



The O.S.C.A.R Foundation

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OFFICIAL INFORMATION ACT

Briefing to Ministry of Social Development – 3 May 2012
Confidential

Scope

Scope of review

1. The implementation by OSCAR of the Deloitte recommendations made in December 2008.
2. How well is OSCAR's governance and management operating now
 - The structure in place;
 - Nature & quality of information provided and the effectiveness of the current leadership team.
3. Examine the actual nature of OSCAR's recent expenditure focussing on whether there is any evidence of unusual or inappropriate expenditure.
4. Assess OSCAR's current financial position and in particular its solvency.

Implementation of Deloitte 2008 recommendations

Deloitte 2008 Recommendations & Status

Recommendation	Implemented?	Observations
Management accounts “sense checked” by an external accountant	No	However Mr Upton advised that OSCAR’s accounts person gets support from the auditors on accounting issues. Despite this OSCAR’s management accounts are materially misleading (see the Solvency section below).
Financial system should report revenues and direct expenses on a contract by contract basis	Yes	The financial system now captures direct costs (but not wages) for specific projects (e.g. conference).
Two passwords for internet banking	No	Mr Upton and the accountant are both password holders, only one required to authorise payments.
Cease signing blank cheques	Yes	Advised this no longer occurs. No signed blank cheques in the cheque book at the time of fieldwork.

