

The Mayor  
Luqa Local Council  
Civic Centre, 173,  
New Street, Luqa  
Malta

29th April 2016

Dear Sir,

## **FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2015**

During our audit for the year ended 31 December 2015, 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 Fixed asset register**

The Council still does not maintain an adequate fixed asset register (refer to note 2.1).

#### **1.2 Classification of fixed assets balances**

The fixed assets are still not being classified correctly in the accounting records and as a result there are discrepancies between the financial statements and the accounts (refer to note 2.2)

## 1.3 Calculation of depreciation

Depreciation is still being computed manually using Microsoft Excel (refer to note 2.3).

## 1.4 Fixed assets insurance

We are pleased to note that following last year's management letter point the Council has renewed the insurance policies on fixed assets which had lapsed in 2014.

Following last year's management letter point, we regret to note that discrepancies between the insurance cover and the net book value of the assets as per nominal ledger were still noted despite the issue being raised in the previous year (refer to note 2.4).

## 1.5 Fixed asset labelling

There is still no adequate fixed asset labelling system in place (refer to note 2.5).

## 1.6 Pre-regional receivables

Pre-regional receivables were not properly accounted for. Discrepancies were found between balance as per accounts and the balance as per LES report generated by Luqus (Datatrak) (refer to note 2.6).

We are pleased to note that the income from regional committees was properly accounted for against LES debtors balance.

## 1.7 Related party balances

Following last year's management letter point, no issues were encountered during 2015 while testing balances with related parties.

## 1.8 Petty cash expenditure

Similarly to previous year, we regret to note that the majority of petty cash purchases were backed up by cash register chits. Such supporting documentation had no visible indication that these were addressed to the Local Council (refer to note 2.7).

We are pleased to note that the Council has acknowledged the previous year management letter point and has adequately followed the petty cash procurement policy. Petty cash expenditure tested was backed up by signed authorizations and all respective petty cash sheets were signed either by the Mayor or the Executive Secretary.

While performing the petty cash reconciliation, we noted that there still was a discrepancy between the balance in the accounts and the balance as per petty cash records (refer to note 2.7).

## **1.9 Bank reconciliations**

We regret to note that year-end bank reconciliations provided by the Local Council included unreconciled balances brought forward from previous years. In addition, a stale cheque was found which was not reversed at year end. Minor unreconciled balances were also traced (refer to note 2.8).

## **1.10 Final withholding tax on bank interest**

Similarly to last year, interest received on the BOV bank account balance is still being charged final withholding tax (refer to note 2.22).

## **1.11 Trade payables**

As in the previous year, no creditors' reconciliations were performed during the year under review (refer to note 2.9).

## **1.12 Overdue balances**

We still found long outstanding creditors' balances due upon review of the aged trade payables' list (refer to note 2.10).

## **1.13 Balance with Asfaltar Limited**

The balance of €16,598.90 owed to Asfaltar Limited for works carried out in previous years is still due (refer to note 2.10).

## **1.14 Balance with Alhag Ltd**

All invoices relating to the payments made to the supplier for works performed on Hal-Farrag Family Park project which were made upon architect's certification were all vouched accordingly. We are pleased to note that the balance in the accounts is in complete agreement with the statement provided by the above named creditor.

## **1.15 Accruals**

Following last year's recommendation, we are pleased to note that expenses for which invoices were already issued were not accounted for as accruals.

## **1.16 Income from central Government**

Income from central government did not agree to the government allocation by €593 (refer to note 2.18).

## **1.17 Wages reconciliation**

As in the previous year, salaries in the accounting records were not in agreement with the amounts declared in the statutory forms (refer to 2.19).

We were pleased to note that the executive secretary's salary is in complete agreement with the respective FS3.

## **1.18 Reconciliation between FS7 and FS5**

We were pleased to note that following the previous year's management letter point, the FS7 and FS5s were in complete agreement at year-end.

## **1.19 Insurance on employer's liability**

The employees of the Local Council are still not covered by an employer's liability policy (refer to note 2.20).

## 1.20 Procurement of expenses

We are pleased to note that following last year's management letter point, the procedures for the procurement of expenses are being followed and the expenses selected for testing were all backed up by a proper invoice and the respective tender documents.

## 1.21 Frequency of Council meetings

We were pleased to note that the minutes and schedule of payments were being uploaded on the Council's website as required after each meeting. However, we regret to note that there were three instances whereby meetings were still found to be more than five weeks apart (refer to note 2.21).

