



**CAMBODIAN RURAL
DEVELOPMENT TEAM (“CRDT”)**

**Management Letter
for the year ended 31 December 2015**



KPMG Cambodia Ltd
4th floor, Delano Center
No. 144, Street 169
Sangkat Veal Vong
Khan 7 Makara, Phnom Penh
Kingdom of Cambodia

Telephone +855 (23) 216 899
Fax +855 (23) 217 279
Internet www.kpmg.com.kh

Mr. Or Channy
Executive Director
Cambodian Rural Development Team
No. 696, Street 2, Sangkat Kratie, Kratie City
Kratie Province, Kingdom of Cambodia

Our ref: NH/SCT/YSL/vy

Contact: You Sokleng

12 May 2016

Dear Sir,

Management Letter – Audit for the year ended 31 December 2015

We have audited in accordance with Cambodian International Standards on Auditing the financial statements of Cambodian Rural Development Team (“the Organisation”), for the year ended 31 December 2015 and have issued our report thereon dated 12 May 2016. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we considered internal control relevant to the Organisation’s 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 the Organisation’s internal control. Accordingly, we do not express an opinion on the effectiveness of the Organisation’s internal control.

The maintenance of adequate control designed to fulfill control objectives is the responsibility of management. Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, controls found to be functioning at a point in time may later be found deficient because of the performance of those responsible for applying them, and there can be no assurance that controls currently in existence will prove to be adequate in the future as changes take place in the Organisation.

During our audit we noted certain matters involving internal control and other operational matters that are presented for your consideration. These comments and recommendations, all of which have been discussed with the appropriate members of management, are intended to improve internal control or result in other operating efficiencies and are summarised in the enclosed report.

Our audit procedures are designed primarily to enable us to form an opinion on the financial statements, and therefore may not bring to light all weaknesses in policies or procedures that may exist. We aim, however, to use our knowledge of the Organisation gained during our work to make comments and suggestions that we hope will be useful to you.



We would be pleased to discuss these comments and recommendations with you at any time.

The Organisation's written response to our comments and recommendations has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

This communication is intended solely for the information and use of the Organisation's management, and others within the Organisation and is not intended to be and should not be used by anyone other than these specified parties.

Yours faithfully,
KPMG Cambodia Ltd

Lim Chew Teng
Partner





Contents

| | Page |
|--|-------------|
| 1. Develop a comparison between budget and actual expenses | 1 |
| 2. Improve control over non-expandable equipment | 2 |
| 3. Improve control over cost sharing | 4 |
| 4. Comply with tax regulations | 5 |
| 5. Improve control over loan at Mekong Credit Association (“MCA”) | 6 |
| 6. Improve control over documentation | 7 |
| Status of the previous year’s recommendations | 9 |

1. Develop a comparison between budget and actual expenses

Observation

The comparison of actual expenditure against the budget did not take into account the under/overspent budget.

This issue was also raised following the previous years’ audit.

Implication

Variances of expenditure against budget if not fully explained makes it more difficult for CRDT to monitor and control the use of its budget for activities and to analyse the results for the year.

Recommendation

The management should perform its formal comparison of actual expenditure against the budget for expenditure on a cumulative basis as well as perform period to period comparison.

Management’s response 2014

In 2014 this control was not implemented. In 2015 this has been partially implemented and it is management’s intention to implement this control fully in 2016. We now prepared budgets by projects which includes a prior year comparison. This is issued to the project managers and budget holders at the beginning of the period and is now updated with actual spent each month as part of the preparation of the monthly management accounts. This has proved to be a useful monitoring tool and to add further analysis to unexpected variances between the expected and actual spent. Budget holders are required to give further explanation on variances greater than 10% from the expected results. We plan to produce an organisational budget for the year ending 31 December 2016 which will show budgets, along with prior year comparatives and will be updated with actuals each month. We also intend to produce a cash flow forecast to monitor our cash balance at the end of each month.