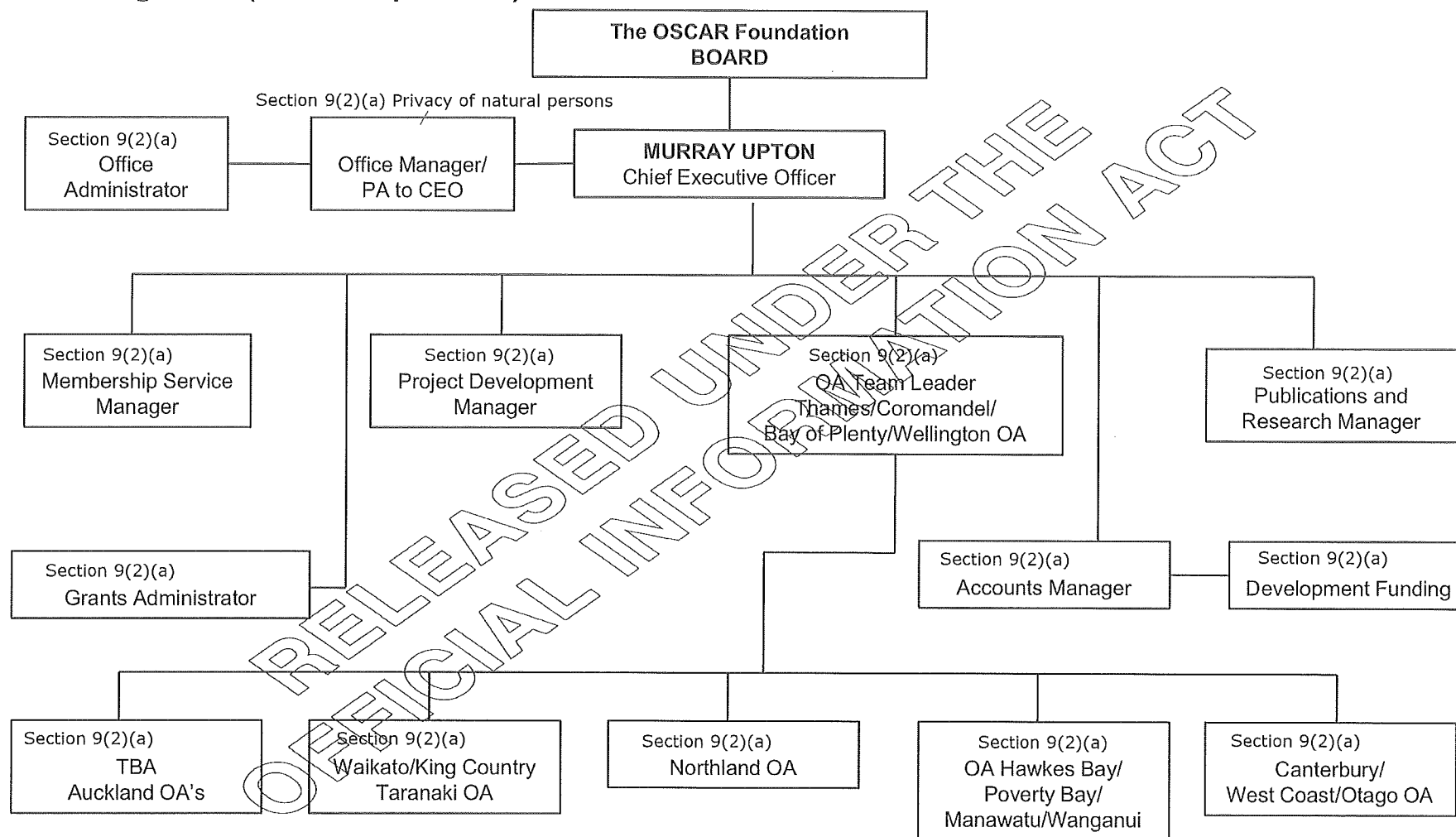
Deloitte 2008 Recommendations & Status

Recommendation	Implemented?	Observations
Petty cash should be topped up to <u>\$200</u> limit, not by \$200	No	
Bank reconciliation should be reviewed	No	
The process for accounting and banking inwards cheques should be changed so that all cheques received are banked	Partial	The process has been modified. Further work would be required to determine if this change was effective.
CEO credit card should not be paid by direct credit and the expenditure should be reviewed by the Chair or Finance Committee	No	The credit card is paid by the CEO (internet transfer) – no evidence of expenditure review by Chair or Finance Committee, although Mr Upton notes the costs are included in the management accounts.

Governance and Management

Governance & Management

Management (as at 12 April 2008)



Governance & Management

Board

Board Members

- Peter Heaslip, Chair
- George Erueti
- Rebecca Scott, Deputy Chair and Treasurer – resigned by email at 1.00 pm 29 March 2012 citing Section 9(2)(a)
- Leigh Gibson – resigned by email at 2.55 pm 29 March 2012 citing Section 9(2)(a)
(see below)
- Annette Reilly – resigned by email at 6.29 am on 30 March 2012 citing Section 9(2)(a)
- Chris Robertson – resigned by email at 7.44 am on 30 March 2012 stating that he concurred
Section 9(2)(a)

Issues

- Constitution requires requires 7 Board members, so 1 short before (due to earlier resignation), now 5 short. Section 9(2)(h)
- Board members are elected by members (OSCAR providers), with a requirement for 2 from the North Island and 2 from the South Island. Perhaps greater risk of not getting the right skills on the Board if the emphasis is on representation rather than skills.

Governance & Management Board

Key concerns raised in Section 9(2)(a) **resignation email (supported by** Section 9(2)(a) **)**

Section 9(2)(ba)(i) Prejudice the supply of similar information.

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Governance & Management

Board

Basic structure in place:

- Board meets regularly (every two months);
- Board provided pack of information (see example in **Appendix A**) – however significant issue with accuracy (e.g. \$120k loan recorded as income instead of liability);
- Minutes kept;
- Appears Board is discussing governance level issues (based on minutes) – e.g. reduction in Ministry funding and response to this was discussed in July 2010 meeting (if not earlier) and subsequent meetings;
- Annual financial statements audited by JSA Chartered Accountants – unqualified audit, although JSA emphasise the uncertainty of the “going concern” assumption;
- In a separate letter the auditors also noted lack of separation of duties as a risk area, but testing did not identify any material issues or concerns.

Governance & Management

Board Member's views

We canvassed the 4 scope areas with various Board Members by telephone. In summary:

2008 Recommendations

- None of the Board Members were present in 2008 so were not aware of the 2008 report or recommendations;

Board and Management

- There are strongly divergent views on the effectiveness of governance (two factions).
- The only new significant negative issue raised that was not canvassed in Section 9(2)(a) email is that issues such as unpaid GST/PAYE were explained away as being “inputting issues” or “errors in the accounts”. We have not verified this.

