



TERMS OF REFERENCE AND SCOPE OF SERVICES
PACIFIC AVIATION SAFETY OFFICE REFORM PROJECT

PROJECT AUDIT FOR PASO REFORM PROJECT
PASO/LCS/P-A04

1 BACKGROUND

- 1.1 The Pacific Aviation Safety Office (PASO) is currently implementing the Pacific Aviation Safety Office Reform Project (PASO Reform Project), supported by the World Bank. The PASO Reform Project has the development objective to ensure effective regional delivery of aviation safety and security oversight in Pacific Island Countries by strengthening the Pacific Aviation Safety Office's technical and coordination capacity. The project's implementing Entity is PASO, with project implementation support from the Technical and Fiduciary Services Unit (TFSU) of the Pacific Aviation Investment Program (PAIP).
- 1.2 The specialized nature of aviation places a high burden on small countries with limited human resources. Assessments of the aviation sector in the South Pacific by the International Civil Aviation Organization (ICAO) have found that many of the countries lack the proper policy, regulatory and infrastructure to comply with ICAO requirements (referred to as Standards and Recommended Practices or SARP). In recent years, these standards have been continuously expanded, particularly those related to security. As a result, the PICs have received less than satisfactory results from the ICAO-mandated Universal Safety Oversight Audit Program and Universal Security Oversight Audit Program.
- 1.3 PASO currently provides advisory, inspection, and oversight services covering the areas of: (i) aerodrome assessment; (ii) security; (iii) aircraft airworthiness; (iv) flight operations; and, (v) personnel licensing. However, its existing subscription and fee-for-service business model has not proven to be sustainable since: (i) countries have not purchased the necessary safety oversight services; (ii) there is a real, or perceived, lack of qualified technical specialists in PASO to perform the technical services, affecting demand; (iii) some countries are in arrears on member subscription fees; and, (iv) salaries and cost structures for PASO do not correctly reflect the demand for services.
- 1.4 To help ensure the long-term viability of PASO, the Pacific Regional Infrastructure Facility (PRIF) has provided resources for the preparation of a new Business Plan as part of the IDA-financed 'Pacific Aviation Investment Program' (PAIP)¹. The PASO Business Plan² provided a strategy for addressing the financial, organizational and operational shortcomings of PASO. The PASO Council agreed to implement the principles of the

¹ Phase 1 includes Kiribati (P128938), Tonga (P128939) and Tuvalu (P128940); Phase 2 includes Samoa (P143408)

² Pacific Aviation Safety Office - Final Business Plan. CAPA Report TAL/CF/PB01. May 2013.

Business Plan at a special general meeting in April 2013 and, once implemented, will reinforce and strengthen PASO's critical role in ensuring safe aviation operations in PICs.

- 1.5 Building on the Asian Development Bank (ADB) TA, the PASO Business Plan calls for significant reforms and a refocusing of the organization on objectives consistent with a Regional Safety Oversight Organizations (RSOO)³ and the global framework of ICAO. A fully-functioning RSOO capable of supporting and assisting the member States in meeting their contracted regulatory obligations by providing high standards of safety and security oversight and ongoing surveillance would provide a significant improvement to the safety of aviation in PICs.
- 1.6 PASO now has a Strategic Plan for 2018-2022 that it is currently implementing that builds on the work of the Business Plan, as well as outlining more strategic initiatives.
- 1.7 The PASO Reform Project is designed around four main components that will support the reform agenda, build institutional capacity to meet international aviation safety regulations across the region, and modernize information systems for enhancing quality control:-

Component A: Transitional Management and Support (approximately US\$ 3.03 million):

Activities to assist PASO through the restructuring process including, financing the costs associated with: (i) implementing a new organizational framework and staff changes, including financing of severance packages for termination of existing contracts of staff; (ii) conducting legal reviews for strengthening its governance and management; (iii) evaluating the PASO funding approach, including finding new revenue sources; (iv) conducting workshops and seminars for PASO Council members; (v) developing a communications strategy; (vi) transitional support to implement the new Business Plan, including engagement of TFSU for provision of support to PASO as per terms of a Service Agreement; (vii) carrying out annual financial audits of the Project as agreed with the Association; (viii) financial modelling; (ix) strategic planning review; (x) stakeholder engagement; (xi) strategic engagement

Component B: Establishment of a Pool of Regional Aviation Inspectors (approximately US\$1.38 million): Activities to assist PASO in establishing a pool of inspectors to be used by PASO to oversee aviation safety and security, including: (i) establishing a comprehensive Register of Inspectors for the region available for PASO-related services; (ii) establishing a Regional Program of Inspectors to build and assess the capacity of inspectors from Member States; (iii) provision of necessary training for inspectors to ensure they meet skill levels necessary to provide PASO services; (iv) provision of training to PASO staff to develop the human resources to deliver the necessary services; (v) Pacific Inspector Development Program training; (vi) training for Civil Aviation Authorities; (vi) governance training and support for Council members;

Component C: Quality Management (approximately US\$0.944 million): Including: (i) establishing a quality assurance system for PASO to ensure that all operations meet an appropriate standard; and (ii) implementing a PASO Management Information System with an appropriate IT network, including a document management system.

