

The Mayor
Hamrun Local Council
Duke of Edinburgh Street
Hamrun HMR 2063
Malta

13th August 2020

Dear Sir,

FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2019

During our audit for the year ended 31 December 2019, we have reviewed the accounting systems and procedures operated by the Council. We have also reviewed the operations of the Council and how they conform to the Local Councils Act, 1993, the Financial Regulations issued in terms of this Act, and the supplementary Financial Procedures. We set out in this report the more important points that arose as a result of our review.

1. Previous Management Letter

1.1 Salaries reconciliation

Similar to the previous year, another difference was noted between the salaries in the accounts and gross wages as per FS7 submitted to the Inland Revenue Department (refer to note 2.1).

Contracts of employment for employees on indefinite period have also not yet been updated (refer to note 2.1).

1.2 Bank reconciliations

We are pleased to note that bank reconciliations for all bank accounts were being performed on a monthly basis.

1.3 Expected credit loss

Similar to previous year, the Council did not calculate and account for the 'expected credit loss' for the impairment of financial assets as per IFRS 9. (refer to note 2.3).

1.4 Fixed asset register

We are pleased to note that no discrepancies were found between the calculation of depreciation on fixed assets as per accounts and the depreciation as per audit calculations.

1.5 Depreciation of Council premises and car park

We also noted that, as in previous year the Council has depreciated the 'Council premises and car park' using the straight-line method at a rate of 1% instead of over its 30-year lease term (refer to note 2.4).

1.6 Amount receivable from Water Services Corporation (WSC)

The overdue balance of €11,326 due from Water Services Corporation (WSC) has not yet been settled (refer to note 2.5).

1.7 Accrued income

Similar to the previous year, the tipping fees were not accounted for properly as at year-end (refer to note 2.6).

1.8 Trade payables

Similar to the previous year, we noted that the Local Council did not obtain creditors' statements from all its suppliers. Thus, reconciliations were not being properly performed (refer to note 2.7).

In addition, the Local Council still had debit balances in the creditors' list (refer to note 2.7).

1.9 Long outstanding trade payables

It was noted that the Local Council still has balances which have been long due for more than one year (refer to note 2.8).

1.10 Accruals

It was noted that the accrual of the Executive Secretary's performance bonus was not accounted for properly (refer to note 2.9).

1.11 Income

We are pleased to note that when testing the Local Council's financial allocation received from Central Government vis-à-vis the expenditure incurred during the year, the Local Council managed to obtain a positive result as required by Section 4c of the Local Council (Financial) Regulations, 1993.

On the other hand, similar to the previous year, some discrepancies in income were found (refer to note 2.10).

1.12 Rent payable

Similar to the previous year, a discrepancy was found in the rent payable as at year-end (refer to note 2.11).

1.13 Procurement of expenses

Similar to the previous year, we noted that the Local Council has incurred expenses for which no proper procurement procedures were carried out (refer to note 2.13).

1.14 Budgeted figures

Similar to the previous year, there were material discrepancies between budgeted and actual figures (refer to note 2.14).

2. Management letter points for the year

2.1 Salaries reconciliation

While testing the salaries for the year, a difference amounting to € 406 was noted between the salaries in the accounts and gross wages as per FSS forms submitted to the Inland Revenue Department. Such amount has been included in the list of unadjusted errors (refer to 2.16).

	€
Gross Wage as per FS7/FS5s	128,577
1/2 the total social security as per FS7/FS5s	7,677
Total as per FS7/FS5s	<u>136,254</u>
Wages and salaries as per accounts	115,222
Mayor's remuneration as per accounts	11,058
NI as per accounts	<u>7,675</u>
As per accounts	133,955
Add opening accrued performance bonus	2,498
Less closing accrued performance bonus	(532)
Less CIES employer's NI	<u>(73)</u>
	<u>135,848</u>
Difference	<u>406</u>

We recommend that a reconciliation is performed at the end of the year before the FS7 is submitted to the Inland Revenue Department. Failure to submit correct forms could result in the Council incurring fines in case of an inspection by tax authorities.

When calculating the allowances payable to the Mayor, an understatement of €400 was noted with respect to the updates in allowances payable as per Circular 14/2019, whereby the yearly allowance has increased from €1,600 per annum to €2,400 per annum. The immaterial difference has been included in the list of unadjusted errors (refer to 2.16).

Another discrepancy of €411 was also noted in the accrual for the performance bonus payable to the executive secretary, which should amount to 10% of the basic pay. Such difference has been included in the list of unadjusted errors (refer to 2.16).

A reclassification (**RECL A/2019**) was also proposed to properly disclose the emoluments paid in relation to the executive secretary salaries and the councillors' allowances (refer to note 2.17).