Expenditure

- There was a reasonably common level of “unease” or “concern” about the level of expenditure, particularly on entertainment (dining, etc).

Financial Position and Solvency

- All the Board Members are aware that OSCAR is in financial difficulty. Some of the Board Members were not aware of the extent of the overdue Inland Revenue debt.

Governance & Management

Conclusions and Key Concerns

Basic governance and management structure in place, but OSCAR has significant issues:

- Deeply insolvent (discussed later).
- Urgently need new Board members, but not clear why someone would accept the appointment with the level of risk attached to this.
- Mr Upton advised there is a plan in place to deal with expenses > revenue (i.e. obtain revenue from other sources) and is confident it will work. We have not tested the reasonableness of this (outside scope) – this needs to be tested before the Ministry places any weight on it. However there is currently no plan to address the current and significant solvency issue (discussed later – but shortfall of \$0.4 to \$0.5 million), apart from hoping the Ministry will assist.
- Staff are leaving – understandable given OSCAR cannot provide certainty of future income.
- Inaccurate and unreliable management accounts.

Expenditure Review

Expenditure Review

Financial Performance

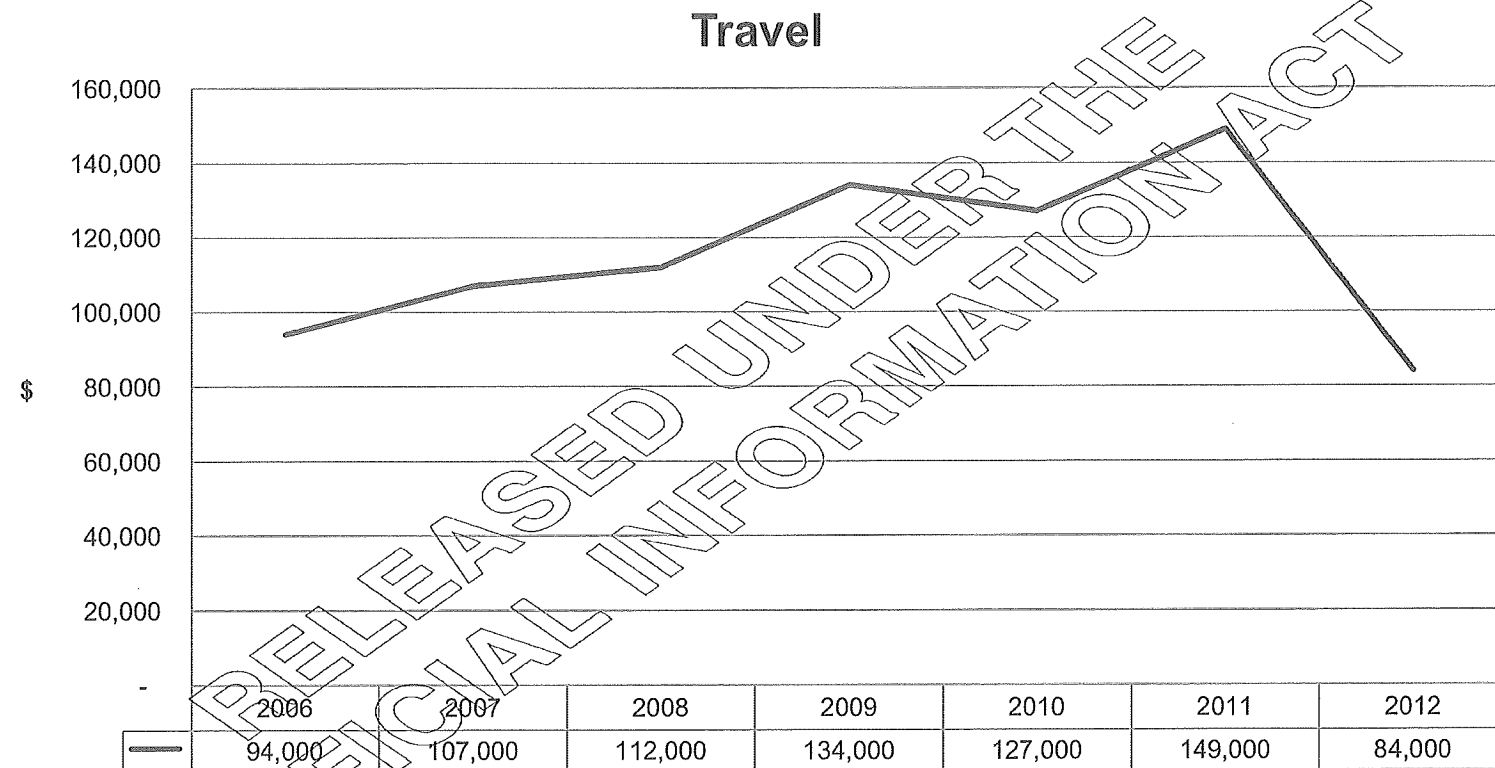
\$'000	2007	2008	2009	2010	2011	2012
INCOME						
MSD Income	1,090	1,149	1,460	1,361	1,411	850
Conference Income	111	0	150	180	113	2
Other Income	109	166	190	148	128	187
TOTAL INCOME	1,310	1,315	1,800	1,689	1,652	1,039
EXPENSES						
Contracts for Services	274	253	157	79	78	22
Conference Expenses	111	10	167	182	138	33
Rent & Utility Expenses	81	89	92	103	101	110
Special Events Related Costs	94	147	133	94	36	48
Staff Training & Welfare	41	39	51	50	59	28
Telephone, Tolls & Internet	30	39	39	53	46	43
Travelling Expenses - National	107	112	134	127	149	84
Wages & Salaries	464	513	759	849	787	846
Other Expenses	103	108	144	196	217	146
TOTAL EXPENSES	1,305	1,310	1,676	1,733	1,611	1,360
NET SURPLUS/DEFICIT	5	5	124	(44)	41	(321)