Management’s response 2015

In 2015 this has been partially implemented and it is management’s intention to implement this control fully in 2016. We now prepared budgets by projects which includes a prior year comparison. This is issued to the project managers and budget holders at the beginning of the period and is now updated with actual spend each month as part of the preparation of the monthly management accounts. This has proved to be a useful monitoring tool and to add further analysis to unexpected variances between the expected and actual spend. Budget holders are required to give further explanation on variances greater than 10% from the expected results. We have produced an organisational budget for the year ending 31 December 2016 which show budgets, along with prior year comparatives and have been updated with actuals each month.

2. Improve control over non-expandable equipment

Observations

- (i) The non-expendable equipment register was not properly updated and no regular reconciliation has been performed between the items listed in the non-expendable equipment listing against those recorded in the general ledger.
- (ii) There are no vehicle logbooks maintained to monitor the vehicles' operation during our review.
- (iii) The financial policy of CRDT is to record the assets with individual price of greater than \$100 into the inventory listing (or know as non-expandable equipment register) for control purpose. However, there are certain minor assets were posted in the non-expandable equipment account code, and they are not reconciled with the non-expendable equipment register.

These issues (i) and (ii) were also raised in the previous years' audit.

Implications

- (i) Without proper reconciliations, CRDT may not be able to ascertain the completeness of additional items which were purchased or transferred from donors during the year. It may be difficult to monitor, control and account for the non-expendable equipment belonging to CRDT.
- (ii) Without the vehicle logbooks, the vehicles might be used for personal purposes and there are no adequate controls to monitor the usage of the vehicles.
- (iii) The inconsistent practice for capitalisation with financial policy makes it harder for the Organisation management to monitor and control the completeness of the non-expendable equipment.

Recommendations

- (i) Proper reconciliation of non-expendable equipment between the general ledger and the listing should be performed on monthly basis.
- (ii) Logbooks should be maintained for all CRDT's vehicles. It should be reviewed and approved by the management.
- (iii) The management should adhere restrict to the financial policy monitoring and controlling the completeness of non-expandable equipment.

2. Improve control over non-expandable equipment (continued)

Management’s response 2014

In 2014 this control was not implemented. In 2015 this has been partially implemented and it is management’s intention to implement this control fully in 2016. The logbooks are now updated each quarter and approved by both the program manager and the Executive Director. We are due to conduct a full review of these items in the year ending 31 December 2016 and following this review we plan to reconcile this account each quarter to ensure completeness. This control recommendation has therefore been implemented with the exception of the performance of regular reconciliations which will be implemented in the next financial year.

Management’s response 2015

In 2015 this has been partially implemented and it is management’s intention to implement this control fully in 2016. The logbooks are now updated each quarter and approved by both the program manager and the Executive Director. We are due to conduct a full review of these items in the year ending 31 December 2016 and following this review we plan to reconcile this account each quarter to ensure completeness. The performance of regular reconciliations will also be implemented in this financial year.

3. Improve control over cost sharing

Observation

We noted that the Project does not have a standard/proper cost sharing procedure in recording expenses by donors.

This issue was also raised in the previous years’ audit.

Implication

This gives rise to difficulties in ensuring the accuracy of the project expenses.

Recommendation

Standard/proper cost sharing procedures by project donor funding should be adopted. This would improve the accuracy and reliability of project expenses.

Management’s response 2014

In 2014 this control was not implemented. It is management’s intention to implement this control fully in 2016. It is one of our main financial management objectives for this financial year to develop an effective absorption cost model to be able to effectively absorb the overhead costs incurred by head office. This control recommendation should be resolved by the audit for financial year ending 31 December 2016.

Management’s response 2015

It is management’s intention to implement this control fully in 2016. We have now developed an effective absorption cost model to be able to effectively absorb the overhead costs incurred by head office. These recharges of the support costs are going to be journaled into each business unit of the CRDT Group each quarter to properly show the true cost of running each unit. This control recommendation will therefore be resolved by the audit for financial year ending 31 December 2016.

4. Comply with tax regulations

Observations

- (i) The staff's 13th month salary/Khmer New Year Bonus as well as the monthly allowance provided to staff were not included in the salary tax calculation.
- (ii) The withholding tax on provincial offices rental (except head office) was not deducted and remitted to the GDT.

