

The Mayor
Zebbug Local Council
Bishop Caruana Street
Zebbug ZBG 1905
Malta

26th April 2019

Dear Madam,

FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2018

During our audit for the year ended 31 December 2018, we have reviewed the accounting systems and procedures operated by the Local Council. We set out in this report the more important points that arose as a result of our review.

1 Previous management letter (for the year ended 31 December 2017)

1.1 Custodial receipts

We are pleased to note that unlike previous year, the Council deposited its income and custodial receipts on a regular basis.

1.2 Payroll

We regret to note that the Council failed to update the employment contracts for employees who are employed for an indefinite period (refer to 2.1).

On the other hand, we are pleased to note that the unaudited financial statements correctly classified the personal emoluments.

Also unlike in previous year, wages agree to the FS7.

1.3 Petty cash payments

We are pleased to note that no payments exceeded the amount of € 23.29 from petty cash. However, the cash balance held at the Council was higher than € 232.94 (refer to 2.2).

1.4 Property, plant and equipment

The Council has not updated its asset insurance policies (refer to 2.3).

Unlike previous year, the Council compiled a fixed asset register although this was not performed using Sage accounting package (refer to 2.4). Also, the fixed assets are still not tagged (refer to 2.4).

Also in previous year, depreciation was calculated manually and calculated on an annual basis. During the year under review, the depreciation was still being calculated manually however, using straight line method on a monthly basis (refer to 2.4).

1.5 Receivables

We were unable to test the completeness and existence of trade receivables (refer to 2.5).

The Council has agreed to write off several overdue receivables through an audit adjustment (refer to 2.6).

Similar to 2017, the receivables list still included an amount of € 10,561 in relation to a garnishee order (refer to 2.7).

The Council has not resolved the issue of the debit balances in creditors' list (refer to 2.8).

1.6 Trade and other payables

Unlike in the previous year, the Council is preparing reconciliations most of the creditors.

Also, the disputed amount with Schembri Infrastructures is still not resolved (refer to note 2.10).

As in previous year, included with the list of accruals was an amount payable to IRD with regards to FSS and NI (refer to 2.11).

Also, a difference was identified between the accruals working and the amount as per financial statements (refer to 2.11).

We regret to note that the Local Council still had long outstanding creditors balances as at year-end (refer to 2.12).

1.7 LES cheques dated 2007

LES cheques are still held at the Local Council premises (refer to 2.17).

1.8 Tipping fees

We are pleased to note that the Council accounted for the amount advanced by DLG in relation to 2018. However, since the amount did not reflect the exact amount, the difference was included with the list of unadjusted errors (refer to 2.13).

1.9 Annual budget

As in previous year, the three-year budget plan was not prepared (refer to 2.14).

1.10 Council's meetings

We are pleased to note that the Council's minutes included all necessary information as required by the Local Councils Act. However, it was noted that one Councillor failed to attend more than one-third of the meetings called within a period of six months (refer to 2.15).

1.11 Deferred income

No difference was noted between the deferred income workings and amounts disclosed in the financial statements. However, an adjustment was required to capitalise part of the deferred income with the plant, property and equipment (refer to 2.16).

1.12 Financial situation indicator

The financial situation indicator is still less than the minimum positive balance of ten per cent of the annual Government allocation (refer to 2.18).

1.13 Budgeted figures

As in previous year, certain expenses exceeded the budgeted figures (refer to 2.19)

1.14 Legal letter

We were not provided with a legal letter for the year under review (refer to 2.20).

2 Management letter points for the year

2.1 Employee register and contract

While testing the payroll, it transpired that two employees were on indefinite contracts as they have been in employment for more than four years and do not have an updated contract.

We recommend that the Council draft a contract for these employees.

2.2 Petty cash payments

We noted that cash balance as at year end held at the Council amounted to € 757, which exceeds the limit of € 232.94 as stipulated by the Local Councils (Financial) Procedures, 1996.

We recommend that the Council abides by the procurement provisions of the Local Councils (Financial) Procedures, 1996 to keep the petty cash balances within the permitted levels.

2.3 Asset insurance

We reviewed the Council's asset insurance policy to determine whether assets are insured adequately. Since the assets are not tagged and there is no asset register, we noted that the insurance covers an estimate amount and not exactly the amount as in the accounts.

Sum insured on:	€
Buildings	73,924
Furniture and equipment	21,878
	<u>95,802</u>
Cost of assets:	€
Office Furniture & Fittings	17,890
Office and Computer equipment	28,555
Plant and Machinery	37,726
	<u>84,171</u>

In this regard, the Council should update its insurance policy to ensure that the value of assets insured against theft, damage and loss agrees to that in its books. We also remind you that the Council is bound by section LCP 1.15b.04 of the Local Councils (Financial) Procedures, 1996 to carry out a periodic review to assess the adequacy of the Council's insurance coverage.

