

II-Management Letter

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27th April 2017**Munxar Local Council**
Profs. Guze Aquilina Street,
Munxar VCT 114
Gozo

Dear Mayor

RE: MANAGEMENT REPORT FOR THE YEAR ENDED 31 December 2016

We have completed our audit of the financial statements of the Munxar Local Council for the year ended 31 December 2016. 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 6 of this report.

During the course of our audit for the year ended 31 December 2016, 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 and the clerk for their assistance during the course of our audit.



Conrad Borg
for and on behalf of
RSM Malta



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Munxar Local Council

Management Report for the year ended 31 December 2016

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1.0 FOLLOW-UP TO LAST YEAR'S REPORT

1.1 Property, plant and equipment

During last year's audit, it was pointed out that an exercise should be carried out to write off the items of property, plant and equipment that are no longer in use. Although the Local Council stated in its comments on the management letter dated 16th June 2016 that the Council intends to carry out an exercise to write off such assets, this was not carried out.

We encountered instances where costs relating to a particular project were still categorized as assets under construction even though such project was ready during the year. A case was also encountered where expenditure of a revenue nature was mistakenly capitalised. There were no such cases during the year under review.

During last year's audit, it was pointed out that the depreciation was not calculated correctly. This was not encountered again this year.

It was pointed out that it is important that the fixed assets register is kept continuously updated and in agreement with the accounts. No action was taken on this matter.

Moreover, the property, plant and equipment found outside the Council's premises were under insured. This issue has been resolved following the guidance issued through Circular 33 of 2016.

1.2 Bank and Cash

Last year, it was pointed out that all cheques need to be approved before sent to the suppliers. Similar occurrences were found during the current year audit.

1.3 Payables

During last year's audit, it was noted that the wrong accounting treatment was applied to the deferred income and the amortisation thereof, where government grants were concerned. During this year's audit, it was found that this weakness still existed.

1.4 Expenditure and Tenders

The Local Council has still not issued a new tender for the services being provided by the Director for Tourism and Economic Development for the cleaning of the public conveniences and therefore is still applying the expired contract mentioned in our management letter last year. The Council was also using the services under an expired contract for street lighting. This issue has been resolved as the responsibility for street lighting was given to the Gozo Regional Committee.

During last year's audit, it was pointed out that the Council has exceeded the budgeted expenditure in certain categories. This was also encountered during 2016.

1.5 Payroll

Last year the performance bonuses of the Executive Secretary and the other employee were being accounted for together with their other salaries costs instead of the specific nominal account for bonuses. During the year under review, the correct nominal accounts were used.

1.6 Liquidity

As at 31 December 2015, the Local Council had a net current liabilities position of Euro 21,556. As at 31 December 2016, the Local Council had a net assets position of Euro 38,839.

2.0 PROPERTY, PLANT AND EQUIPMENT

- 2.1 When carrying out the physical inspection of a sample of assets found in the fixed assets register, we found that some of the electronic equipment listed therein, were not being used since new electronic equipment was purchased to replace it. We were informed that the Local Council should have carried out an exercise to write off any assets which are no longer being used, but the staff did not have sufficient time to do this. This exercise was performed in January 2017, and approved by the Local Council on 25th January 2017.
- 2.2 It is important that the Local Council carries 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 a good condition for use, after making the necessary investigations, 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 When carrying out the reconciliation between the fixed assets register and the accounts it was noticed that these were not agreeing, before passing any audit adjustments. The net book value in the accounts was Euro 1,086,450, the cost was Euro 2,006,434 and the accumulated depreciation plus grants was Euro 919,984. On the other hand, the fixed assets register had a net book value of Euro 1,035,730, a cost of Euro 1,729,732 and an accumulated depreciation of Euro 694,002.
- 2.4 It is recommended that the Council updates its fixed assets register so that the totals of each asset category match those in the nominal ledger in all respects, that is, cost, accumulated depreciation, grants and net book value. The more time is allowed to pass the more complex the exercise will become.

3.0 BANK AND CASH

- 3.1 During our testing, it was noted that some cheques were issued before they were actually approved in a Council's meeting. These cheques included the payments of the December wages and salaries of the employees and other expenses which were eventually approved in the meeting held on 25 January 2017.
- 3.2 All payments need to be approved by the Council during a meeting before being affected. In the case of the wages and salaries, these could be approved in the last meeting of that particular year. It is important that meetings are planned in such a way so as to avoid having such occurrences.