## 1.22 Councillors' allowance

We are pleased to report that following last year's management letter point no issues were encountered with regards to councillor allowances and attendance. All absences were backed up by a letter of excuse attached to the minutes of the meetings, as per memo 108/2010.

## 2. Management letter points for the year under review

### 2.1 Fixed asset register

As in previous year, the Council still has not managed to maintain an accurate fixed asset register.

We recommend that an adequate fixed asset register is drawn up and carefully maintained in order to keep detailed records of all property, plant and equipment which are purchased, disposed of or written off by the Council.

### 2.2 Classification of fixed assets balances

While testing the classification of fixed asset balances between the accounts and the financial statements, we noted that there are some discrepancies in classifications of *Office furniture and fittings, Construction, Urban Improvements, and Playground equipment*. We were not provided with the necessary groupings in order to identify and verify the amounts as per the fixed assets schedule in the financial statements with the individual accounts as per Sage accounting

software. However, we verified that depreciation charge for the year is not affected by this issue, as depreciation workings are based on classifications of fixed assets included in the financial statements. Moreover, during audit fieldwork, the accountant instructed us to pass a reclassification between construction and playground equipment, due to a mis-posting (refer to note 2.26).

Following last year's management letter point, we reiterate our recommendation that an exercise is performed in order to correctly classify fixed assets and group them accordingly in order to easily identify assets and verify their cost.

### **2.3 Calculation of depreciation**

As per the Local Councils (Procedures) Regulations, 1996, Councils are to use the month-end facility in the Sage accounting package to calculate depreciation automatically on fixed assets.

Moreover, depreciation workings were not correct, since opening net book value of fixed assets on which depreciation was being worked out did not agree to 2014 audited financial statements, and grants were not being deducted from the net book value. An audit adjustment was passed to correct the € 48,956 depreciation over charged (refer to note 2.25). We reiterate our previous year's recommendation that the Sage accounting package is utilised to calculate the depreciation.

### **2.4 Fixed assets insurance**

Local Councils are bound to insure their assets in line with the Local Councils (Financial) Procedures, 1996. Whilst going through the insurance policy held by the Council during 2015, we found the below discrepancies between the sum insured and the NBV as per financial accounts:

	Sum insured	NBV of the class of assets	Difference
Property	€149,121	€152,912	(€3,791)
General contents and assets including machinery but not limited	€22,565	€32,834	(€10,269)
Outside property	€164,229	€383,188	(€218,959)
Electronic equipment	€9,248	€997	€8,251
Motor vehicle	€5,500	€4,223	€1,277
Total	€350,663	€574,154	(€223,491)

As reported in the previous year's management letter, the assets owned by the Council are being underinsured. We recommend that the Local Council increases the sum insured to more than the actual book value of the accounts, in order to cater for any fixed asset additions during the year.

## 2.5 Fixed Assets Labelling

Similarly to the previous year, it was noted that only some of the Local Council's assets are labelled.

We recommend that all the assets of the Local Council are labelled to facilitate identification as per Local Council (Financial) Regulations.

## 2.6 Pre-regional receivables

While testing the balance receivable from LES debtors as at year-end, we noted that the LES report as at 31 December 2015 showed a balance due to the Council from pre-regional LES of €408,612. However, the receivable balance in the Local Council's books amounts to €409,916. Although the Executive Secretary obtained a detailed report from LES, no explanation regarding such difference was provided.

We are aware that the Loqus system was never subject to an IT audit. However, its reports were the only supporting documentation in order to test LES debtors.

We reiterate last year's recommendation that the Council reconciles this receivable balance from the LES Debtors to reflect the amount shown in the Loqus report. Given that the discrepancy was immaterial, no audit adjustment was passed (refer to list of unadjusted errors in note 2.27).

## 2.7 Petty cash expenditure

When testing petty cash expenses, we noted that the majority of such purchases are backed up by cash register chits and thus are not addressed to the Local Council. This may cast doubts on whether such expenses were actually incurred by the Council. As recommended in the previous year's management letter, all supplies to the Local Councils are to be made on the provision of a fiscal receipt clearly addressed to the Council and also properly accounted for with respect to VAT.

Similarly to previous year, we found a discrepancy of €4.77 between the petty cash balance in the accounts and the balance in the petty cash sheets. We recommend that the Council performs the necessary exercise in order to ensure that the cash balance in the accounts is in complete agreement with the actual petty cash balance. The discrepancy is below the materiality threshold and was included in list of unadjusted errors (refer to note 2.27).