2.4 Fixed asset register

We are pleased to note that during the year under review, the Council performed a fixed asset register using Microsoft Excel. Depreciation was calculated using the correct depreciation policy, that is on monthly basis using the straight-line method. In view of this, the qualification in last year's audit report was removed.

However, we recommend that the Council complies with the Local Councils (Financial) Procedures, 1996 which require Councils to use the month-end facility on the Sage accounting package to calculate depreciation on fixed assets.

Whilst performing the audit, the Council provided us with an adjustment amounting to € 144,317 regarding the depreciation charge for the year. This was included in the list of audit adjustments (refer to adjustment 5 in 2.25).

In addition, a discrepancy amounting to € 4,097 was found between the depreciation as per audit working and as per fixed asset register. However, since the discrepancy was not material, it was included with the list of unadjusted errors (refer to adjustment 6 in 2.26).

Also, as in previous year, we noted that the Council's assets have not yet been tagged including those acquired in 2018. This is in breach of the Local Councils (Financial) Procedures, 1996.

We recommend that the Council tags its fixed assets, where practicable, as soon as possible. This would enable individual assets to be identified and their physical existence verified.

2.5 Receivables

During our audit testing of trade receivables, we were unable to confirm all balances due as at year-end. The extrapolated error amounting to € 6,946 was not considered material for audit purposes and hence it was included with the list of unadjusted errors (refer to adjustment 7 in 2.26).

We recommend that the Council performs regular reconciliations with its debtors.

2.6 Overdue receivables

In prior years, the Council's receivables included long overdue balances and since we were unable to test the recoverability of such debtors, the audit report was being qualified in this respect.

During the year under review, the Council agreed to write off debtors amounting to € 12,700 through an audit adjustment (refer to adjustment 6 in 2.25). Remaining overdue balances are mostly receivables from Government entities and hence there are no problems with regards to their recoverability. In this respect, the audit report was not qualified.

2.7 Garnishee order

As in previous year, while testing receivables we enquired on the € 10,561 receivable from Siggiewi Local Council. We were informed that an amount of € 10,561 is held by the Law Courts through a garnishee order. We were not provided with any documentation to support and verify this information and hence we were not able to test the balance and its recoverability. Given that the amount was not considered material for audit purposes, it was transferred to the list of unadjusted errors (refer to adjustment 8 in 2.25).

We recommend the Council to analyse the situation and obtain documentation to support this balance.

2.8 Debit balances in creditors' list

Similar to previous year, the Council's books include debit balances in the creditors' list amounting to € 20,682. We were informed that these debit balances relate to payments issued but invoices not posted in the books since they were not received. (The accounts include an accrual for these invoices.) Section 26 of the Local Councils (Financial) Procedures prohibits Councils from issuing payment without the provision of a valid tax invoice.

These debit balances were reclassified to other debtors by means of audit reclassification RECL A/18 (refer to 2.25), which was approved and posted by the Council. We reiterate our recommendation that the Council reclassifies debit balances in the creditors' list and discloses these with receivables rather than setting off against trade creditors.

2.9 Trade payables

During our testing for trade payables, we had an extrapolated error amounting to € 1,559 when comparing the balance as per accounts and balance as per statement provided. Given that amount was not considered material for audit purposes, this was included with the list of unadjusted errors (refer to adjustment 3 in 2.26).

2.10 Disputed amount

The Council has not resolved a disputed amount of € 71,253 that is being claimed by Schembri Infrastructures. Schembri Infrastructures had opened a court case against the Local Council. The Local Council has not paid the amount, since it is claiming works were not done properly. The Council opened a counter claim. According to the Council, the outcome of such a dispute is expected to be in favour of the Council.

2.11 Accruals

Included with the list of accruals was an amount payable to the Commissioner for Revenue with regard to FSS and NI of € 187. This was separately identified as other liabilities through a reclassification RECL B/18 (refer to 2.25).

A difference of €268 in the accruals when compared to the financial statements balance was not identified at accounts preparation stage neither by the accountant nor by the Executive Secretary. Since the amount was not considered material for audit purposes, it was included with the list of unadjusted errors (refer to adjustment 1 in 2.26).

We recommend that this balance is written off in the accounts, unless it is properly identified.

Also, we found a discrepancy amounting to € 480 between the accrual for Christmas decorations as per trial balance and workings provided by the Council. Given that the amount was not considered material for audit purposes, it was included with the list of unadjusted errors (refer to adjustment 2 in 2.26).

Also, during our testing, we found a discrepancy of € 1,007 between accruals as per trial balance and the figures as per financial statements. We were informed that an accrual amounting to € 1,007 was omitted from the trial balance and hence this was passed through an audit adjustment (refer to adjustment 1 in 2.25).

