

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

30th 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 local Council. We set out in this report the more important points that arose as a result of our review.

1 Previous management letter

1.1 Income

Similar to last year, the Council failed to deposit its income and custodial receipts on a regular basis (refer to 2.1).

We noted that the financial allocation was correctly accounted and classified during the year.

1.2 Payroll

We are pleased to note that this year, wages as per accounts reconciled to the FSS forms.

As regards to the FSS tax and NI due, although such balances are still not yet settled, during 2015 the council signed a repayment agreement with the Inland Revenue department (refer to 2.2).

Similar to last year, the Council failed to reclassify the mayor's allowance (refer to 2.3).

During 2015, the Council prepared an employee register but failed to update the employment contracts (refer to 2.4).

1.3 Expenditure

We regret to note that the Council is still supporting petty cash payments by cash register chits. Furthermore, the Council has again made payments of more than € 23.29 from petty cash (refer to 2.5).

Similar to last year, we noted that certain unpresented cheques were stale (refer to 2.6).

On the other hand we are pleased to note that the council followed the Local Council (Tendering) Procedures and purchases in excess of € 4,658, were supported by a call for tenders.

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1.4 Property, plant and equipment

The Council has not updated its asset insurance policies (refer to 2.7).

As in the prior year, the Council did not compile the fixed asset register and the fixed assets are still not tagged (refer to 2.8).

Depreciation is still being computed on an annual basis rather than on a monthly basis, and the Council is still not using the Sage accounting package (refer to 2.9).

Similar to prior year, the Council is still not recognising the Council's premises in its books of account (refer to 2.10).

1.5 Inventories

The Council has not implemented last year's recommendation to write off the carrying amount of inventories (refer to 2.12) and the stock list does not agree with the accounts (refer to 2.13).

1.6 Receivables

Similar to last year, we were unable to test the receivables (refer 2.14).

We are pleased to note that the Council has prepared a reconciliation of LES receipts.

Similar to last year, the council has several overdue receivables (refer to 2.16).

The garnishee order has not yet been released (refer to 2.17).

The Council has not resolved the issue of the debit balances in creditors' list (refer to 2.18).

We noted that this year, the prepayments and accrued income were properly accounted.

1.7 Creditors

The Council still did not obtain statements from all creditors and reconcile to accounts (refer to 2.19) and we have re-identified differences in creditors' reconciliations (refer to 2.19).

Similar to last year, the disputed amount with Schembri Infrastructures is still not resolved (refer to 2.20).

The amount due to South Regional Committee remained the same as it was in 2013 and 2014 (refer to 2.21).

We noted that the Local Council still had long outstanding creditor balances (refer to 2.22).

The Council did not advance the allocated amount for tipping fees to WasteServ Malta Limited and this was deducted directly from the first tranche (refer to 2.23).

We were pleased to note that this year, the balance with WasteServ Malta Limited as per accounts reconciled with the statement.

1.8 Opening balances

As in prior year, we noted certain discrepancies in the opening balances (refer to 2.24).

1.09 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 2.26).

1.10 Budget

We were pleased to note that contrary to the previous year the Council prepared a budget, for 2016.

1.11 Council meetings

This year the meetings' duration were less than three hours as stipulated by law.

1.12 Accounting function

Audit adjustments were passed during the year under review and therefore the loss for the year changed to profit as from the unaudited financial statements (refer to 2.27).

1.13 Going concern

The Council is still facing liquidity problems and has not taken any remedial action to improve the situation (refer to 2.25).

1.14 LES cheques dated 2007

LES cheques are still held at the Local Council premises (refer to 2.28).

1.15 Councillors' allowance

We were pleased to note that the Councillors who did not attend meetings supply a valid reasons for their absence.

2 Management letter points for the year

2.1 General income and custodial receipts

During the audit, we noted that the Council did not deposit its income and custodial receipts at least twice weekly in some instances. We advise the Council not to leave cash and cheques unnecessarily on the premises for a prolonged period of time as this contravenes the relevant procedures and raises security concerns.