Note: 2012 results are year to date (Feb 2012) pro-rated for 12 months. No adjustments made for conference income or expenses (which should largely offset each other) or balance sheet adjustments noted in the Solvency section below. These will increase the deficit reported in the current financial year.

The key observation: 2012 – the expenses are at similar levels to 2011, despite significant reduction in revenue. This has caused a significant loss in 2012.

Expenditure Review

Travel



Expenditure Review

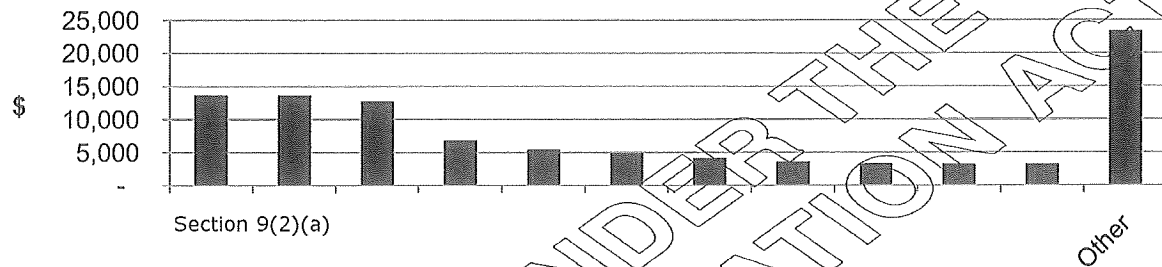
Travel

	2011	YTD 2012	Comments
Airfares	37,000	12,000	Most of the flights are NZ based. Given OSCAR visits providers NZ wide, there will be a high need for flights. There is some travel to Australia – which is discussed in the credit card section below.
Mileage	33,000	8,000	Oscar Advisors cover large geographic areas by vehicle. This cost, particularly in 2012, seems reasonable.
Accommodation	17,000	9,000	Nightly rates of accommodation and locations seem reasonable.
Car Hire/Lease	27,000	15,000	There are 4 leased cars which are based in each location of Oscar advisors. Some vehicles are shared between advisors.
Food & Beverages	16,000	4,000	
Other	19,000	8,000	
Total	149,000	56,000	

