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19th May 2020

Ghasri Local Council
6, Triq Dun Karm Caruana,
Ghasri GSR 1021,
Gozo

Dear Mayor,

RE: MANAGEMENT REPORT – FOR THE YEAR ENDED 31 DECEMBER 2019

We have completed our audit of the financial statements of the Ghasri Local Council for the year ended 31 December 2019. The purpose of this report is to summarise our principal findings arising from this work.

Our audit was primarily based on verifying balances in the financial statements to ensure that they are free from material error and comply with relevant legislation. Consequently, the matters raised in this report cannot be regarded as a comprehensive statement of all weaknesses that exist or all improvements that might be made. Our aim is to offer guidance to the Local Council such that it would be in a better position to improve its internal controls, enhance its book-keeping function and consolidate its overall governance.

Our engagement obliges us to distribute copies of this report to: (a) your Council; (b) the National Audit Office; and (c) the Local Councils Department. Consequently, this report may not be distributed, used or quoted in part or in full, except for the scope it is prepared, without our prior written consent.

This report has been prepared on the basis of the limitations set out in the Responsibility Statement as presented on page 10 of this report.

During the course of our audit for the year ended 31 December, 2019, we examined the principal documents, systems and controls used by the Council, to help it ensure, as far as possible, the accuracy of these documents and to assess how much can one rely on these documents to safeguard the assets of the Council. We also examined whether or not your Council abided by the procedures as they are provided for in the Local Councils Act, 1993, the Financial Procedures and various Legal Notices issued to your Council.

The objective of this letter is to bring to your attention those divergences in the system that were noticed during our audit work and suggest ways of how these can be remedied.

We would like to take this opportunity to thank the Executive Secretary for his assistance during the course of our audit.

Yours faithfully



Conrad Borg (Partner)
for and on behalf of
RSM Malta

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Ghasri Local Council

Management Report for the year ended 31 December 2019

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1.0 FOLLOW-UP TO LAST YEAR'S MANAGEMENT REPORT

1.1 Property Plant and Equipment

The fixed assets register was not updated to include enough details to be able to easily identify the items of electronic equipment during the physical inspection and hence it was difficult to determine if they were still in use. During 2019, it was noted that there were no updates to the fixed assets register in this respect.

When checking the depreciation charge for the year, we noticed that the depreciation for the year was not properly calculated following the adoption of the new accounting policy for depreciation whereby the straight-line method is now being adopted. This issue has been resolved in 2019 despite it is being calculated on a yearly basis rather than on a monthly basis.

While reviewing the minutes of the Council's meetings in the prior year, it was noted that during meeting No.63 held on 15 February 2018, certain items of property, plant and equipment were approved for disposal but they were not written off from the accounts. These disposals were reflected in the current year.

It was highlighted that the buildings with a carrying value of €106,014 were being insured for €70,000, hence being under insured. The insurance coverage was properly updated during the year under review.

1.2 Stocks

In the prior year, we noticed that cash movements related to sub-post office services were not being recorded in the accounts per transaction undertaken and no records of the movements were being kept on a manual ledger either, as is done for the petty cash. We also noted that the Local Council was recognising the commission earned from the sale of stamps and cards on the date of purchase of the stocks rather than upon the sale of such items. These issues were still present in 2019.

1.3 Receivables

Accrued income and prepayments were being accounted for in the wrong nominal account. The same issue was encountered in 2019.

It was noted that the Council was passing the prepayment journal entries based on the prior years, without doing the necessary re-assessment. In fact, errors were found in the prepaid amounts.

A grant of €5,000 which was received after year-end for an event held during 2018, was not accrued for. This grant was not reversed by the Council in the current year despite it was received.

Last year we noted some discrepancies between the customers' statements and the receivable balances as per books. No such issues were noted in the current year.

1.4 Payables

From the architect's letter received, it transpired that works carried out by various contractors on resurfacing of roads and restoration of a niche, for which invoices have not yet been issued as at the end of the year, as either the works were not yet certified or the works were still in progress, have not been accrued for. Similar issues were encountered during the current year.

1.5 Income

During our testing on income, we noted that the Local Council is netting off the income received from Wasteserv for organic waste collection against the cost of waste collection rather than showing them separately. The same issue has been noted in the current year.

