of communicating matters to those charged with governance are given in Annexure to this letter. The other findings are –

1. MSACS has not developed a timely medium-term and long-term financial strategy which should seek to ensure financial stability over a challenging but realistic period of time; you have been reliant on external financial support whilst longer-term service redesign has not progressed at all.
2. Budget holders need to exercise effective financial control; we would like that you focus on “Value for money” approach throughout MSACS. Value for money is about getting the maximum benefit over time with the resources available. It is about achieving the right balance among economy, efficiency and effectiveness (the ‘3Es’), spending less and spending wisely to achieve priorities for target population.

Over the years, value for money (particularly in relation to effectiveness) has evolved to embrace expectations that are placed on public services also underpinning considerations of the quality and effectiveness of public services

As sustainable development has risen up the agenda there is recognition that efficiency and sustainability need to be balanced within robust decision making so that outcomes are effective over time. In this context, we have drawn attention to and discussed following expenditure instances with the management –

- a) The absence of an approved cost allocation plan as it increases the risk that MSACS is not fully compensated for support provided. Failure to complete and/or adequately document cost sharing and effort requirements increases the risk of reduced reimbursements and jeopardizes the future of the grant programs.
- b) procurement function needs to be strengthened with skilled personnel having strategic approach to procurement and effective management of procurement risks;
- c) printing of IEC materials on need-based activities at various locations;
- d) logistics and warehouse expenses;
- e) filling up of vacancies and training and capacity building of staff; this failure impairs the effectiveness of controls;
- f) Voluntary blood donation drive expenses through State Blood Transfusion Council;





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g) Administration of projects and programmatic grants was not always appropriate or adequately organized at peripheral units particularly DAPCUs and NGOs. These administrative and financial policies and procedures for the administration of programs proper administration of programs increases the risk of non-compliance with programmatic requirements such as cost sharing and financial/technical reporting and decreases the organizational efficiencies gained by a good administration.

h) documentation to support training for program and those responsible for the administration of contracts and grants needed improvement; the training was not documented by a formalized training schedule

i) inadequate monitoring of sub-recipient activities for various reasons including due to ineffective oversight, personnel resource constraints, staff turnover, deficient and untimely responses by sub recipients, and insufficient documentation of requests sent to sub recipients; failure to monitor sub-recipient activities increases the risk of non-compliance and jeopardizes the future of the grant programs.

j) control and accountability issues concerning staff appointed on contractual basis

k) MSACS also needs to look at:

- the extent to which there are shared objectives and whether the principles of value for money are applied to shared resources;
- whether partners in an area have a clear and common understanding of the public spending under their influence;
- whether partners understand delivery chains for outcomes and align resources and overcome barriers;
- whether partners recognize the extent to which spending in one sector could bring better value for money in another and lead to more effective overall resource use;
- how well partners measure and manage efficiencies and exploit the potential efficiency gains from working together; and
- how well partners understand the resources available to them and the extent to which they influence spending decisions, including to shift resources to deliver improved outcomes.

Action required by the Governing Board

You need to note the following significant matters –

- i) Executive Committee needs to play an effective role; system wide policies and procedures need to be developed, updated, and/or finalized for certain contracting, procurement and grant activities;
- ii) Develop a clear vision for the future or effective leadership at MSACS;
- iii) Develop strategic approach to procurement that provides value for money;
- iv) Develop strong and sustainable partnership working with NGOs and peripheral units;
- v) Strengthen middle management capacity with implications for strategic planning and management of change;
- vi) Introduce adequate and timely training for staff as also performance appraisal arrangements for staff; and
- vii) Fill up vacancies in staff positions and ensure proper segregation of duties.





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- ii) Develop a culture of financial discipline and control throughout MSACS and ensure that all staff understands the financial impact of their decisions.
- iii) Ensure that budgets and associated plans are developed and agreed in advance of the financial year to which they relate.
- iv) Review and challenge financial plans and monitoring reports to ensure that assumptions are reasonable and robust and that appropriate action is being taken to address problem areas.
- v) Ensure that financial risks are adequately identified, managed and monitored during the year and that contingency plans are established to address new or emerging issues.