Furthermore, we noticed that there was one instance where the petty cash float was exceeded by €2.46. Whilst we acknowledge that this may be due to particular one-off event, we recommend that the Council uses the Imprest system and tops up petty cash on a monthly basis, by cheque encashment and not relying on Council personnel. The use of the Imprest System is a requirement of the Financial Regulations.

## 2.8 Bank reconciliations

As in the previous year, we noted that there was a cancelled cheque (Cheque number 7054) amounting to €2,959, which was still showing as part of the unreconciled items in the year-end reconciliation.

We also noted that year-end reconciliation included a double payment (made by cheque number 7052) amounting to €2,039.66 payable to WasteServ Malta Limited. After several discussions with the Executive Secretary, this was deemed to be a wrong entry in the accounts, as cheque was cashed in 2015. Furthermore, it was noted that a stale cheque amounting to €200 was not reversed in the accounts.



The discrepancies outlined above are of an immaterial nature and no adjustments were proposed in this respect (refer to list of unadjusted errors in note 2.27). We recommend that such amounts are properly reversed in order to avoid such issues being carried forward to the following year.

Moreover, no bank reconciliation was provided for BOV bank account number 12903677023, with a discrepancy of €344.29. Discrepancy was not material and therefore no audit adjustment was passed (refer to note 2.27 for list of unadjusted errors).

## 2.9 Trade payables

While testing trade payables, a difference of €1,217 was noted between the balance as per accounts (€4,505) and the statement provided by WasteServ Malta Limited as at 31 December 2015 (€5,722). This resulted in an extrapolated error of €1,583.98. No audit adjustment was proposed as the discrepancy is not material (refer to unadjusted errors in note 2.27). We still recommend that the Council investigates this difference and reconciles the balance accordingly.

In addition, we also noticed that no creditors' reconciliations are performed. Whilst we acknowledge that a number of creditors do not prepare statements and duly make them available, we strongly suggest that a periodical exercise that confirms creditor balances is still performed.

Creditor reconciliations are an essential element of a good internal control system. They can assist in enhancing the internal control system of company whilst also ensuring that the supplier balances reflected in the accounts are accurate.

## 2.10 Overdue balances

Upon reviewing the year-end aged creditors list, we have noted that there were some creditors' balances which have been long overdue as per list below:

	2015	2014
Supplier	Amount due	Amount due
Asfaltar Limited	€ 16,598.90	€ 16,598.90
Environment Management Design Planning	€ 529.50	€ 529.50
Environmental Landscapes Consortium	€4,591.68	-
Enemalta Corporation	€120.00	-
J.B Concrete mix	€1,910.42	-
<b>Total</b>	<b>€23,750.50</b>	<b>€17,128.40</b>

We recommend that an exercise is performed by the Council to discuss these balances with the respective suppliers to come into agreement on whether they are payable or not, and if they are payable to agree on a repayment programme.

Moreover, despite last year's management letter point, the issue of the payable balance of €16,598.90 due to Asfaltar Limited is still unresolved. While we understand that if the Council does not consider the works performed to be satisfactory it has every right to withhold payment until the project is done correctly, we reiterate our previous year's recommendation that the Council reaches an agreement with Asfaltar Limited in order to avoid any further complications which may arise in future years.

## 2.11 Accrued income

Following testing performed on year-end accrued income, it transpired that funds not yet received with respect to Hal-Farrug project are misstated by €252. Such an amount represents the difference between value of works for which funds are yet to be received as per architect's valuation (€67,494) and accrued income as per accounts (€67,242).

The discrepancy noted above is not material, and was included in the list of unadjusted errors (refer to note 2.27).

## 2.12 Debit balances in creditors' list

Whilst going through the trade payables' list, we noticed that there were three suppliers who had a debit balance, as per below table:

Supplier	Amount
GO plc	€174.13
Mr Jeffrey Mifsud	€1,050.00
Polidano Brothers Limited	€28,946.03

A reclassification between trade debtors and trade creditors was passed in this respect (refer to note 2.26).

As part of our trade payables testing, we selected the receivable balance from Polidano Brothers Limited amounting to €28,946. The statement provided by the supplier showed a payable balance by the Local Council of €62,193.71. With respect to the material difference of €90,139, the Executive Secretary advised that this is partly due to an invoice (reference – 59250) dated 02/01/2009 relating to Triq Sir Ugo Mifsud amounting to €11,511.60, which was not settled by the Council due to the poor quality of material used during the related works. Moreover, the Executive Secretary is claiming that works which were done by Alhag Limited at the Laqa Family Park (sub-contracted by Polidano Brothers Limited) were charged twice to the Council (through invoice number 150530 by Polidano Brothers Limited). Payments were made to Alhag Limited for the works completed, however Polidano Brothers invoiced directly the Local Council as opposed to Alhag Limited.