When analysing the income accounts, we came across a government grant relating to a project of a capital nature that was not yet carried out either. A similar situation has been noted this year.

1.6 Personal emoluments

A recurring problem is the lack of contracts between the Local Council and its employees in line with their present working conditions. The Council still does not have contracts for its employees.

Some reclassification adjustments had to be passed as some payroll costs were not accounted for in the correct nominal account. We had to pass similar adjustments in 2019.

Variances were noted between the amounts declared in the FS5s and the amounts declared in the FS7. Similar instances were encountered this year.

1.7 Expenditure and tenders

Last year, we pointed out that the expenditure in certain categories exceeded the budget. A similar situation was encountered this year.

The Council used one form for the purchase request and the purchase order which is not in line with the prescribed regulations. This was still being done during 2019.

One case was encountered where the Council did not issue a call for quotations despite the related expenditure exceeded the thresholds for direct orders. A similar case was noted in 2019.

When browsing through the administrative expenses' accounts, we noted that there was included therein a control account used for the Ghasri Sub Post office services. In the Sage accounting system, this account was set as an expense account and as a result thereof, it did not carry forward any balances from one year to the other. The same issue has been noted in the current year.

1.8 Liquidity

As at 31 December 2018, the current liabilities exceeded the current assets of the Local Council. As at 31 December 2019, the current liabilities were less than the current assets.

2.0 PROPERTY, PLANT & EQUIPMENT

- 2.1 During a physical inspection carried out on a sample of assets found in the fixed assets register, we found that some electronic equipment could not be identified due to the lack of details found in the fixed assets register. Therefore, we could not verify whether the assets were still in use. In prior years, this weakness was already communicated to the Local Council, but no action has been taken.
- 2.2 We emphasise the importance that the Local Council maintains enough details in the fixed assets register to easily identify each item of property, plant and equipment listed therein. The Local Council should also carry out physical inspections regularly on a sample of items of property, plant and equipment, to check whether the assets are still in existence and in good condition for use. If any assets are found missing or not in good condition for use, the Council should follow the regulatory procedures to ensure that such assets are written off from the accounts and the fixed assets register.
- 2.3 The Local Council should be depreciating its assets on a monthly basis in line with the accounting policies applicable to Local Councils rather than on a yearly basis as is currently being done. The fixed asset register only includes the year of purchase rather than the exact date of purchase, and as such, it is not possible to calculate the depreciation charge on a monthly basis. We determined that the depreciation charge for the current year is not materially overstated. We urge the Council that going forward the fixed asset register should include the exact date of purchase, and the depreciation charge is to be calculated on a monthly basis in line with the accounting policy.
- 2.4 It was noted that the Local Council had capitalised costs amounting €88,753 under the category 'Construction' relating to projects which were not finalised by the end of the year. These costs had to be reclassified to under the category 'Assets under construction'. An adjustment of €2,160 was passed to reverse the depreciation calculated on these capitalised assets. Furthermore, government grants amounting to €67,149, which had been set off against the capitalised assets were reversed against deferred income.
- 2.5 It is important that until an asset is finished and is available for use, it is classified under 'Assets under construction' and no depreciation is calculated thereon and no government grants are to be capitalised in respect to that asset.

3.0 STOCKS

- 3.1 During our audit, we noticed that the Local Council is not conducting any cash counts of the cash held for the sub-post office activities. Cash movements related to sub-post office services are not being recorded in the accounts per transaction undertaken and no records of the movements are being kept on a manual ledger either, similar to what is done for the petty cash. As a result, we could not obtain confirmation of the cash held in hand as at the end of the year from this activity.
- 3.2 We urge the Local Council to start maintaining a manual ledger of all the transactions undertaken for the sub-post office activity, which ledger can then be used to update the accounts. Regular cash counts should also be carried out and the result reconciled with the ledger and the accounting records. Furthermore, the cash received should first be accounted for in a separate cash account in the books and then, make a transfer to the bank account only when the actual deposit is made.

- 3.3 We also noted that the Local Council recognises the commission earned from the sale of stamps and cards on the date of purchase of the stocks rather than upon the sale of such items.
- 3.4 The Council should take remedial action to ensure that it is compliant with IFRS 15 – Revenue from Contracts with Customers despite the commission might not be considered as material.