These issues were also raised in the previous years' audit.

Implication

CRDT may be subject to a unilateral assessment for salary and withholding tax. This could result in the imposition of penalties to 40% of the unpaid tax, together with interesting accruing at the rate of 2% per month. CRDT would also be liable for the amount for tax not declared.

Recommendation

We recommend that the management should review all expenditures subject to salary tax, fringe benefit and withholding tax and ensure that those taxes are paid to the GDT in accordance with the Cambodian Law on Taxation.

Management's response 2014

- (i) The salary tax withheld from local staff and paid to the GDT during the year is now correctly based on the gross amount. The staff's 13th month salary/Khmer New Year Bonus is not included in the salary tax calculation for the year ended 31 December 2014. However, management plan to tax the bonus which is payable in March 2016 so this control recommendation will have been fully taken up in the audit of the financial statements for the year ending 31 December 2016.
- (ii) This was applicable in 2014 and this control was not implemented. However, it is noted that this is not yet being followed in full, but we plan to follow this in the year ending 31 December 2016.

Management's response 2015

- (i) The salary tax withheld from local staff and paid to the GDT during the year is now correctly based on the gross amount. The staff's 13th month salary/Khmer New Year Bonus is not included in the salary tax calculation for the year ended 31 December 2014. However, management plan to tax the bonus which is payable in March 2016 so this control recommendation will have been fully taken up in the audit of the financial statements for the year ending 31 December 2016.
- (ii) This was applicable in 2014 and this control was not implemented. However, it is noted that this is not yet being followed in full, but we plan to follow this in the year ending 31 December 2016.

5. Improve control over loan at Mekong Credit Association (“MCA”)

Observation

Some important information were not included in the loan listing, such as loan ID, interest rate, term, start date, maturity date, etc.

This issue was also raised in the previous year’s audit.

Implication

Without those detailed information, management may find it difficult and time consuming to review or verify the documents.

Recommendation

Important information of each loan should be recorded in the loan listing which eases management’s review and analysis of the loan status.

Management’s response 2014

This recommendation has been implemented. The loan listing now shows the key aspects of the loan, namely the loan ID, interest rate, term, start date, maturity date, etc.

This control recommendation has therefore been partially taken up.

Management’s response 2015

This recommendation has been partially implemented. The loan listing now shows the loan ID and the start date. We will ensure in 2016 the listing will also include the term, the interest rate and the maturity date.

6. Improve control over vouchers and documentation

Observations

- (i) Some vouchers were not approved by the Executive Director (“ED”), especially those prepared from quarter 4 of 2015.
- (ii) The official receipts were not pre-numbered.
- (iii) There was no timesheet for each employee is prepared.

Implications

- (i) In the absence of ED approval, error and unauthorised payment or receipts may not be detected and corrected in timely manner.
- (ii) Management may be difficult to ensure completeness of receipts during the years.
- (iii) Without prepared timesheets, cost allocation among projects and donors; meanwhile, since CRDT is implementing projects sponsored by USAID, it is non-compliant with the USAID guideline.

Recommendations

- (i) Management should ensure that all vouchers including payment vouchers, receipt vouchers and journal vouchers are properly reviewed and approved by ED.
- (ii) The pre-numbered official receipts should be prepared and reviewed by the authorised persons so that the completeness
- (iii) Timesheet should be regularly prepared by staff, reviewed and approved by superior or management.

Management’s response

- (i) Noted. We are in the process of revising our financial policy, namely our authorisation process to make the process more realistically feasible. It is noted the time it takes to authorise each voucher is too considerable and therefore is too much of an onus on the Executive Director’s time. This means he is spending too much time of his time not acting in the best interests of the company, which can be a breach of his fiduciary duty to the Board of Directors. Therefore, it is proposed that the authoriser is the Finance Manager (a member of the management committee who answers to the board), the reviewer is the direct manager to the preparer, and the preparer is a third person. This is deemed to be sufficient segregation of duties to comply with good financial internal control.