Excluding the latter invoice, no alternative testing could be performed on the net difference of €67,426.23, since no reconciliation was provided. The audit report is qualified in this respect (refer to note 2.27).

### 2.13 Accruals

Upon testing the Local Council's accruals, a discrepancy of €164.55 was noted in the performance bonus accrued for in the accounts. No explanation was given by the Local Council with regards to this difference and since it is of a non-material nature, no further testing was performed, and the difference was included in the list of unadjusted errors (refer to note 2.27).

#### **2.14 FSS due**

While testing the accruals at year-end a difference of C26 was noted between FSS due as per accounts with the amount shown in the statutory forms. The discrepancy was not material and no adjustment was proposed. Refer to list of unadjusted errors – note 2.27.

#### **2.15 Rent Payable**

While testing expenditure, it was noted that the rent expense for the year in relation to a garage being rented from Mr Johnny Cassar and property rented from the Lands Department was understated by €25 when tested with the rent agreements. Being of a non-material nature, no adjustments were proposed and our report is not qualified in this respect. Refer to list of unadjusted errors – note 2.27.

#### **2.16 Deferred Income – Opening Balances**

Upon testing deferred income it was noted that there were no workings provided by the Council showing release of opening deferred income amounting to C10,598 (N/C 4010 – N/C 4013). The nature of such a grant remains unknown. Consequently the relative fixed asset category could not be identified. This means that depreciation is being charged annually whilst no income is being released.

We recommend that the Council identifies the nature of such deferred income by tracing relevant documentation in order to release income on a yearly basis over the useful life of the particular fixed asset.

#### **2.17 Deferred Income – Release for the year**

Following testing of deferred income released during the year under review, it transpired that such income is understated by €4,269 as per below:

Nominal Code/Account	As per accounts	As per audit	Difference
	€	€	€
4001 - Creditor : Projects and Initiatives	-	2,598.34	(2,598.34)
4002 - Creditor : Public Private Partnership fuq Toroq	-	2,192.55	(2,192.55)
4003 - Deferred Income: Accessibility Scheme	780.97	1,492.88	(711.91)
4007 - Deferred Income: Hal Farrug Project	176,241.08	175,657.47	583.61
4008 - Deferred Income: Live Streaming	-	265.45	(265.45)
4014 - Deferred Income: Measure 125	2,961.26	2,045.99	915.27
			(4,269.37)

An audit adjustment (AA 01/15) was proposed and approved in this respect (refer to note 2.25). The financial statements presented for the audit did not include the appropriate reclassification between short-term and long-term deferred income. A reclassification was proposed and eventually approved and passed (refer to note 2.26).

We recommend that the Local Council ensures that the deferred income workings are up-to-date so that the appropriate income is released to the Statement of Profit or Loss and Other Comprehensive Income and the apportionment between short and long term is performed before the financial statements are presented for the audit.

## 2.18 Financial allocation

Income from central Government as per accounts did not agree with government budget by €593. When we enquired with the Executive Secretary, we were told that the difference is due to telecommunications expenses which were not paid by the Council and thus netted off from Government allocation. In this regard, a reclassification was passed in the accounts so that the financial allocation agrees with the budget. Refer to reclassifications in note 2.26.

We recommend that for future years, the government financial allocation is shown in full before the financial statements are presented for the audit.

## 2.19 Wages reconciliation

During our testing we requested a wages reconciliation but we were informed that the Council does not prepare this reconciliation. From the reconciliation performed at audit stage, we have encountered a difference of €272 between the salaries in the accounting records and the amounts declared in the statutory forms, as per below (refer to note 2.27):

	€
Gross Wage as per FS7/FS5s	100,593.00
1/2 the total social security as per FS7/FS5s	6,561.22
	<hr/>
Total as per FS7/FS5s	107,154.22
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Wages and salaries as per accounts	89,398.00
Mayor's remuneration as per accounts	12,498.00
NI as per accounts	6,258.00
Less closing accruals	(7,299.00)
Add opening accruals	6,027.00
	<hr/>
	106,882.00
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Difference	272.22

We reiterate our previous year's recommendation that the Council prepares reconciliations on a regular basis to reconcile the balances as per accounts to FSS forms. This will ensure that any differences are revealed and can be dealt with immediately.