2.12 Long-outstanding creditors

The Council's creditors' list includes the following long outstanding balances:

Creditor	2018 €	2017 €
Avantgarde Caterers	155.95	155.95
Bonnici Bros (in dispute)	514,224.68	514,224.68
Capital Pest Control	97.23	97.23
Med Design Associates	6,875.34	6,925.95
Media & Graphic	9,544.56	9,544.56
Mica Med Ltd	18,712.69	27,149.18
Ritemix	3,750.35	101,022.18
Schembri Infrastructures	71,252.64	71,252.64

We advise the Council to individually review these amounts, and either settle them or, if not due, reverse them after careful consideration and approval by the Council.

2.13 Tipping fees

While testing the accrued income for the year, it was noted that there was a balance receivable amounting to €1,348 with respect to shortages of tipping fees in relation to WasteServ Malta Limited, which was not accounted for. Given that amount was not material for audit purposes, it was included with the list of unadjusted errors (refer to adjustment 5 in 2.26).

We recommend the Council to obtain the amount of accrued tipping fees from WasteServ and update the accrued income before the financial statements are approved.

2.14 Annual budget

The rolling three year budget plan was not prepared.

We reiterate our recommendation to prepare the budget in accordance to the Local Councils (Financial) Procedures, 1996.

2.15 Council's meetings

While reviewing the Council's minutes, it was noted that one Councillor was excused for one-third of the meetings called within a period of six months. Although the Council discussed his absence in the following meeting, we recommend that the Council complies with the Local Councils Act and send its recommendation to the Minister not to declare the seat vacant.

2.16 Deferred income

While performing our testing on deferred income, we noticed that part of the grant which was received for 'Gnien I-Infetti' amounting to € 62,687 had to be capitalised against the plant, property and equipment, given that part of the project was complete. The adjustment amounting to € 22,379 was calculated on the basis of the bill issued by the supplier amounting to € 172,536 compared with the completion of the project and the grant received by end of year. Further to this, an additional adjustment amounting to € 560, was required to account for the accumulated depreciation on such grant. Refer to audit adjustments 2 and 3 in note 2.25. The remaining balance of € 40,309 was retained as deferred income in relation to the remaining part of the project.

We recommend that such workings are reviewed before the financial statements are passed for audit.

2.17 LES cheques dated 2007

As reported in previous years, stale cheques amounting to a recoverable aggregate amount of €5,346.33 were found by the current Executive Secretary when she was employed. The Executive Secretary reported this issue to the DLG and the NAO. Receipts used to be issued but cheques not deposited with the bank. Even though this related to the previous administration, according to the Department, this matter falls within the responsibility of the current Executive Secretary.

We recommend that the Executive Secretary discusses this issue again with the DLG and asks for a practical written recommendation to resolve the matter.

2.18 Financial Situations Indicator

The Council's Financial Situations Indicator (FSI) at the end of the financial year under review is at -31.52%, and hence less than the minimum positive balance of ten per cent of the annual Government allocation.

Details	€
Current Assets	817,333
Less committed current assets	(62,665)
Net Current Assets	754,668
Non-Current Liabilities	-
Current Liabilities	1,366,530
Total Liabilities	1,366,530
Less LT balance payable under PPP scheme	-
Less long-term deferred income	-
Less short-term deferred income	(338,019)
Net Liabilities	1,028,511
Net Current Assets less Net Liabilities	(273,843)
Government Allocation	837,286
FSI	-32.71%

The Executive Secretary is bound by section 4(1)(c) of the Local Councils (Financial) Regulations, 1993 to maintain a positive balance and the FSI must not be less than ten per cent of the allocation approved in terms of section 55 of the Local Councils Act. The Regulations also state that the Executive Secretary must immediately notify the DLG when the FSI falls below ten per cent, and explain the actions that are to be taken by the Council to remedy the situation.

2.19 Budgeted figures

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

Expenses	Actual	Budgeted	Difference
	€	€	€
Architect fees	21,016	-	21,016
Depreciation	460,078	437,730	22,438
Legal fees	34,638	-	34,638

We recommend that the Local Council endeavours to be as accurate as possible when preparing the budget.

2.20 Legal letter

During the audit, we requested the legal letter in the normal course of the audit to determine whether there are any legal cases and the possibility and probability of the outcome of such cases. Unfortunately, we were not provided with a legal letter.

We recommend that the Council obtains the legal letter for future audits.

2.21 Expected credit loss

IFRS 9, which became effective for periods that begin on or after 1 January 2018, introduced 'an expected credit loss' model for the impairment of financial assets.

The Council did not calculate and account for this 'expected credit loss' in fact the disclosure within the unaudited financial statements did not include such accounting policy. We suggested that 'IFRS 9' accounting policy should be included in the financial statements and the Council approved such recommendation. The receivable balances of the Council are 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 effect is not material, the audit report is not qualified in this respect.