Expenditure Review

House of Travel (primary provider of travel)

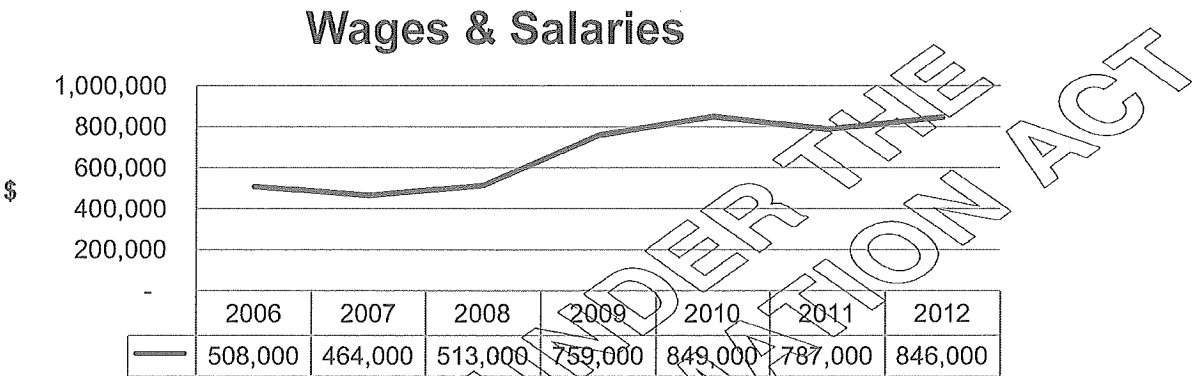
House of Travel Spend



Name	Comments
Section 9(2)(a)	Mostly Auckland/Wellington flights. One trip to Melbourne. One trip for Section 9(2)(a) to Sydney.
Section 9(2)(a)	Napier to Auckland/Wellington travel
Section 9(2)(a)	Hamilton to Auckland travel. Also 4 flights to Sydney for a conference all under her account for Section 9(2)(a),
Section 9(2)(a)	Most of the spending under Section 9(2)(a) name was venue booking for Board meetings/Conferences/AGM's

Expenditure Review

Staff



Salaries > \$50,000 at 30 March 2012		
Name	Role	Salary

Section 9(2)(a)

Expenditure Review

Credit Card

There is one credit card which is issued to Murray Upton. The expenditure on this credit card for the 1 July 2010 to 29 February 2012 is summarised below:

Category	Value	Comments
Travel	\$32,000	Large amounts of this travel relates to payments to Executive Travel Agents and other online bookings. An inspection of the supporting invoices showed that the travel was for a number of staff members, not just Mr Upton.

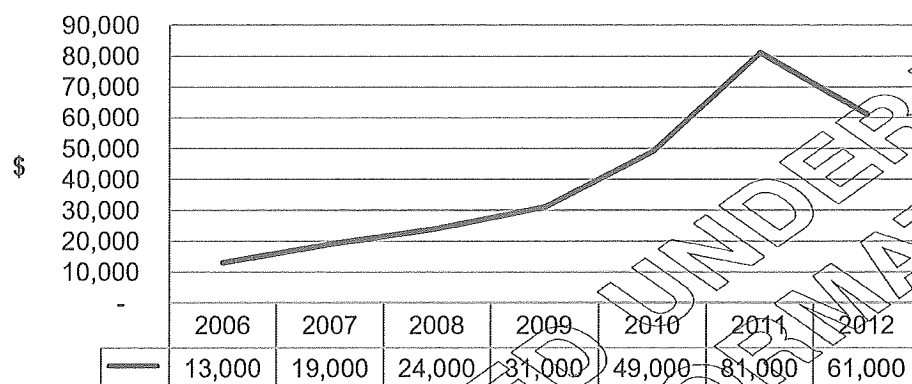
Entertainment	\$19,000	See the detailed timeline in Appendix B for a detailed analysis on the spending within this category. We reviewed the supporting invoices for some of these items. We found that spending falls into two broad categories: invoices for large amounts (\$>200) typically have 10+ people involved. Mr Upton explained the OSCAR team come together for various events, including training held quarterly and as part of this the team goes out for dinner. Many of the staff would need to stay overnight, incurring dinner costs anyway.
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The invoices for the smaller amounts typically have 2 – 4 people. Mr Upton advised he has dinner with Board members and also a strategic adviser, who does not charge for his time. We have not attempted to verify the people involved in the meals, etc.