Similar to the previous year, contracts of employment have not been updated for an indefinite period. We reiterate our recommendation that the Local Council performs an indefinite contract for each employee that has been in employment for more than four years.

2.2 Petty cash

When testing petty cash payments we have noted that the Local Council has made cash purchases which exceed the €50 limit.

We recommend that the Local Council ensures that the proper procurement procedures are abided with at all times.

2.3 Expected credit loss

The Council did not calculate and account for this 'expected credit loss'. The receivable balances of the Council are mainly composed of balances with Government related entities. Given the low risk associated with such entities the default risk is considered to be insignificant and will not result into a material amount. Since the potential effect is not material, the audit report is not qualified in this respect (refer to note 2.16).

2.4 Depreciation of Council premises and car park

The Council has been depreciating the 'Council premises and car park' using the applicable depreciation rates on buildings (reducing balance method at a rate of 1% per annum by financial year ended 31 December 2017 and straight-line method at a rate of 1% per annum as from financial year ending 2018) instead of over its 30-year lease term. This resulted in a variance for the year under review of €38,727 for which we did not propose an audit adjustment, since the Council intends to renew the lease in perpetuity.

When comparing the effect of the method used in depreciating the cost of the Car Park on the accumulated depreciation as at year-end, it was noted that should the Council have based the depreciation on the 30-year lease term, the accumulated depreciation as at 31 December 2018 would have been €536,585 higher than the balance shown in the financial statements.

We reiterate our recommendation to discuss the issue with the appropriate Government authority, to come to an agreement so that the intention of the Council to renew the lease in perpetuity can be made possible and implemented.

2.5 Amount receivable from Water Services Corporation (WSC)

The Council is still carrying an amount of €10,904 receivable from WSC which has been outstanding for a number of years.

We reiterate our recommendation to investigate and discuss this balance with WSC and if it is decided that it is not recoverable, it should be written off after the Council's approval is obtained. After further enquiry with the Executive Secretary with regard to the recoverability of such balance, it was advised that this should not be written off at this stage given that communications between the Council and the debtor are taking place with the intention to obtain confirmation on the recoverability of the balance due.

2.6 Accrued income

While testing the accrued income for the year, it was noted that the balance receivable with respect to shortages of tipping fees in relation to WasteServ was overstated by €1,423. Such difference has been included in the list of unadjusted errors (refer to 2.16).

In addition, it was also noted that income receivable of €18,744, with respect to the share of profits of the car park for 2019 was not accrued for, whereas an additional discrepancy of €5,244 representing an understatement of the share of profits accruing for 2018 was also noted. Given the materiality of the balances, an audit adjustment (**AA 03/19**) was proposed and approved by the Local Council (refer to 2.15). The amount of €13,290 representing the share of profits for 2018 was reclassified from accrued income to Other Receivables.

We recommend the Local Council to obtain the actual amounts of accrued tipping fees from WasteServ and car park share of profits and update the accrued income before the financial statements are approved by the Local Council.

2.7 Trade payables

While performing our testing on trade payables, we selected two suppliers for testing and found that no reconciliations were available. We enquired whether trade payables reconciliations are performed at any other time, and we were informed that no reconciliations are performed:

Supplier	Year-end balance
Saviour Mifsud	€35,443
J & K Contractors	€64

With respect to the balance with Saviour Mifsud, it was noted that the Local Council did not account for invoices amounting to €15,825. An audit adjustment (**AA 06/19**) was proposed and approved by the Local Council (refer to 2.15).

The extrapolated error value arising from the testing of trade payables resulted into an overstatement in trade payables amounting to €100. Given that the difference is not material it has been included with the list of unadjusted errors (refer to note 2.16).

We recommend that the creditors reconciliations are performed to determine if there was any omission of invoices before the approval of the financial statements. Creditor reconciliations are an essential element of a good internal control system. They can assist in enhancing the internal control system of the Council while also ensuring that the supplier balances reflected in the accounts are accurate.

We have also noted that the debit balances in creditors' list re the previous year were not properly accounted for. Thus an audit adjustment (**AA 04/19**) was proposed and approved by the Local Council (refer to note 2.15). A reclassification (**RECL D/19**) was also passed with respect to the classification of debit balances in creditors' list for the year (refer to note 2.17).

We recommend that the Council follows the procurement regulations and pay suppliers only after the invoice is issued.