Management Response

It is our understanding that MSACS management generally agrees with the findings as presented and that relevant comments from the management responsible for addressing the findings are not separately provided.

Limitations

- i) The management of MSACS is responsible for complying with laws and regulations applicable to MSACS. We performed tests of its compliance with certain provisions of laws and regulations; we limited our tests of compliance to these provisions, and we did not test compliance with all laws and regulations applicable to MSACAS. Providing an opinion on compliance with certain provisions of laws and regulations is neither an audit nor an objective of our audit.
- ii) Domain for audit was restricted to accounting procedures at MSACS in accordance with terms of reference in RFP for audit – any other information or transactions, financial or otherwise, generated or recorded based on decisions or otherwise taken at NACO or outside MSACS was not within scope of our audit;
- iii) During our walk through, we could not complete controls testing and compliance testing as planned where information requested has not been provided. An external impairment, among other things, might be
- a) non-submission of information; and
 - b) unreasonable restrictions on the time to complete an audit

In particular, we have not been able to consider information/data requested by us not provided including but not limited to relevant policies, instructions, procedures etc., ; consequently, we have not been able –

- to ensure adherence to management policies and directives in order to achieve the entity's objectives
- to safeguard assets
- to secure the relevance, reliability and integrity of information, so ensuring as far as possible the completeness and accuracy of records





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- v) Technical knowledge of business is not fully known to us and reliance is placed on identification of proprietary nature of items/proprietary source(s) of supply, where applicable;
- vi) Our work is performed on the basis of information/data furnished or made available during our visit and is not responsible for misinformation and/or non-submission of information/data. We rely on the reliability or accuracy of information provided or obtained in the course of our work and further, audit procedures that are effective for detecting a misstatement that is unintentional may not be effective for a misstatement that is intentional and is concealed particularly through forgery, collusion or management override of control systems.
- vii) In selecting our samples and other data for audit, we relied on the data provided by the management from the financial system by utilizing excel spreadsheets that has neither been subjected to IT/EDP systems audit nor reviewed for security/application controls and have not performed any additional testing on such data; such spreadsheets are prone to conversion, input and formulaic errors
- viii) Inherent limitations, if any, in financial system software and our reliance on the data validated by others as part of the audit process; we did not rely on any other systems other than to make selections for testing purposes.
- ix) Our work did not involve a detailed review of all aspects of the systems including but not limited to the financial system in CPFMS, and cannot be regarded as a comprehensive statement of all weaknesses that might exist, or of all improvements that might be made/required. In particular, the financial system (CPFMS) has neither been subjected to IT/EDP systems audit nor reviewed for security/application controls by us
- x) Balances due to and from parties including old balances and deposits are subject to confirmation
- xi) We did not visit sub-offices and other operational areas/ sites for present audit work.
- xii) We did not audit management's comments, where provided, and accordingly, we express no opinion on additional inputs/response provided by management.



Closing remarks

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Status of our reports to MSACS

Our audit management letter is prepared in the context of: the responsibilities of external auditors and MSACS management. The matters raised in this letter are only those that came to our attention during the course of our audit and are not necessarily a comprehensive statement of all inefficiencies, errors and weaknesses that exist in your systems and practices or of all improvements that might be made/required.

Our work did not involve a detailed review of all aspects of the systems, and cannot be regarded as a comprehensive statement of all weaknesses that might exist, or of all improvements that might be made.

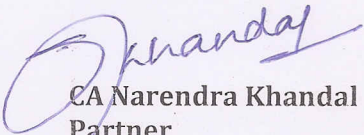
You should assess our recommendations for improvement for their full commercial implications before they are implemented. In particular we would emphasize that we are not responsible for the adequacy and appropriateness of the monitoring and evaluation study data and methodologies.

MSACS operates in a continually changing environment and MSACS and its operations are subject to a number of uncertainties and other factors, many of which are outside our control. We undertake no obligation to revise or update this information whether as a result of new information, future events or otherwise.