Component D: Supporting Regional Aviation Infrastructure (approximately US\$1.30 million including contingencies): Including: (i) Expanding regional aeronautical data and communication network through the acquisition and installation of very small aperture terminal equipment for the Cook Islands and Niue; (ii) supporting States with their Remotely Pilot Aircraft Systems (RPAS) requirements.

- 1.8 Day to day implementation of the PASO Reform Project is led by PASO, with the support of the PAIP 'Technical and Fiduciary Services Unit (TFSU)' and is formalized in a Service

³ "Classification of Regional Safety Oversight Organizations", ICAO, December 2012.

Agreement. The TFSU provides technical, procurement, financial management, contract management and overall project management services.

- 1.9 A PASO Steering Committee (PSC) has been established comprised of PASO Council members from Papua New Guinea, Vanuatu, New Zealand, Samoa and Kiribati, to oversee the project direction and coordination.
- 1.10 The main objective of this assignment is to undertake an annual financial project audit for 4 financial years:
 - January to December 2018
 - January to December 2019
 - January to December 2020
 - January to December 2021

2 Background on assignment

Responsibility for Preparation of Project Financial Statements

Accounting and financial management practices are governed by PASO's Manual on Financial Policy and Procedures and Financial Regulations and Delegations of Authority and other financial management procedures of the World Bank: Bank's Guidelines on Annual Financial Reporting for World Bank – Financed Activities, 30th June 2003; World Bank Procurement Guidelines; and Disbursement Guidelines for Projects: May 2006. PASO used MYOB for financial management purposes. Financial reports i.e. budget and project financial accounts can be extracted as required.

The Client (PASO) is responsible for preparing the financial statements that:

- Comply with generally accepted accounting practice;
- Fairly reflect PASO reform project's financial position; and
- Fairly reflect PASO reform project's service performance, outcomes and objectives.

The Financing Agreement and Grant Agreement requires the Client to submit to the Bank no later than six months after the end of each accounting period to which the audit refers, the financial statements, including the audit report and management letter.

Project Financial Statements

The project financial statements will be produced on cash basis in accordance with the International Public Sector Accounting Standard (IPSAS) by PASO and will rely on information contained in the quarterly Interim Financial Reports. Information contained in the financial statements shall include:

- a) a Statement of Cash Receipts and Payments;
- b) a Statement of Comparison of Budget and Actual Amounts;
- c) Notes, comprising a summary of significant accounting policies and other explanatory notes

3 Outcomes and objectives

By the end of this assignment:

- PASO will have fully audited financial statements for the calendar years of 2018, 2019, 2020, and 2021 of the PASO Reform Project
- PASO will be aware of any financial issues regarding the PASO Reform Project and be able to act on them for the next financial year

The objective of the audit of the project financial statements is to enable the auditor to express an opinion:

on the financial position of the project at the end of each accounting period and of the funds received and expenditures for the accounting periods ended 31 December each

year, as reported by the project financial statements (PFS), as well as an opinion on the Statements of Expenditures and the Designated Account.

The project accounts provide the basis for preparation of the project financial statements and are established to reflect the financial transactions in respect of the project. The project's accounting system including book keeping is maintained by PASO as the Implementing Agency

4 Scope of work

The audit will be carried out in accordance with International Auditing Standards (IAS) and will include such tests and controls as the Auditor considers necessary under the circumstances so as to allow an audit opinion to be formed. It is highly desirable that the Auditor be familiar with the Guidelines: Annual Financial Reporting and Auditing for World Bank Financed Projects (June 2003). The Auditor should also be familiar with the Bank's Disbursement Manual and Procurement Policies and Procedures. These documents may be obtained from the Project Team.

The Auditor shall submit the audit report no later than six (6) weeks after receiving the financial statements for each period at the end of the Financial Year, to PASO General Manager as the Client's designated agent.