2.2 Payment of FSS tax and NI

According to the books of account, the Council owes the amount of € 53,439 to the Commissioner of Inland Revenue in respect of FSS tax and NI due from November 2011 to December 2015. At the end of the year, the council signed a repayment agreement with the Inland Revenue Department, for the balance of € 50,088 related to 2011, 2012, 2013 and 2014. € 3, 351 related to December 2015. The Council is honouring the payments agreed with the Commissioner.

2.3 Mayor's allowance

The unaudited financial statements of the Council incorrectly disclosed the Mayor's allowance of € 1,600 with the honorarium. An audit reclassification was proposed and this was approved by the Council (refer to note 2.27).

We recommend that the Council reports the Mayor's allowance with the allowance of the other Councillors in the financial statements.

2.4 Employee register and contract

While testing the payroll we noted that the Council prepared an employee register this year that includes the appointments, resignations, dismissals, suspensions, secondments, transfers, absence from duty for sickness, leave, training and changes in remuneration and other employee records.

We were also informed that two employees were on an indefinite contract as they have been in employment for more than four years and they do not have an updated contract. We recommend that the Council draft a contract for these mentioned employees.

2.5 Petty cash payments

During our audit, we found that the source document for most petty cash expenditure is a cash register chit. Some instances which were encountered during our audit fieldwork are the following:

Sel.	Date	Detail	Ref	Amount €
1	21/12/2015	Maltapost	168	19.76
2	09/12/2015	Raymond self-service	160	23.22
3	06/08/2015	Gaetano Caruana	98	23.00
4	30/09/2015	Grima industrial supplies	117	21.65
5	13/04/2015	Maltapost	54	19.76

Cash register chits do not satisfy the requirements of the Local Councils (Financial) Procedures, 1996 that supplies are only made on the provision of a valid invoice which is addressed to the Council. To this end, we recommend that, where possible, the Council obtains a tax invoice or a VAT receipt appropriately addressed for petty cash purchases.

It was noted that certain petty cash payments exceeded the limit of € 23.29 imposed by the Local Councils (Financial) Procedures, 1996. Also, we noted that at certain times, balance held at the Council was higher than €232.94.

2.6 Unpresented cheques

During our testing, we noted that certain unpresented cheques were stale. Since the amount was not material, no adjustment was passed.

2.7 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	96,234
Electronic Equipment	<u>7,943</u>
	<u>104,177</u>
Costs of Assets:	€
Office Furniture and Fittings	18,769
Office and Computer equipment	24,711
Plant and machinery	<u>35,554</u>
	<u>79,034</u>

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

2.8 Fixed asset register

The Council is required to prepare the fixed asset register which reconciles with the nominal ledger. This, however, was not provided.

We recommend that the Council prepares the fixed asset register and that the following details are included:

- Description of asset
- Date of purchase
- Supplier details
- Invoice number
- Asset tag code
- Cost
- Depreciation method and rate
- Location of the asset

We noted that the Council's assets have not yet been tagged. 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 once the plant register is compiled.

2.9 Depreciation

When testing depreciation for reasonableness, we observed the following:

- a) In the absence of a plant register, the Council is not using the Sage accounting package to calculate the depreciation charge but is calculating it manually.
- b) Depreciation was calculated on an annual basis and a full year's charge was taken for assets acquired or completed during the year.

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. Moreover, depreciation should be calculated on a monthly basis using the reducing balance method in line with the respective Procedures and memos.

2.10 Devolution of property

We regret to note that the Council did not follow prior year recommendation and recognise the Council's office premises, which were devolved to the Council by Water Service Corporation in 1993, in the Council's books of account.

We recommend the Council records the asset at fair value, at the time of devolution, in the Council's book of account to comply with International Financial Reporting Standards.

2.11 Expired contract

During our testing, it was noted that contract with Raymond Calleja, regarding road surfacing work amounting to € 11,645 was outdated. Also, we were not presented with the full version of the agreement.

We recommend that a new tender is issued and an updated agreement is performed.

2.12 Net realisable value of inventories

The Council's inventories amounting to € 5,291 comprise books intended for resale. However, we noted that the stock is slow moving, with the majority of the books being given as prizes.

The Council should assess whether the books are being carried at the lower of cost and net realisable value in the financial statements in accordance with generally accepted accounting principles. Write-offs or provisioning of inventories might be necessary if the books remain slow-moving or have no realisable value in accordance with IAS 2, *Inventories*.