Expenditure Review

Computers/IT

Computer Expenses



Conclusions

High level of IT spend for an organisation of this size.

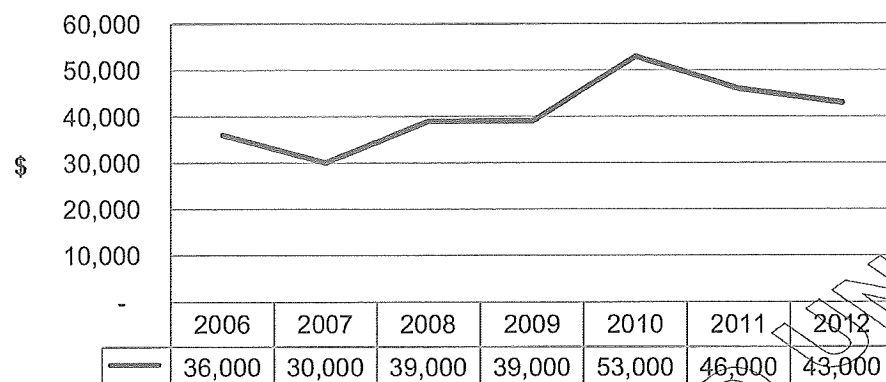
However, one possible explanation is that this increased outsourced expenditure has been offset by reduction in salary cost of an IT specialist, and depreciation in the form of capital investments in servers/computers. Further work would be required to determine this.

Supplier	Monthly Amount	Purpose
Code Blue	\$4,000 - \$8,000	Provides outsourced solution for servers, workstations, support, backups, additional data/storage

Expenditure Review

Telephone

Telephone, Tolls & Internet



Supplier	Approximate Monthly Cost	Purpose
UCS	\$650	Fixed Line Telecom Provider
Vodafone Mobile	\$1,600 - \$2,000	24 Mobile Phones used by staff
Vodafone Fixed Line	\$130	Alternative Fixed Line mainly used to call Vodafone mobiles
Vision Rentals	\$500	Phones lease
Employee Reimbursements	\$400	Home phone & broadband reimbursed for regional advisors
Total	Approx \$3,500	

Conclusions

There are currently more mobile phones being paid for than there are employees and as such these costs are inflated.

Mr Upton explained that OSCAR explored cheaper alternatives but until the contracts expire on these contracts it is cheaper to continue than break them.

Expenditure Review

Other risks

We also considered two other key risks:

1. **Electronic batch payments** – payee bank account number changed from legitimate suppliers' (e.g. Vodafone) to the bank account number of employee or friend/family member. If this occurs – the electronic payments for one supplier will often be linked to two (or more) bank account numbers.

We obtained OSCAR's electronic payment batches for 1 Jul 2010 to 29 Feb 2012 and visually analysed the relationships. The exceptions (e.g. 1 supplier to 2 bank accounts) are listed in **Appendix C**. None of these exceptions are linked to known bank accounts of employees.

2. **Bogus suppliers** – employees or others submit bogus invoices to OSCAR for payment. We often find that bogus suppliers will be linked to employees (e.g. telephone number, bank account or via Companies Office).

We completed background searches using publicly available information for certain OSCAR employees and the Chair. The results are included in **Appendix D**.

Using OSCAR's accounting system we have then identified its suppliers and have gathered "master data" (e.g. telephone number, bank account number, director, shareholders, etc) from an invoice for each supplier that was not known to the review team. This information is visually plotted in **Appendix E** along with the results from Appendix D. This visual map shows no links between key OSCAR staff and the chair and OSCAR suppliers (the reader is not expected to be able to read the detail – rather just to note there are no links between these two groups).

