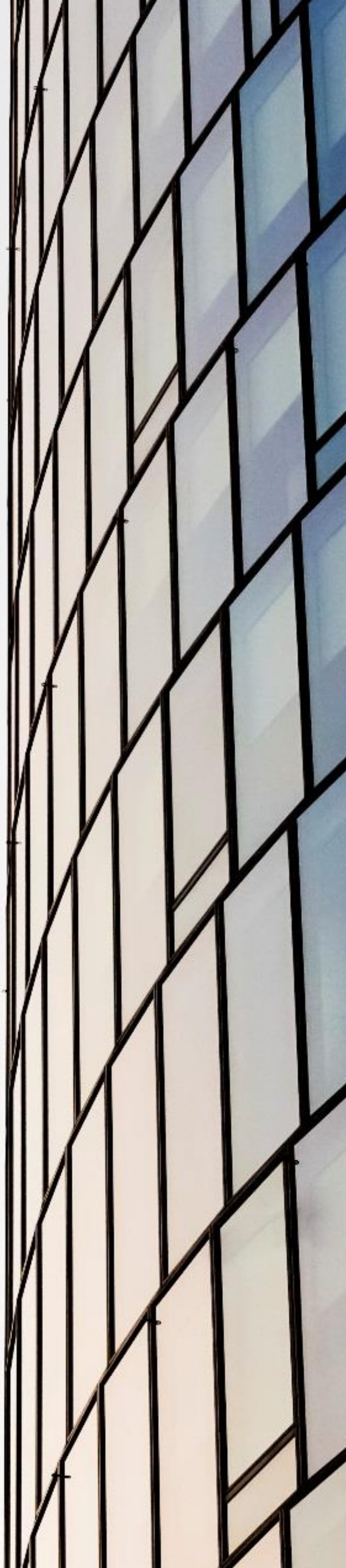
KPMG

Science and Technology Center in Ukraine Management Letter

For the year ended 31 December 2020



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Private and confidential

5 August 2021

Dear Mr. Curtis M. Bjelajac and Mr. Anthony Nichol,

We have audited the financial statements of the Science and Technology Center in Ukraine (hereinafter "STCU") as at and for the year ended 31 December 2020.

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

During the performance of our audit, we noted certain matters that are presented for your consideration. Our comments and recommendations, all of which have been discussed with the appropriate members of management, are intended to improve the internal control structure or result in other operating efficiencies and are noted in the attached appendix. This management letter also includes the responses by management to our recommendations.

We would like to express our appreciation to the management and employees of the STCU for their cooperation during the audit.

We would be pleased to discuss these comments and recommendations with you at any time. This report is intended solely for the information and use of the management.

Yours sincerely,
KPMG Baltics AS

Armine Movsisjana
Partner

Contents

1 Accruals recognition

Observation

During the course of the audit, we have discovered instances when for large procurement contracts, both purchase of equipment or receiving a service that overlaps between two financial periods, neither accruals were recognised in the Statement of Financial Position as of 31 December 2020, nor expenses were recognised in the Statement of Revenues and Expenditure in 2020. For example, we identified that there were no accruals recognised for project 9700 (Facilia agreement) as of 31 December 2020.

Implications

While the STCU implemented an informal process over accrual recognition following auditor's recommendation from prior year audits, there are still gaps in the internal process, which resulted in a misstatement in the Statement of Revenue and Expenditure of the reporting period, as accounting accrual basis was not followed.

Accruals may be understated in the Statement of Financial Position, and accordingly project expenses are understated in the Statement of Revenues and Expenditure.

Recommendation

We recommend the STCU to implement a common documented policy with respect to accruals by establishing procedures for identifying those contracts with suppliers where invoicing period does not correspond to the financial year period. Taking into consideration the specifics of each contracts with suppliers, the STCU should carefully assess amount of accruals to be recognised at each reporting period.

Management response

The invoice from Facilia and a second not mentioned above but referred to in the SOAM on project P753 were excluded from accruals at the year end as the invoices were not received until after the accounts had been closed for December 2020.

As part of the year end schedule a balance has to be struck between closing the accounts for the year end to move on with the process and keeping the accounts open to be able to post invoices that are received late. Unfortunately, these two invoices were received after that date.

Whilst for IFRS purposes these accruals should have been included as project income equals project expenditure the effect on the financial statements is minimal.

2 Prepayment recognition

Observation

Upon testing the project expenses for a sample of projects, we identified certain prepayments on works that were not finished till the end of the financial year. These prepayments were made during 2020 and expensed in the Statement of Revenue and Expenditure in 2020 with assumption of agreements being executed within the financial year. While total amount of prepayment to be kept on the balance sheet as at 31 December 2020 for sample of projects reviewed is not material in aggregate, this is a clear indication of the weakness in internal control over prepayment recognition. For example, there were prepayments for projects P711A and 9700 (agreement with ZVO).

Implications

While the STCU implemented an informal process over prepayment recognition following auditor's recommendation from prior year audits, there are still gaps in the internal process, which may result in a misstatement in the Statement of Revenue and Expenditure, as accounting accrual basis is not followed.