We would also like to refer you to memo 7/2004 which requires Councils to expense stocks if they are not held for resale.

2.13 Stock list

The stock list provided by the Council does not agree to the control account by € 467. We noted that the discrepancy was created because the Council did not record the stock movements in the books of account, and therefore the stock as per books is overstated by the said amount (refer to note 2.29).

We recommend that the Council accounts for all stock movements and ensures that the list reconciles to the control account.

2.14 Receivables

During our audit testing, confirmations were sent to trade receivables Rite Mix (€ 5,250), Best Print (€ 3,000), Mr Victor Borg (€ 1,500) and Smart Technologies (€ 7,200) but only the one sent to Rite Mix was received with a confirmation of Nil balance. This immaterial discrepancy was noted and transferred to unadjusted errors (refer to note 2.29). We asked for any receipts after year end but none were provided to us as, according to the Executive Secretary, these are going to be set off against future works.

Confirmation letters were sent to the below related parties but only the confirmation letters sent to South East Region and South Region were received. Discrepancies, as indicated below, resulted in both cases and were transferred to unadjusted errors (refer to note 2.29). For the remaining confirmations, since they were not received, no testing could be done:

Region	As per FS €	Differences €
Central Region	4,885.00	-
Gozo Region	391.00	-
North Region	1,164.00	-
South East Region	1,645.00	1,645.00
South Region	8,231.00	(871.00)
Siggiewi Local Council	10,561.00	-

We recommend that the Council obtains confirmations for these balances before each year's audit is performed, so that reconciliations will be performed and necessary adjustments passed before the audit.

The audit had to be qualified in this respect as we were only able to test € 15,126 from the total receivables balance of € 50,112.

2.15 Local Enforcement System

During the year under review, we were provided with statement to confirm balance due by LES. Since the report was not provided last year and the balance was not correct this year, we had to pass an adjustment of € 37,180 to update the balance and bad debt provision as per report (refer to note 2.27).

2.16 Overdue receivables

The Council's receivables include the following amounts which have been long overdue:

Receivable	Amount as per trade receivables list €	Provision for bad debts €
Best Print	3,000	-
RiteMix	5,250	-
Smart Technologies	7,200	-
Victor Borg	1,500	-
LES	181,299	181,299
ADT	1,808	1,808
	<u>216,057</u>	<u>183,107</u>

From the debtor list above, the amounts of Best Print, and Rite Mix are amounts receivable from sponsorships which have been outstanding for a long period of time. We recommend that the Council contacts these debtors to chase for payment and if it remains unlikely that they will be settled, these should be considered for a complete write off. In doing so, the Council should obtain prior approval in a meeting and document the decision in the meeting minutes.

2.17 Garnishee order

Related party balance include an amount of € 10,561 in relation to a garnishee order which was served on the Council by Siggiewi Local Council on 7 November 2006. However, the bank confirmation letter does not disclose this garnishee order.

We recommend that the Council checks with the bank if the garnishee order has been released and, if in the affirmative, when the funds will be deposited in the bank account.

2.18 Debit balances in creditors' list

The Council's books include debit balances in the creditors' list of € 44,351 compared to € 41,944 of last year. We were informed that these debit balances relate to payments issued but invoices not posted in the books since they were never received. 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 our proposed audit reclassification. We again recommend that the Council reclassifies debit balances in the creditors' list and discloses these with receivables rather than set off against trade creditors.

2.19 Trade creditors

The Council did not obtain statements from all suppliers to confirm the year-end balances. This is contrary to the Procedures and memos specifically requiring Councils to reconcile creditors' balances to statements on a monthly basis. The following are the sample of creditors that we selected but we were not provided with a creditors' statement:

Trade payable	€
Marvic and Sons Limited	15,813.00
Mica Med	51,722.00
Raymond Calleja	31,819.00
Ritemix	504,555.00
Philip Seguna	4,165.00
WM Environmental Ltd	5,652.00
M&E Management Group	-
Mario Cachia	1,693.00

A number of exceptions were identified in our reconciliation of creditor balances to available supplier statements or outstanding invoices/subsequent payments (refer to note 2.29).