2.22 Accrued income

While testing accrued income, we were informed that amount of € 22,439 which related to retention money receivable from Water Services Corporation was to be reversed, given that the Council received all the money in relation to the grant for 'Vjal il-Helsien' and there was no balance due as at year-end (refer to audit adjustment 4 in 2.25).

We recommend that the Council reviews its workings before the financial statements are passed for audit.

2.23 Inventories

While performing testing on inventories, we found a discrepancy between the balance as per trial balance and the stock list. The amount of € 2,089 was not considered material for audit purposes therefore it was included in the list of unadjusted errors (refer to adjustment 4 in 2.26).

We recommend that the Council accounts for movement in inventories and updates the financial statements accordingly.

2.24 Prior year adjustment

While testing the prior year adjustment passed initially by the Council for the incorrect release of grant in relation to prior years, it transpired that such adjustment was incorrect. We discussed such matter with the accountant and revised workings were provided. In this respect, this misstatement was corrected through audit adjustment 7 included in note 2.25.

2.25 Adjustments and reclassifications

We proposed the following adjustments and reclassifications, which were approved and passed by the Local Council.

No.	Description	Statement of Profit or Loss and other Comprehensive Income Dr (+) / Cr (-) €	Statement of Financial Position Dr (+) / Cr (-) €
	Adjustments		
1	Fuel	359	
	Bulky refuse collection	648	
	Accruals		(1,007)
	Being adjustment with regards to accruals – 2.11		
2	Advance payments		22,379
	Grant Gnien I-Infetti		(22,379)
	Being adjustment with regards to deferred income – 2.16		
3	Accumulated depreciation urban improvements		560
	Depreciation expense urban improvements	(560)	
	Being adjustment with regards to accumulated depreciation of grant – 2.16		
4	Grant Vjal il-Helsien		6,735
	Reversal of accrued income (P/L for the year)	15,704	
	Accrued income receivable		(22,439)
	Being reversal of retention money receivable from WSC – 2.22		
5	Depreciation expense construction	(3,770)	
	Depreciation expense urban improvements	148,087	
	Accumulated depreciation construction		144,317
	Being adjustment with regards to depreciation charge for the year – 2.4		
6	Bad debts	12,700	
	Debtors control account – Smart Tech		(7,200)
	Debtors control account – Best Print		(3,000)
	Debtors control account – La Barbon		(250)
	Debtors control account – Raymond Kellies		(2,250)
	Being write-off of debtors – 2.6		

No.	Description	Statement of Profit or Loss and other Comprehensive Income Dr (+) / Cr (-)	Statement of Financial Position Dr (+) / Cr (-)
		€	€
	Adjustments - continued		
7	Deferred grant – PPP		26,884
	Retained earnings b/f		(26,884)
	Being correct release of grant re prior years - 2.24		

Ref.	Description	Statement of Profit or Loss and other Comprehensive Income Dr (+) / Cr (-)	Statement of Financial Position Dr (+) / Cr (-)
		€	€
	Reclassifications		
RECLA/18	Dr balance in creditors list		20,682
	Creditors control account		(20,682)
	Being reclassification with regards to negative balances in creditors list – 2.8		
RECLB/18	Accruals		187
	Other liabilities – FSS and NI		(187)
	Being reclassification with regards to accruals – 2.11		

2.26 Unadjusted errors

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

No.	Description	Statement of Profit or Loss and other Comprehensive Income	Statement of Financial Position
		Dr (+) / Cr (-)	Dr (+) / Cr (-)
		€	€
1	Profit or loss	268	
	Accruals		(268)
	Being under-accrual as per workings of accruals – 2.11		
2	Christmas decoration	480	
	Accrual		(480)
	Being under-accrual of Christmas decoration as per invoice issued – 2.11		
3	Profit or loss	(1,559)	
	Creditors control account		1,559
	Being extrapolated error in trade payables – 2.9		
4	Stock (balance sheet)		2,089
	Stock (profit or loss)	(2,089)	
	Being understatement of stock as per accounts – 2.23		
5	Accrued income		1,348
	Income	(1,348)	
	Being understatement of accrued income with regards to tipping fees – 2.13		
6	Depreciation (profit or loss)	4,097	
	Depreciation (balance sheet)		(4,097)
	Being understatement in depreciation as per accounts – 2.4		
7	Trade receivables		(6,946)
	Profit or loss	6,946	
	Being overstatement of debtors balance – 2.5		
8	Siggiewi Local Council – garnishee order		(10,561)
	Profit or loss	10,561	
	Being overstatement of debtors balance- 2.7		



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 Local 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, Council members and staff for their help during the course of our audit.

Mr Manuel Castagna
For and on behalf of Nexia BT