Prepayments may be understated in the Statement of Financial Position, and accordingly project expenses may be overstated in the Statement of Revenues and Expenditure.

Recommendation

We suggest to the STCU to revise introduced control over prepayment recognition e.g. closely follow terms and conditions of the contracts with suppliers to identify the moment when the prepayment can be contractually offset against the subsequent received invoices.

Management response

Management considers that the control over prepayment recognition is adequate and no further change is required.

The contract with ZVO (Project 9700) was signed on 15 May 2020 and the contract with IT Solutions on 6 August 2020 and both contracts were to be implemented in 120 days. Therefore, both contracts were expected to be completed before the year end and the advance payments were not treated as prepayments*.

ZVO invoiced STCU on 24 November for the work completed to that date and deducted the full amount of the advance payment. As to why the contractor chose to deduct the full amount of the advance payment at this stage is unknown, STCU did not question this as it reduced our financial risk.

Therefore, at the year end there was no prepayment remaining on this contract and the financial statements presentation is correct. The contract with IT solutions was 97% complete and invoiced by 17 December 2020, strictly speaking there should have been a prepayment remaining of $ 2,428.37, which management consider to be not material.

* - For the purposes of reporting on individual projects to the funding parties and partners the periodisation of expenses by financial years is irrelevant hence if an advance is not expected to cover the year end it is not treated as a prepayment, only where an advance payment is to straddle the year end will it be treated as a prepayment to ensure we comply with IFRS in the annual financial statements. Should a contract implementation be delayed and consequently straddle the year end STCU would adjust for the prepayment at the year end. In checking for prepayments at the year end the IT solutions contract was overlooked.

3 Access rights to bank accounts and payment authorisation

Observation

Upon performing audit procedures, we obtained a letter from Access Bank which states that ex-chief accountant, Maryna Dziubynska, has access rights to the online banking system and has first signatory rights. Additionally, during internal process evaluation we discovered that there is lack of four-eye principles for payment initiation and authorisation through Bank of Georgia's online banking system. During interview with Larissa Maiboroda (acting chief accountant) and Anastasia Kulenko (deputy of chief financial officer) we discovered that both ladies can initiate and authorise payments solely using the same calculator.

Implications

Lack of established and strong process relating to outgoing payments review might lead to fraudulent activities exercised by the staff.

Recommendation

We suggest to the STCU to amend access rights to Access Bank's online banking system. Additionally, we suggest to revise the process for payment initiate and authorisation through Bank of Georgia's online banking system.

Management response

Whilst Maryna Dzubynska is mandated as a signatory at Access Bank she does not have access rights to the online banking sysytem as these were established two years after Ms Dzubynska left STCU and are all in the names of current STCU staff.

The procedures for changing signatories at Access Bank are very involved and require the presence in Azerbaijan of all the signatories. Management are aware of this issue and the need to formalise these arrangments which will be done when it is possible for all three signatories to be in Azerbaijan at the same time. In the meantime, as the bank requires dual signatures for any transaction, either online or in writing, management does not consider there to be a significant risk attached to this until we are able to update the records.

The use of one signatory is determined by Bank of Georgia's online banking system and it is unlikely that STCU would be able to change this. Management are satisfied that together with other controls, which include the bank accounts in Georgia being operated on an imprest basis, there is sufficient authorisation control over the bank accounts. Management will review the signatory policy for Bank of Georgia and discuss with the bank the possibilty of changing the number of signatories on transactions.

4 Credit risk disclosure – ageing of accounts receivable

Observation

Upon performing audit procedures, we obtained a subledger for accounts receivable that among other information about balances included term structure of account receivable and ageing for short term receivables. Due dates indicated in Navision are outdated and do not provide reasonable basis for conclusion over ageing structure of short term account receivables. Therefore, subledger contained manual division, while we have identified that the ageing is not updated in accordance with changes in project agreements such as amendments and prolongation.

Implications

The ageing is disclosed within credit risk disclosure as part of financial risks note in the financial statements. Therefore, credit risk disclosure might not be accurate. This also might result in inability to identify overdue amounts that require the STCU's attention.

Recommendation

We suggest to the STCU to enhance the control over term structure and ageing of account receivables e.g. closely follow terms and conditions of the agreements with partners to identify the moment when the receivable changes it's term due to amendments signed or becomes overdue.

Management response

Whilst the ageing of accounts receivable for the financial statements is primarily based on the due date for payment of invoices which are raised when a project is signed and entered in Naivision the calculations in the spreadsheet are adjusted for any changes in due dates caused by the prolongation of projects (recently a number of projects have had to be prolonged). The finance staff are aware of the status of each project.

Management notes that the examples that were raised as being potentially incorrect were correctly aged and believe that the financial statement presentation is correct.

The procedure to change the due dates in Naivision is such that it can cause issues with other reports and therefore with the small number of projects at STCU currently and the ability to use the spreadsheet to ensure the correct ageing of accounts receivable management sees no advantage in making the change recommended.

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