4.0 RECEIVABLES

- 4.1 It was noted that the prepayments and accrued income were being accounted for in nominal account 4150 – prepaid income. This is incorrect as accrued income should be allocated to nominal account 0201 – accrued income while prepayments should be allocated to nominal account 0250 - prepayments. The same issue was pointed out in the prior year.
- 4.2 It is important that care is taken when posting journal entries to ensure that the correct entries are passed in the correct nominal accounts. This would ensure proper presentation of figures in the financial statements.
- 4.3 The Council did not reverse opening accrued income of €5,760 despite it was received and opening prepayments of €466. An audit adjustment was passed to adjust these errors.
- 4.4 The Local Council should have a detailed breakdown of the opening accrued income and prepayments so that it would be in a position to reverse all prepayments during the year, as well as be able to follow up the accrued income and reverse such when it is received.

5.0 BANK AND CASH

- 5.1 When checking the bank reconciliations, it was noted that cheques amounting to €404 became stale by the end of the year and have not been reversed.
- 5.2 At the end of each financial year, the Local Council should go through the list of un-presented cheques and any cheques that would have become stale by that date should be investigated. It could be that another cheque was issued to replace a particular cheque and the old cheque would have not been reversed.

6.0 PAYABLES

- 6.1 From the architect's letter that we received as part of our audit procedures, it transpired that works carried out by various contractors on resurfacing of roads for which invoices have not yet been issued as at the end of the year, as either the works were not yet certified or the works were still in progress, have not been accrued for. The total of such works was estimated by the architect at €247,525, part of which were already invoiced during the year, leaving a balance of €158,732 that has not been accrued for. An audit adjustment was passed to reflect these accruals not accounted for.
- 6.2 Invoices amounting to €117,682 were received in 2020 relating to a capital project which was certified as completed in 2019. These costs were not accrued for as at the end of the year. An adjustment was passed to reflect such expenditure. As a result, deferred income received to partially cover the afore-mentioned expenditure amounting to €106,249 was reclassified from under deferred income to under property, plant and equipment. Depreciation on the difference, amounting to €1,143 was accounted for as well.

- 6.3 The Local Council should be fully aware of the projects ongoing as at the end of the year and should accrue for all the costs incurred till the end of the year for which it would not have been invoiced, in accordance with the accruals concept. The accruals for such projects should be based on estimates that are to be worked out by the architect.

7.0 INCOME

- 7.1 Within the other government income, we found an amount of Euro 5,749. When we obtained the necessary documentation and agreements, it transpired that this amount was received from Water Services Corporation to cover costs relating to a project of a capital nature. Hence these funds were transferred to deferred income through an audit adjustment.
- 7.2 Before accounting for any funds received, it is important that one checks the supporting documentation available and treat that income accordingly. If the income relates to future projects, then it should be deferred to be matched against the related costs that would be incurred in the future.
- 7.3 During our testing on income, we noted that the Local Council is netting off the income received from Wasteserv for organic waste collection against the cost of waste collection rather than showing them separately, a similar approach to that adopted in the previous year. We noticed also that the income for 6 months of the year was then accounted for under the income, meaning not being consistent in the approach. Similarly, we noticed that income for library services amounting to €651 was posted in the library expenses account. A reclassification adjustment was passed with respect to this error.
- 7.4 Kindly note that IFRS 1 – Presentation of Financial statements, specifically states that an entity shall not offset assets and liabilities or income and expenses unless required or permitted by an IFRS. Hence, the cost and income relating to organic waste collection should be shown separately in the financial statements.
- 7.5 Within the cultural activities income account which is classified under general income in the financial statements, there was an amount of €6,800 received from the central government. A reclassification adjustment was passed to ensure it is properly presented.
- 7.6 Care should be taken when accounting for an income transaction to ensure it is reflected in the correct nominal account and consequently ensure that income is properly presented in the financial statements.