	Amount as per trade	Amount verified as	Amount verified as	
Trade payable	payables list	per statement	per circularisation	Difference
	€	€	€	€
Bonnici Bros	514,180.00	504,723.00		9,457.00
Mica Med	51,722.00		53,624.00	(1,902.00)
Ritemix	504,555.00		506,055.00	(1,500.00)

During our testing, we noted that the Local Council posted twice invoices amounting to €7,049 and €8,189 from Bonnici Bros and invoice of €20,068 from Mica Med. Adjustments were proposed to the Council and these were passed in the accounts (refer to note 2.27). Bonnici Bros adjustment AA 05/15 has affected the assets - 'Construction' and therefore another adjustment amounting to €1,524 had to be passed to adjust for depreciation, refer to AA 06/15.

In view of the mistakes identified in the creditor balances during the course of our current and preceding audits, we strongly recommend that the Council appreciates the importance of creditor reconciliations to statements. The Procedures and memos specifically state the Council should obtain monthly statements from suppliers and agree amounts to the balances in the accounts.

2.20 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 as the Council had not paid the amount due to them. The Local Council had not paid the amount as works were not done properly and therefore the Council opened a counter claim. According to the Council, the outcome of such a dispute to be favourable to the Council.

2.21 Accruals and deferred income

Still included in accruals is an amount of € 6,444.87 due to the South Regional Committee in respect of post-regional contraventions remitted by the LTD to the Council by mistake. The Council is claiming that it has already remitted this amount to the committee. However, we were not given any evidence supporting this.

We recommend that the Council communicates directly with the Regional Committee to resolve the issue as soon as possible.

An amount of €5,715 related to street lighting was also not reversed in the accounts and therefore an adjustment was proposed and passed in the accounts. Refer to AA 07/15 (note 2.27).

While testing the deferred income, we were provided with the workings done by the accountant and noted that these do not tally with the amounts recognized in the financial statements. Adjustments were proposed to the Council and both were passed in the accounts. Refer to AA 03/15 and AA 04/15 (note 2.27).

2.22 Long-outstanding creditors

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

Creditor	2015 €	2014 €
Avantgarde Caterers	155.95	155.95
+ Bonnici Bros ✓	529,462.68	484,481.03
Capital Pest Control	97.23	130.98
Corinthia San Gorg ✓	738.20	738.20
Do it all	5,225.71	3,514.55
Horace Enterprises	47.20	47.20
+ Med Design Associates ✓	49,389.39	60,298.46
Media & Graphic ✓	11,544.56	6,136.24
+ Mica Med Ltd ✓	71,789.54	45,383.71
+ Raymond Calleja ✓	31,818.63	27,231.55
+ Ritemix ✓	504,554.94	652,051.79
+ Schembri ✓	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.

2.23 Tipping fees

During 2015, the DLG deducted the amount of € 44,081 from the annual allocation in respect of overdue invoices for tipping fees. It was also noted that in 2016, the DLG advanced an amount of €45,313 related to 2015 which was not accounted for. An adjustment was proposed to the Council and passed in the accounts of Zebbug Local Council (refer to 2.27).

We recommend that the Council advances the relevant amounts allocated by Government (as indicated in the allocation document) to WasteServ Malta Limited.

2.24 Opening balances

We identified that opening balances were not properly brought forward. No audit adjustment was proposed in respect of the above discrepancies as these were corrected subsequently. However we recommend that the Council refers any exceptions and inconsistencies in the Sage accounting package to technical staff to rectify them.

2.25 Going concern

The schedule below shows that the Council's performance, financial and liquidity position (after any prior year adjustments) have improved significantly over the last years:

Financial year	Profit (loss) €	Retained funds €	Negative liquidity €
2013	(265,191)	213,070	(1,362,696)
2014	(84,283)	128,787	(657,958)
2015	32,206	160,993	(551,568)

The negative liquidity balance indicates that the Council has assumed significant amounts of debt during these past years which will take several years to be repaid back considering that the Council has to meet fixed operating costs annually to maintain a minimum level of service. The Council is also reliant on the continuing support of the Government and of its creditors.