2.8 Long outstanding trade payables

While reviewing the aged list of trade payables, it was noted that a number of balances which have been outstanding for more than one year until 2018, have been written off during the year, except for two balances. These are:

Creditor	2019	2018
	€	€
Standard Publications Limited	-	52.86
Venture Trading Business Solutions	-	99.02
C. Gerada	-	100.00
Historical Re-Enactment Group	-	708.00
Kumitat Kongunt Centrali	-	1,465.40
Schembri Infrastructures Limited	-	1,567.56
Asfaltar Limited	2,329.37	2,329.37
Burmarrad Commercials	-	250.00
Audio Visual Centre	-	41.99
Enemalta Corporation	-	332.38
Guard & Warden Services	-	102.60
Grupp Armar San Gejtanu	-	154.60
George Mifsud	-	180.00
1st Hamrun Scout Scout	-	250.00
Med Developers Designers	165.67	165.67
Smart Office Supplier	-	41.14

We recommend that the Council investigates these amounts, and if they are no longer due, writes them off after careful consideration and approval by the Council members.

2.9 Accruals

It was noted that the accrual for the executive secretary's bonus was understated by €411, as already noted in note 2.1 above. Such difference has been included in the list of unadjusted errors (refer to 2.16).

Bank loan interest not accrued for as at year-end amounted to €760. Given that the amount is not material, such difference has been included in the list of unadjusted errors (refer to 2.16).

It was also noted that accruals as at year end were overstated by €5,163 with respect to cleaning and maintenance. An audit adjustment (**AA 05/19**) was proposed and approved by the Local Council (refer to note 2.15).

We recommend that the necessary accruals are accounted for before the approval of the financial statements by the Local Council.

2.10 Income

When testing the Local Council's financial allocation received from Central Government vis-à-vis the expenditure incurred during the year, we noted that the Local Council did not manage to obtain a positive result as required by Section 4c of the Local Council (Financial) Regulations, 1993. The Local Council is bound by section 4(1)(c) of the Local Councils (Financial) Regulations, 1993 to maintain a positive balance in terms of section 55 of the Local Councils Act.

When testing income arising from rent receivable from the Local Council's car park it was noted that the share of profit receivable for 2018 was understated by €5,244 (refer to note 2.6). No prior year adjustment was proposed in this respect given that the amount involved was not material. Similarly, the share of profits for 2019 were completely omitted from the Local Council's accounts. As stated in note 2.6 above, such amount was adjusted for through an audit adjustment.

When testing income with respect to the CIES scheme, it was noted that the amount included in the accounts was overstated by €10,150. This represents income in relation to 2020 which was received by the Local Council in advance. An audit adjustment (**AA 02/19**) was proposed and approved by the Local Council (refer to note 2.15).

We have also proposed and passed a reclassification (**RECL B/19**) with respect to income on Special Initiatives amounting to €10,000 from Funds received from Central Government to General income (refer to note 2.17).

Another reclassification was proposed and passed (**RECL C/19**) with respect to reimbursement of costs in relation to a weekend break organised by the Local Council amounting to €6,651 which was accounted for as Other income rather than netted off in the social events expenses (refer to note 2.17).

We recommend that proper accounting of the income registered by the Local Council for the year is performed in order to enter proper disclosures in the financial statements.

2.11 Rent payable

Rent payable to the Government of Malta for the rental of the car park site was overstated by €300 in the accounts when compared to the agreement. Given that the difference is not material for audit purposes, this was included in the list of unadjusted errors (refer to note 2.16).

2.12 IFRS 16: Leases

IFRS 16, which became effective for periods that begin on or after 1 January 2019, introduced the identification of a right-of-use asset with respect to leased items and a financial liability to pay rentals. The Local Council has entered into a long-term lease agreement of 30 years for the lease of the land on which the council premises are situated. With this respect the Local Council should have accounted for such asset and liability, and the respective finance costs in replacement of the actual rent which is payable each year. An audit adjustment (**AA 01/19**) was proposed and approved by the Local Council in this respect (refer to note 2.15).

2.13 Procurement of expenses

We noted that the Council incurred expenses with International Trading Company Limited with respect to the rental of lights, generators and other related fees in relation to the chocolate festival 2019 amounting to €5,723, for which no proper procurement procedures were carried out.

We recommend that proper procurement procedures are carried out in the provision of the services in question given that the current situation is in contravention to the procurement procedures as per the Local Council Regulations.

2.14 Budgeted figures

When comparing the budgeted to actual figures, we noted the following major discrepancies:

Expenses	Actual	Budgeted	Difference
	€	€	€
Personnel emoluments	133,955	155,000	21,045
Waste disposal	78,997	54,083	(24,914)
Repairs and upkeep	21,572	35,000	13,428
Refuse collection	95,620	74,385	(21,235)
Other repairs and upkeep	59,137	15,500	(43,637)
Social events	96,237	50,000	(46,237)
Depreciation	161,605	64,000	(97,605)

We recommend that the Local Council analyses the above variances in order to be as accurate as possible when preparing the budget.