12 The information in this report was prepared by MKPS & Associates in connection with the external audit service under donor programs of the fund-awarding agencies and pass-through entities provided to MSACS, the audited body, and was therefore prepared specifically for the purposes of those services and solely for the benefit of MSACS, the fund-awarding agencies and pass-through entities. MKPS & Associates neither owes nor accepts any duty of care to any third party and shall not be liable for any loss, damage and/or expense, which is caused by any reliance that any other party may place on this information.

Yours truly,

For MKPS & Associates
Chartered Accountants
Firm's Regn No. 302014E


CA Narendra Khandal
Partner
M No. 065025

August 7, 2013





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As external auditors, we will only formally communicate those audit matters that have come to our attention as a result of the performance of the audit.



During our audit, we reviewed the accounting systems and management controls operated by MSAC. To the extent we considered necessary for the effective performance of the audit. As a result of the review, we detected no material weaknesses in the management control environment and material weaknesses in the design or operation of the internal control structure are given below.



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- a) need to strengthen procedures for effective grant management with a central approach for accounting, management, and training for grant compliance to reduce the risks of mismanagement in grant funding;
- b) formalizing arrangements in respect of grants provided to sub-recipient peripheral units to ensure accountability over sub-recipient peripheral units;
- c) accounting for cost-sharing and cost-allocation to different programmes with a need to formalize the system;
- d) need to improve data collection form, reporting by and oversight of DAPCUs, the district-level nodal units;
- e) timely submission of Statements of expenditure/Utilization certificates by sub-recipient NGOs (including lead NGO) and peripheral units, their verification to confirm the validity of amounts reported and adequacy of the supporting documentation and ultimately their timely adjustment in the financial record of MSACS as grant expenditure;
- f) records for Fixed assets (including but not limited to obsolete/discarded assets) at MSACS, sub-recipient NGOs and peripheral units;
- g) records for Testing Kits at MSACS and sub-recipient peripheral units
- h) Non availability of / or the non completion of internal audit at the office of the society as well as at DAPCU level etc.
- i) vacancies in sanctioned staff positions not filled also resulting in inadequate control especially lack of segregation of duties and weak governance;
- j) Management has not established a road plan or formal process to change to accrual system of accounting that will facilitate improved financial reporting and increase the financial control; in the current accounting system, there are inherent limitations and constraints on the detailed review of current assets, advances and current liabilities;
- k) Management has to design an internal control system and establish procedures for dealing with discontinuance of grants to and/or termination of tie up arrangements with sub-recipient NGOs and recoveries from sub-recipient NGOs including but not limited to assets and other materials given to sub-recipient NGOs;
- l) robust financial plans linked with operational plans need to be in place, and ensure that such plans are being delivered for ensuring value for money;
- m) suitable insurance coverage to ensure the appropriate levels and types of coverages are in place;
- n) formal policy for assuming financial obligations of employees/ex-employees who are/were on deputation from State Government, the sponsor body;
- o) Operational and fiscal evaluations or reviews of sub-recipient NGOs (including lead NGO) need to be enhanced in assessing NGOs/Peripheral units' internal control and compliance for purposes of achieving effective oversight instead of relying heavily on information obtained through interviews; Operational and fiscal evaluations or reviews presently not carried out should also be carried;



p) oversight implications of non-compliance with -



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- guidelines on financial and procurement systems for sub-recipient NGOs/CBOs prescribed by NACO with consequential impact on project implementation by sub-recipient NGOs/peripheral units, as the case may be;
- q) monitoring activities and financial utilization for which grants are awarded by MSACS to sub recipient NGOs/peripheral units where there is comingling or overlapping of other activities or there is funding received from other donor agencies;
- r) accounting discrepancies, inappropriate accounting heads used and non-reconciliation of system-generated Financial Management Reports (FMRs) and other data with financial results on timely basis due to, among other things, application software-related problems;
- s) compliance with statutory provisions of Income Tax law with respect to filing of annual income tax return and with governing organizational law for charitable/non-profit entities;
- t) consistent and timely checks on monthly salaries to contractual staff before making payment and periodical management review thereof;
- u) detailed periodical analyses of material variations between actual and budgeted expenditure and impact of adjustment of old advances (in certain cases going back by 3-4 years) during the year