In carrying out the audit, special attention should be paid to the following: General matters, Statement of Expenditure, Designated Accounts, Audit Opinion and Management Letter, as well as the following:

- a. **Fraud and Corruption:** Consider the risks of material misstatements in the financial statements due to fraud as required by IAS 240: The Auditor's Responsibility to Consider Fraud in an Audit of Financial Statements. The auditor is required to identify and assess these risks (of material misstatement of the financial statements) due to fraud, obtain sufficient appropriate audit evidence about the assessed risks; and respond appropriately to identified or suspected fraud;
- b. **Laws and Regulations:** In designing and performing audit procedures, evaluating and reporting the results, consider that noncompliance by the implementing agency with laws and regulations may materially affect the financial statements as required by IAS 250: Consideration of Laws and Regulations in an Audit of Financial Statements;
- c. **Governance:** Communicate audit matters of governance interest arising from the audit of financial statements with those charged with governance of an entity as required by International Standards on Auditing 260: Communication of Audit Matters with those Charged with Governance
- d. **Risks:** In order to reduce audit risk to an acceptable low level, determine the overall responses to assessed risks at the financial statement level, and design and perform further audit procedures to respond to assessed risks at the assertion level as required by Internal Standard on Auditing 330: the Auditor's Procedures in Response to Assessed Risks.

General Matters

- a. All external funds have been used in accordance with the conditions of the relevant financing agreements, with due attention to economy and efficiency, and only for the purposes for which they were provided.
- b. Goods and services financed have been procured in accordance with the relevant financing agreement;
- c. All necessary supporting documents, records, and accounts have been kept in respect of all project activities including expenditures reported via quarterly Interim Financial Reports. Clear links should exist between the project account records and reports presented to the Bank.

- d. The Designated Accounts have been used and maintained in accordance with the provisions of the relevant financing agreement;
- e. The project financial statements have been prepared in accordance with consistently applied cash basis International Public Sector Accounting Standards (IPSAS) and give a true and fair view of the financial situation of the project as at 31st December of the audit period (i.e. 2018, 2019, 2020, 2021) and of resources and expenditures for the period ended on that date.

Statements of Expenditures

As part of the audit of the project financial statements, the Auditor is required to audit Statements of Expenditure used as the basis for the submission of withdrawal applications. The Auditor shall apply such tests and controls as he considers necessary under the circumstances. These expenditures should be carefully compared for project eligibility with the relevant financing agreements. Where ineligible expenditures are identified as having been included in withdrawal applications and reimbursed against, the same should be separately noted by the Auditor.

Designated Accounts

The Designated Accounts usually comprise: advances received from the Bank; payments substantiated by withdrawal applications; interest earned from the balances and which belong to the Borrower; and the remaining balances at the end of each fiscal year.

The Auditor must form an opinion as to the degree of compliance with the Bank's procedures and the balance of the Designated Accounts at year-end. The audit should examine the eligibility and correctness of financial transactions during the period under review and fund balances at the end of such a period, the operation and use of the Designated Accounts in accordance with the financing agreement, and the adequacy of internal controls for this type of disbursement mechanism.

Designated Account statements will be included with each Withdrawal Application reporting eligible expenditures paid from the Designated Account.

Employment Authority or Entity

PASO is the contracting authority for the auditing service. The proposal for auditing service should be addressed to the General Manager of PASO who will select and make the appointment of the auditor.

Audit Opinion

The auditor will issue an audit opinion on the Project Financial Statements and in addition separate paragraphs should give an opinion on:

- a. the accuracy and propriety of expenditures withdrawn under Statements of Expenditure procedures and the extent to which the Bank can rely on Statements of Expenditures; and
- b. the operations of the Designated Accounts.
- c. key internal control weaknesses and non-compliance with the financing agreement terms.

Management Letter

As part of audit reports, the Auditor will prepare a "management letter", in which he will:

- a. give comments and observations on the accounting records, systems, and controls that were examined during the course of the audit and make recommendations for improvement;

- b. identify specific deficiencies and areas of weakness in systems and controls and make recommendation for their improvement;
- c. report on the degree of compliance of each of the financial covenants on the financing agreement and give comments, if any, on internal and external matters affecting such compliance and make recommendations for improvement;
- d. communicate matters that have come to attention during the audit which might have a significant impact on the implementation of the project;
- e. give comments on the extent to which outstanding issues/qualifications issues have been addressed;
- f. give comments on previous audits' recommendations that have not been satisfactorily implemented; and
- g. bring to the Client's (PASO) borrower's attention any other matters that the Auditor considers pertinent.

Ideally, the management letter should also include responses from the implementing agency (PASO) to the issues highlighted by the auditor.

The financial statements, including the audit opinion, and management letter should be received in four copies in English not later than June 30 of each fiscal year.