## 2.20 Insurance on employer's liability

It was noted that the Local Council's employees are not covered by an employer's liability insurance policy. We recommend that such issue is addressed immediately, given that as per section 36.4 of the Local Council (Financial) Regulations, 1993, Council members and employees are to be insured against third party liability.

## 2.21 Frequency of Council meetings

Whilst reviewing the Council meeting minutes, we noted that Meetings 3, 8 and 11 were held just over five weeks from the preceding meeting. Section 43(2) of the Local Councils Act states that Council meetings should be held at least once a month or at any other shorter intervals as the Council may decide. This period should not however exceed five weeks. We recommend that the Council organises meetings as stipulated by the relevant legislation.

## 2.22 Final withholding tax on bank interest

We noted that interest received on one of the Council's BOV bank accounts was charged final withholding tax of €1.25. We reiterate that the Council should instruct the bank not to withhold tax from interest earned, since Local Councils are exempt from income tax. The tax at source is hence being suffered unnecessarily.

## 2.23 Budget figures

When testing budgeted expenditure with that actually incurred, we noted that there were a couple of items on which there was a material difference between budgeted and actual figures. These included repairs and upkeep expenses and depreciation charge for the year:

Expense	Budgeted amount	Actual amount	Variance
Repairs and upkeep	- C50,367	C20,556	C29,811
Depreciation	-	€263,481	(€263,481)

## 2.24 Accounting function

The unaudited trial balance showed a loss of €37,200 which after our proposed audit adjustments as per below, changed to a profit of C16,025. We recommend that greater attention is paid to the book-keeping function to ensure that the annual financial statements do give a true and fair view of the Local Council results and state of affairs.

## 2.25 Audit adjustments list

AA 01/15	Dr Deferred income (b/s)	€4,269
	Cr Revenue (p/l)	€4,269

*Being adjustment to release of deferred income for the year (refer to note 2.17)*

AA 02/15	Dr Depreciation (b/s)	€48,956
	Cr Depreciation (p/l)	€48,956

*Being adjustment to depreciation for the year (refer to note 2.3)*

## 2.26 Reclassifications list

RECL 01/15	Dr Trade debtors	€30,170
	Cr Trade creditors	€30,170

*Being reclassification of debit balances in creditors' list (refer to note 2.12)*

RECL 02/15	Dr Deferred income – current	€234,358
	Cr Deferred income – long term	€234,358

*Being reclassification of deferred income from current to non-current (refer to note 2.17)*

RECL 03/15	Dr Construction	€77,721
	Cr Playground equipment	€77,721

*Being reclassification of fixed assets provided by accountant (refer to note 2.2)*



RECL 04/15	Dr Telecommunication costs	€593
	Cr Annual Government Income	€593

*Being reclassification of government income (refer to note 2.18)*

## 2.27 List of unadjusted errors

During our 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:

Dr Performance bonus	€165
Cr Accruals	€165

*Being understatement of accrual of performance bonus (refer to note 2.13)*

Dr National insurance contribution	€26
Cr FSS due	€26

*Being understatement of FSS due (refer to note 2.14)*

Dr Accrued income	€252
Cr Revenue	€252

*Being understatement of accrued income (refer to note 2.11)*

Dr Bank	€344
Cr Expense	€344

*Being understatement of bank balance (refer to note 2.8)*

Dr Rent	€25
Cr Accruals	€25

*Being understatement of rent expense (refer to note 2.15)*

Dr Wages	€272
Cr Accruals	€272

*Being understatement of wages (refer to note 2.19)*

Dr Revenue	€1,303
Cr LES debtors	€1,303

*Being overstatement of LES debtors balance (refer to note 2.6)*

Dr Bank	€5,019
Cr Trade payables	€5,019

*Being stale cheques not reversed (refer to note 2.8)*

Dr Purchases	€1,584
Cr Trade payables	€1,584

*Being extrapolation of €1,216 discrepancy in trade payables (refer to note 2.9)*

Dr Expenses	€4.77
Cr cash	€4.77

*Being overstatement of cash balance (refer to note 2.7)*

Moreover, during the audit we encountered a potential error which exceeded our performance materiality. As explained in note 2.12, in absence of a reconciliation and further information, no audit adjustment was passed and this contributed to our qualified opinion.

Dr Purchases/Property, plant and equipment	€67,426
Cr Creditor – Polidano Brothers Limited	€67,426

*Being potential understatement of Polidano Brothers Limited balance (refer to note 2.12)*

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 company. 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 their help during the course of our audit.



Mr Manuel Castagna  
For and on behalf of Nexia BT