Financial Position and Solvency

OSCAR's Financial Position

Summary

OSCAR's Estimated Financial Position as at 29 February 2012 - \$'000

	Per management accounts	Adjustments	Adjusted
Current assets			
Cash	184	(30)	154
Trade debtors	127	(111)	16
Prepayments	73	(73)	0
Other	17	(7)	10
	<u>401</u>	<u>(221)</u>	<u>180</u>
Current liabilities			
Trade creditors	(24)	-	(24)
GST	(91)	(18)	(109)
PAYE	(100)	(27)	(127)
Sundry	(55)	-	(55)
Leave pay	(59)	-	(59)
Prepaid MSD income	(283)	-	(283)
	<u>(612)</u>	<u>(45)</u>	<u>(657)</u>
Working capital	<u>(211)</u>	<u>(266)</u>	<u>(477)</u>
Fixed assets	18	-	18
Net assets/(liabilities)	<u>(193)</u>	<u>(266)</u>	<u>(459)</u>

OSCAR's Financial Position

Summary

OSCAR is insolvent:

- Liabilities exceed assets by c \$400k to \$500k at 29 Feb 2012 (the \$111k adjustment for trade debtors is for three invoices OSCAR sent the Ministry in early 2009. We have included a copy of the covering letter and invoices in **Appendix F**. If these invoices are payable, this will improve OSCAR's financial position by \$111k).
- PAYE hasn't been paid since July 2011 (except for February 2012 period). Currently \$113k overdue.
- GST hasn't been paid except for offsetting refunds since April 2011. Currently \$109k overdue.
- Informal arrangement now in place with Inland Revenue to pay current PAYE/GST plus \$5k a month. OSCAR unlikely to be able to generate an additional \$60k per annum to honour this agreement – therefore high risk of this informal agreement unwinding and Inland Revenue taking enforcement action.

OSCAR's Financial Position

\$120,000 loan from Section 9(2)(a)

- The loan was advanced by Section 9(2)(a) in two tranches - \$100k on 27 Oct 2011 and \$20k on 20 Dec 2011. The loan was fully repaid on 31 Jan 2012 including \$6k interest (calculated at 22%).
- We are satisfied OSCAR needed short term finance – its bank balance would have been \$107k OD immediately before the Ministry's deposit of \$489k on 26 January 2012, if this funding was not obtained.
- OSCAR has used bank OD in the past to fund cash shortfalls – the balance was \$43k OD on 6 Jul 2011 and \$72k on 8 Dec 2010.
- However OSCAR's bank would not provide a sufficient loan or OD on this occasion (verbal – no documentation). Mr Upton sought approval in writing from Peter Heaslip (Chairman) for OSCAR to borrow funds from Section 9(2)(a) source;
- Mr Upton notes that he has the authority to incur debt for OSCAR, but given Section 9(2)(a) he obtained Mr Heaslip's approval (see **Appendix G**).

Conclusions and Next Steps

Conclusions

The trigger for the review was around OSCAR's management, finances and concerns about OSCAR's plan to address the reduction in funding.

OSCAR has implemented some, but not all of the 2008 recommendations. Importantly, OSCAR has not addressed the weaknesses around electronic payments (only one password holder required) or the CEO's credit card expenditure.

We found that OSCAR was incurring high levels of expenditure at "high-end" restaurants in the period from 1 July 2010 onwards. This expenditure was imprudent in our opinion, particularly given OSCAR's funding cuts and OSCAR's poor financial position. We have not seen any evidence that would enable us to draw a conclusion that the expenditure was fraudulent.

The critical factor now is that OSCAR is insolvent and only has two current Board members. It will fail without significant intervention/change. The Board members face personal risk (legal and reputation) if they decide to continue trading, in current circumstances. Unless OSCAR can urgently address its financial and governance issues it should discontinue trading and move to an orderly wind-down.

Limitations

Limitations

This was a focussed, intensive review over 1½ days onsite. We have not audited or otherwise verified the information provided to us. Instead we relied on experience and judgement. There is an inherent risk material matters may not be identified.

OSCAR has not been provided with this final briefing for review and comment. However we discussed the key findings with OSCAR at the conclusion of the fieldwork using a (very) draft version of this briefing as a prompt.

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