6. Improve control over vouchers and documentation (continued)

Management’s response (continued)

- (ii) Noted. This recommendation will be implemented in the next financial year as it has been assessed this would be feasible to implement.
- (iii) Noted. This is not feasible with our current resources yet. Maybe in the future we can consider implementing timesheets but at the moment, without investing in an integrated timesheet system this would take up considerable time for all staff which would mean we wouldn’t be able to focus on how core responsibilities to our donors.

Status of the previous year’s recommendations

| No. | Auditors’ recommendation | Status |
|-----|---|--|
| 1. | <p>Improve control over cash management</p> <p>(i) We recommend that CRDT should prepare a cash book to record the cash transactions for internal control purpose.</p> <p>(ii) Regular reconciliation should be carried out to identify potential unrecorded items such as interest and bank charges as well as potentially unusual movement of balances every month while regular or surprise cash counts should be conducted by the attendance of independent staff.</p> | Implemented. |
| 2. | <p>Obtain official approval for the annual budget</p> <p>We recommend that CRDT should obtain the official written approval of the budget from the BoD in a timely manner.</p> | Implemented. |
| 3. | <p>Develop a more detailed budget and comparison with the actual expenses</p> <p>(i) The management should consider preparing a detailed budget at the beginning of each year and use it as a tool to monitor that the use of its funds is consistent with the planned allocation of funds.</p> <p>(ii) The management should perform its formal comparison of actual expenditure against the budget for expenditure on a cumulative basis as well as perform period to period comparison.</p> | Partially implemented. Refer to management letter, item #1. |
| 4. | <p>Improve control over non-expandable equipment</p> <p>(i) Proper reconciliation of non-expendable equipment between the general ledger and the listing should be performed on monthly basis.</p> <p>(ii) Logbooks should be maintained for all CRDT’s vehicles. It should be reviewed and approved by the management.</p> | Partially implemented. Refer to management letter, item #2. |

Status of the previous year’s recommendations (continued)

| No. | Auditors’ recommendation | Status |
|-----|---|--|
| 5. | <p>Improve control over cost sharing</p> <p>Standard/proper cost sharing procedures by project donor funding should be adopted. This would improve the accuracy and reliability of project expenses.</p> | Not implemented. Refer to management letter, item #3. |
| 6. | <p>Improve control over advance</p> <p>(i) CRDT should set up a policy for cash advances, including the limits to the size of advances and timetables for clearance. It should also ensure that advances are not recorded as expenses until they have been cleared.</p> <p>(ii) A record or listing of advances should be prepared and updated each time the advance is made or cleared and liquidated. The record/listing should contain sufficient information (i.e., name, cash advance form reference number, date of cash advance, amount advanced, date of clearing the advances, amount cleared).</p> | Implemented. |
| 7. | <p>Complying with tax regulations</p> <p>We recommend that the management should review all expenditures subject to salary tax, fringe benefit and withholding tax and ensure that those taxes are paid to the GDT in accordance with the Cambodian Law on Taxation.</p> | Partially implemented. Refer to management letter, item #4. |
| 8. | <p>Take up agreed audited adjustments</p> <p>All post audit adjustments should be recorded immediately to correct the beginning balance of the preceding year.</p> | Implemented. |
| 9. | <p>Improve control over documentation</p> <p>We recommend that CRDT should ensure that all supporting documents are attached with receipt and payment vouchers and should be prepared, reviewed and approved by appropriated person.</p> | Implemented. |

Status of the previous year’s recommendations (continued)

| No. | Auditors’ recommendation | Status |
|------------|---|---|
| 10. | <p>Improve control over loan at Mekong Credit Association (“MCA”)</p> <p>(i) Without loan follow-up report, the management may not be able to assess the appropriateness of the loan disbursed to the SHG.</p> <p>(ii) Without management review and approval on the loan listing, errors or misstatements may not be detected and corrected in a timely manner.</p> <p>(iii) Without those detailed information, management may find it difficult and time consuming to review or verify the documents.</p> | <p>Partially Implemented. Refer to management letter item #5.</p> |