The Council's negative liquidity position indicates that there are doubts regarding the ability to continue as a going concern. In fact, we have included an emphasis of matter paragraph in our auditor's report on the financial statements.

2.26 Financial Situations Indicator

The Council's Financial Situations Indicator (FSI) at the end of the financial year under review is negative of 65.63%, and hence than the minimum positive balance of ten per cent of the annual Government allocation.

Details	€
Current Assets	336,478
Less committed current assets	(33,916)
Net Current Assets	302,562
Non-Current Liabilities	1,743,275
Current Liabilities	888,046
Total Liabilities	2,631,321
Less LT balance payable under PPP scheme	(817,013)
Less long-term deferred income	(926,262)
Less short-term deferred income	(98,781)
Net Liabilities	789,265
Net Current Assets less Net Liabilities	(486,703)
Government Allocation	741,581
FSI	-65.63%

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.

2.27 Accounting function

The unaudited financial statements showed a loss of €35,112 which after our proposed audit adjustments and reclassification as per below, changed to a profit of €32,206. 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 Council results and state of affairs.

	Adjustments	€	PL/BS	Nominal
AA 01/15	Dr Accrued income	45,313	BS	0260
AA 01/15	Cr Other Supplementary Income	- 45,313	PL	0002
AA 01/15	Being payment done by DLG to Wasteserv – 2.23			
AA 02/15	Dr Creditor - Mica Med	20,068	BS	4000
AA 02/15	Cr Street lightning	- 20,068	PL	3067
AA 02/15	Being reversal of invoices posted twice – 2.19			
AA 03/15	Dr Depreciation P/L	5,499	PL	8001
AA 03/15	Cr Depreciation B/S	- 5,499	BS	8031
AA 03/15	Dr Grant B/S	2,474	BS	4104
AA 03/15	Cr Grant P/L	- 2,474	PL	0002
AA 03/15	Being adj in depreciation and release of grant – 2.21			

AA 04/15	Dr Depreciation P/L	4,949	PL	8001
AA 04/15	Cr Depreciation B/S	- 4,949	BS	8031
AA 04/15	Dr Grant B/S	2,672	BS	4104
AA 04/15	Cr Grant P/L	- 2,672	PL	0002
AA 04/15	Being adj in depreciation and release of grant – 2.21			
AA 05/15	Dr Creditor – Bonnici	15,238	BS	4000
AA 05/15	Cr Construction (Assets)	- 15,238	BS	7100
AA 05/15	Being reversal of invoices – 2.19			
AA 06/15	Dr Depreciation B/S	1,524	BS	8031
AA 06/15	Cr Depreciation P/L	- 1,524	PL	8001
AA 06/15	Being dep adjustment regarding the above adjustment – 2.19			
AA 07/15	Dr Accrual	5,715	BS	4100
AA 07/15	Cr Street lightning	- 5,715	PL	3067
AA 07/15	Being dep adjustment regarding the above adjustment – 2.21			
AA 08/15	Dr LES Debtors	37,180	BS	0210
AA 08/15	Cr Administrative fee	- 37,180	PL	0024
AA 08/15	Dr Increase in provision for Bad debts - LES	37,180	PL	New
AA 08/15	Cr Provision for Bad debts - LES	- 37,180	BS	0211
AA 08/15	Being adjustment regarding the LES Debtors – 2.15			
	Reclassification			
RECL A/15	Dr Mayor's Allowance	1,600	PL	
RECL A/15	Cr Councillors Remuneration	- 1,600	PL	
RECL A/15	Being reclassification of mayor allowance – 2.3			

2.28 LES cheques dated 2007

An amount of 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 to the DLG and the NAO regarding this issue. Receipts used to be issued but cheques not deposited to the bank. Even though, this related to previous administration, according to the department, it is the responsibility of the current executive secretary.

We recommend the executive secretary to discuss again this issue with the DLG and ask for a practical written recommendation from the DLG.

2.29 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:

No.	Description	SoCI €	SoFP €
1	Dr P/L	467	
	Cr Stock		(467)
	Being difference in stock – 2.13		
2	Creditors		8,334
	Cr P/L	(8,334)	
	Being differences in creditors – 2.19		
3	Debtors		(6,024)
	P/L	6,024	
	Being difference in debtors – 2.14		

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