Delivery of Opinions and Reports

The auditor is required to provide the following opinions and reports to PASO who will distribute the reports as applicable to:

- Technical Financing Services Unit (TFSU)
- World Bank
- Audit Opinions on the project financial statements of each fiscal year.
- Additional, specific opinions on the Statement of Expenditures and Designated Account at the end of each fiscal year.
- Management Letter that covers all matters arising from the audit outlined above

PASO may also require other documents to be submitted for the auditors to support the findings in the management letter and to conform to reporting requirements of the International Auditing Standards.

The auditor will provide a copy of audit evidence that supports the issues raised in the management letter to PASO at the completion of the audit. The auditor will also make themselves available and the full audit file upon request of PASO should any matters arise that require further clarification.

All reports must be provided in the English language and within specified timeframes as required by PASO.

General Provision on Client's Inputs

The Auditor will be given access to all legal documents, correspondence, and any other information associated with the project and deemed necessary by the Auditor. Confirmation should also be obtained of amounts disbursed and outstanding at the Bank and of amounts disbursed under IDA and PRIF funding. The World Bank disbursement department can provide separate confirmation of these amounts, which can be accessed with assistance from the World Bank Task Team Leader for the project. Available information should include copies of the relevant: project appraisal document; financing agreement; financial management assessment reports; supervision mission reports and implementation status reports.

General Provision on World Bank Guidelines

It is highly desirable that the auditor becomes familiar with the Bank's Guidelines on Annual Financial Reporting for World Bank-Financed Activities, June 30, 2003, which summarizes the Bank's financial reporting and auditing requirements. The auditor should be familiar with World Bank Procurement Guidelines, which can be obtained from the project implementing agency. The auditor should also be familiar with the Bank's Disbursement Handbook for World Bank Clients, Disbursement Guidelines for Projects: May 2006. These documents are available on the Bank's website and could be obtained from the Task Team Leader.

Independence

The auditor will be impartial and independent from any aspects of management or financial interest in the entity under audit. In particular, the auditor should be independent of the control of the entity. The auditor should not, during the period covered by the audit, be employed by, or serve as director for, or have any financial or close business relationship with the entity. The auditor should not have any close personal relationships with any senior participant in the management of the entity. The auditor must disclose any issues or relationships that might compromise their independence.

Auditor and Audit Staff Competence

The auditor must be authorized to practice in the country and be capable of applying the agreed International Auditing Standards. The auditor should have adequate staff, with appropriate professional qualifications and suitable experience, including experience in auditing the accounts of entities comparable in nature, size and complexity to the entity whose audit they are to undertake.

5 Expertise requirements

The following criteria should be considered for evaluation:

- The firm should demonstrate good track record of undertaking audits;
- Comply with all appropriate independence and professional procedures as specific under International Auditing Standards;
- Demonstration of understanding of WB policies with respect to procurement and financial management including auditing guidelines while managing WB assisted projects;
- Clarity of proposed work plan and meeting expected timeline for completing the service;
- Experience and qualification of proposed key persons within the audit team;
- Reasonable audit fee and hours proposed to complete the audit; and
- Whether the firm has professional indemnity insurance in place and a statement of independence and how this will be managed during the audit.

PASO is a regional organisation and is comprised of members from the Pacific Island Forum; accordingly, the firm will require exceptional communication, personal and cross-cultural skills in delivering these services in the context of the multi-cultural and multi-national environment.

6 Schedule of deliverables, payment milestones & proposal requirements

The firm is expected to complete the above scope per below timeline.

| DELIVERABLE | Due | Payment Milestone* |
|------------------------------------|-------------------|--------------------|
| D1 Final Project Audit Report 2018 | End of March 2019 | 25% |
| D2 Final Project Audit Report 2019 | End of March 2020 | 25% |
| D3 Final Project Audit Report 2020 | End of March 2021 | 25% |
| D4 Final Project Audit Report 2021 | End of March 2022 | 25% |

*Payments will be made on acceptance of deliverables

- Regular updates to the PASO General Manager on the progress of works including significant issues or achievements that may impact on the normal course of deliverables.
- All deliverables will be paid on acceptance.

7 Services and facilities to be provided by the client & statement of access

The auditor will have full and complete access, at all reasonable times, to all records and documents including books of account, legal agreements, bank records, invoices and any other information associated with the project and deemed necessary by the auditor.

The auditor will be provided with full cooperation by the project Executing, Implementing units and Entities, whose activities involve, or may be reflected in, the Annual Project financial statements. The auditor will be assured rights of access to banks and depositories, consultants, contractors and other persons or firms hired by the PASO relating to this project.

Access to office facilities, international and national phone lines and internet access.