2.15 Adjustments

Ref		€	PL/BS
AA 01/19	Dr Right-of-use asset	130,535	BS
	Cr Lease liability	130,535	BS
	Dr Lease liability	30,849	BS
	Dr Retained earnings b/f (interest)	53,707	BS
	Cr Retained earnings b/f (rent)	84,556	BS
	Dr Retained earnings b/f (depreciation)	47,861	BS
	Cr Right-of-use asset (depreciation b/f)	47,861	BS
	Dr Depreciation charge	4,351	PL
	Cr Right-of-use asset depreciation	4,351	BS
	Dr Lease liability	3,550	BS
	Dr Lease liability interest	4,137	PL
	Cr Rent expense	7,687	PL
	<i>Being adjustment re IFRS 16 – refer to note 2.12</i>		
AA 02/19	Dr Other government income	10,150	PL
	Cr Deferred income	10,150	BS
	<i>Being overstated income – refer to note 2.10</i>		
AA 03/19	Dr Accrued income - 2019	18,744	BS
	Cr Accrued income - 2018	8,046	BS
	Dr Other debtor: MCP share of profits 2018	13,290	BS
	Cr Rental income	23,988	PL

Being adjustment to income from share of profits of car park – refer to note 2.6

AA 04/19	Dr Creditors (individual supplier accounts) Cr Debit balances in creditors list	4,682 4,682	BS BS
	<i>Being reversal of wrong adjustment passed in 2018 – refer to note 2.7</i>		
AA 05/19	Dr Accruals Cr Cleaning and maintenance	5,163 5,163	BS PL
	<i>Being reversal of accrual – refer to note 2.9</i>		
AA 06/19	Dr Domestic refuse collection Cr Creditors control account	15,825 15,825	PL BS
	<i>Being understated creditors balance – refer to note 2.7</i>		

2.16 List of unadjusted errors

During the audit we encountered a number of errors which were at trivial level for which there was no need to adjust the financial statements. Refer to the details below:

Ref		€	PL/BS
1	Dr Bank loan interest Cr Accruals	760 (760)	PL BS
	<i>Being bank loan interest not accrued for – refer to note 2.9</i>		
2	Dr Prepayment Cr Rent expense	300 (300)	BS PL
	<i>Being overstated rent expense– refer to note 2.11</i>		
3	Dr Mayor's allowance Dr Executive secretary performance bonus Dr Salaries Cr Accruals	400 411 406 (1,217)	PL PL PL BS
	<i>Being understated salaries – refer to note 2.1</i>		
4	Dr Income Cr Accrued income	1,423 (1,423)	PL BS
	<i>Being overstated accrued income– refer to note 2.6</i>		
5	Dr Creditors control account Cr Purchases	100 (100)	BS PL
	<i>Being overstated creditors balance – refer to note 2.7</i>		
6	Dr Allowance for expected credit loss Cr Allowance for expected credit loss	1,012 (1,012)	PL BS
	<i>Being recognition of an estimation of the expected credit loss omitted from the accounts - refer to note 2.3</i>		

2.17 Reclassifications

Ref		€	PL/BS
RECL A/19	Dr Executive secretary salary	6,805	PL
	Cr Councillors allowances	2,299	PL
	Cr Employees salaries	(9,904)	PL
	<i>Being reclassification between salaries expenses – refer to note 2.1</i>		
RECL B/19	Dr Annual Government income	10,000	PL
	Cr General Income	(10,000)	PL
	<i>Being reclassification of other income– refer to note 2.10</i>		
RECL C/19	Dr General income	6,651	PL
	Cr Social events	(6,651)	PL
	<i>Being reclassification of expense– refer to note 2.10</i>		
RECL D/19	Dr Debit balances in Creditors' list	4,354	BS
	Cr Creditors control account	(4,354)	BS
	<i>Being reclassification of negative balances– refer to note 2.7</i>		

We would like to point out that the matters dealt with in this report came to our notice during the conduct of our normal audit procedures which are designed primarily for the purpose of expressing our opinion on the financial statements of the Council. In consequence, our work did not encompass a detailed review of all aspects of the system and cannot be relied upon necessarily to disclose defalcations or other irregularities or to include all possible improvements in internal control that a more extensive special examination might develop.

We would also like to take this opportunity to thank the Mayor, Executive Secretary and staff for the help during the course of our audit.



Mr Manuel Castagna CPA
For and on behalf of Nexia BT