8.0 PERSONAL EMOLUMENTS

- 8.1 The employees still do not have a signed contract of employment with the Local Council in line with their present conditions of work, except for the new executive secretary.
- 8.2 As per our previous years' recommendation, a contract should be drawn up for all the Council employees setting out the current conditions of employment. The employer is legally bound to have a signed contract of employment in place, with each employee.
- 8.3 During our audit, we have passed a reclassification adjustment in relation to the wages and salaries costs to ensure that they are reflected in the correct payroll costs nominal accounts.
- 8.4 To ensure correct and consistent disclosures of personal emolument costs in the notes to the financial statements, it is important that the correct nominal accounts are used when posting the payroll costs related transactions.

- 8.5 A variance of €2,667 was found between the gross emoluments reported in the FS7 and the FS5s. The variance mainly resulted from the financial incentives given to employees under the CIES workers scheme, which were not included in the FS5s but were properly reported in the FS7 and in the FS3s.
- 8.6 It is important that when preparing the FSS forms, all the figures reported therein tally. Reconciliations are to be carried out between the FS7, FS5s and FS3s.
- 8.7 During our audit, we found a variance of €32 when we tried to reconcile the payroll costs in the accounts with the figures shown in the FS7.
- 8.8 The Local Council should carry out such reconciliation on an annual basis and any variances found should be investigated. The auditor should be presented with such a reconciliation that should include an explanation of the variance.
- 8.9 When checking the calculation of the performance bonuses of the executive secretary that was accrued for, we noticed that there was an under accrual of €47.
- 8.10 Care should be taken when calculating the performance bonuses to ensure that the appropriate basis is used for their calculation.

9.0 EXPENDITURE AND TENDERS

- 9.1 It was noted that the Council has exceeded the budgeted expenditure for several categories, namely:
- 9.1.1 Materials and supplies (Category 2200) by €2,518
 - 9.1.2 Office services (Category 2600) by €158
 - 9.1.3 Transport (Category 2700) by €359
 - 9.1.4 Contractual services (Category 3000) by €1,258
- 9.2 The Financial Procedures applicable for Local Councils require Councils to draw up twelve (12) months budgets, three (3) years business plans, quarterly reports and eventually yearly administrative reports at the end of the year. The Council is also allowed to revise budgets in line with actual requirements, and there are enough reporting tools to note which areas in the budget need revising.
- 9.3 We recommend that the Council makes use of the reporting tools in hand to take corrective measures in the budget every quarter such that by the end of the accounting period/year such discrepancies would not materialise.
- 9.4 While testing expenditure, we noted that the Council uses one form for purchase requests which is then used as a purchase order instead of using a separate form in line with the prescribed regulations.
- 9.5 We recommend that the Council should adhere to the procedures applicable to Local Councils. Moreover, the proper use of purchase orders would also help the Council to identify all liabilities at year-end.
- 9.6 Following Directive 03/2017 issued by the Department for Local Government to Local Councils on the change in the public procurement regulations, we noticed an instance from the samples tested, where the Council did not abide with the new regulations where expenditure up to the value of €5,000 was concerned. We came across an instance where the Local Council was invoiced a total of €7,960 during the year for 2 separate projects and no quotations were obtained.

- 9.7 We understand that the bureaucratic requirements of the public procurement regulations may be cumbersome. However, we highly suggest that the Council adopts these regulations to full effect.
- 9.8 When browsing through the administrative expenses' accounts, we noted that there was included therein a control account used for the Ghasri sub-post office services. In the Sage accounting system, this account was set as an expense account and as a result thereof, it did not carry forward any balances from one year to the other. We also noticed that this control account is showing an amount receivable when this account could only have amounts that are payable to Maltapost representing bills settled at the Local Council. We passed an audit adjustment to reclassify this account to under other receivables rather than leaving it under the expenses.
- 9.9 The Local Council should ensure that the setting of this account is changed in the Sage accounting system and should also investigate what the balance as at the end of the year represents. The balance in this account should be reconciled with the amounts that are payable to Maltapost.

Responsibility Statement

While our report includes suggestions for improving accounting procedures, internal controls and other aspects of the Local Council arising out of our audit, we emphasise that our consideration of the Local Council's system of internal financial control was conducted solely for the purpose of our audit having regard to our responsibilities under International Standards on Auditing.

We make these suggestions in the context of our audit, but they do not in any way modify our audit opinion, which relates to the financial statements as a whole. Equally, we would need to perform a more extensive study if you wanted us to make a comprehensive review for weaknesses in existing systems and present detailed recommendations to improve them.