4.0 PAYABLES

- 4.1 When testing the amortisation of the deferred income relating to capital projects, we noted several variances. An adjustment had to be passed to correct these errors, which adjustment had the net effect of Euro 2,176, being a reduction in the release for the year.
- 4.2 We recommend that in the future, the matching concept and the application of the International Accounting Standard 20, are correctly applied. It is important that funds received are allocated as deferred income until the respective works are completed. Once the works are completed, the treatment of the grant is to be made on the income approach basis in accordance with International Accounting Standard 20.
- 4.3 During 2016, the Local Council received three claims for the refund of part of the grants given to it with respect to capital projects. These claims included also an interest element. This interest element amounting to Euro 797 was deducted from the deferred income instead of being shown separately as interest payable. Also, the amounts to be refunded were accounted for as accruals instead of as other payables. A reclassification of Euro 20,029 was passed in this respect. Finally, some of these refunds were incorrectly accounted for between the various deferred income accounts. Therefore, we had to reclassify these refunds to be reflected in the proper nominal accounts with the difference of Euro 3,121 being posted in the other payables account to gross it up to the actual total amounts to be refunded of Euro 23,150. These refunds were then paid in 2017.

4.4 With respect to the deferred income, we also had to pass another reclassification adjustment between two different deferred income accounts. The reclassified amount was Euro 1,312.

4.5 It is important that the deferred income is correctly classified between the different projects to which it relates to ensure that there is proper traceability and that the correct amounts are used when calculating the amortisation for the year. It is also important that any excess funds received are classified separately from deferred income and from accruals.

5.0 EXPENDITURE AND TENDERS

5.1 The Council has exceeded the budgeted expenditure under the following headings:

- 5.1.1 International memberships (Category 2500) by Euro 550;
- 5.1.2 Community Services (Category 3300) by Euro 2,530.

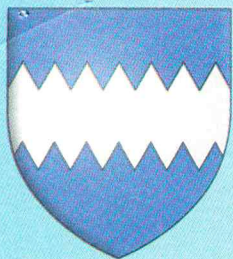
5.2 The Financial Procedures applicable for Local Councils require Councils to draw up twelve (12) months budgets, three (3) year business plans, quarterly reports and eventually yearly administrative reports at the end of the year. The Council is also allowed to revise budgets in line with actual requirements and there are enough reporting tools to help the Council revise the budgets in line with actual expenditure.

5.3 While testing a sample of expenses, we noticed that the Local Council was still using the services of the Director for Tourism and Economic Development for the cleaning of the public conveniences under an expired contract. The contract which was entered into way back in 1994 was valid for 3 years. The total amount invoiced to the Local Council for this service during 2016 was Euro 6,729. The Executive Secretary told us that if a new call for tender is issued, the cost for the cleaning of the public conveniences would be almost five times more than which the Council is currently paying which does not make sense.

5.4 We recommend that when a contract is about to expire and the contract does not have provisions for any further extensions, then a new tender should be issued immediately as stipulated in the regulations. We can understand that at times the Council keeps using expired contracts since the rates charged would be definitely lower than the rates that would be quoted under a new contract. In such cases, the Local Council should seek guidance and approval from the Local Government Department rather than just extend the contracts without any approval.

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.



Our Ref.: DGL/03/2017.

29th May 2017.

Director Local Government
Monitoring Unit
Department for Local Government
26/28, Archbishop Street,
Valletta
Malta

RE: REPLY TO REPORT BY AUDITOR GENERAL FOR THE PERIOD ENDED 31 DECEMBER 2016

1.0 FOLLOW UP TO LAST YEAR'S REPORT

Noted and currently action is being taken to, as much as possible, address any pending issues.

2.0 PROPERTY, PLANT AND EQUIPMENT

The issue about Property, Plant and Equipment has been with the Council for a couple of years. It's the intention of the Council to tackle the Fixed Asset Register problem, to compile, reconcile and update the Fixed Asset Register. As discussed also in the management report itself, this is not an easy and straight forward task, however, the Council will be doing its utmost to reconcile and update the Fixed Asset Register. This also in line the latest Circular to this matter as issued from the Department for Local Government.

3.0 BANK AND CASH

The Council always strives to get prior approval from the Council before issuance of payments. However, kindly note that cheques for wages and salaries do not require such approval prior to their issuance as long as they are then included in the following schedule of payments to be approved during the Council meeting. This is in line with the Council's obligation as an employer to issue the salaries to its employees in a timely manner.

4.0 PAYABLES

Noted. Any requirements, mainly in relation to Amortisation of Government Grants coming out from International Financial Standard 20 will be adhered to. Any proposed audit adjustments and reclassifications were posted in the updated financial statements.

5.0 EXPENDITURE AND TENDERS

Noted. The Council actually experienced a decrease in the actual Community Service cost from 2015 to 2016 amounting to Eur1719 and had a minimal increase in national and international membership of just Eur40. The council does its utmost to stick to the budget, however one have to keep in mind that it's the priority of the Council to keep the locality well maintained. Overall the Council experienced a considerable decrease in operation and maintenance expenses and administration and other expenditure. Comment about the tender for the cleaning of the public convenience noted. However, as stated during the audit, the Council is acting very diligently by using the services of a Government Entity and saving considerable amount of money since the cost of a new tender is expected to be six times the current cost of the Council.



Carmen Said
Mayor



Anthony Grech
Executive Secretary

Copies: National Audit Office, Malta.
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