

22/2023

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02 May 2023

Local Council Ghajnsielem  
J.F Chambray,  
Ghajnsielem GSM 1501,  
Gozo

Dear Mayor,

**RE: MANAGEMENT REPORT – FOR YEAR ENDED 31 DECEMBER 2022**

We have completed our audit of the financial statements of the Local Council Ghajnsielem for the year ended 31 December 2022. 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, in part or in full, may not be distributed, used or quoted 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 12 of this report.

During the course of our audit for the year ended 31 December 2022, 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 Council Staff for their assistance during the course of our audit.

Yours faithfully



Conrad Borg (Principal)  
for and on behalf of  
RSM Malta

REGISTRY

- 8 MAY 2023

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**Local Council Ghajnsielem**

**Management Report for the year ended 31 December 2022**

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## 1.0 Follow-up to Last Year's Report

### 1.1 Property, plant and equipment

During the previous audit, several weaknesses relating to the property, plant and equipment had been identified namely:

- During the exercises carried out by the Local Council on the fixed assets register in 2012 and in 2017, variances were found that were simply written off without the necessary justifications. The method used for the building up of the new fixed assets registers was not reliable.
- The fixed assets register lacked certain important details.
- The adoption of Directive 01/02017 was not properly carried out.
- The net book value of the fixed asset register was not reconciling to the amount shown in the financial statements.
- Grants received for projects not yet carried out were still being capitalized and grants not yet received relating to completed projects, were not being accrued for.
- Projects completed were still being classified as assets under construction.
- Accruals were being capitalized with no support.
- An invoice dated in 2020 was posted in 2021.

During the year being reviewed, the issues mentioned above still existed with the exception of the final three points.

### 1.2 Receivables

From the three samples chosen for the confirmation of the accounts receivable, only one confirmation was received by the date we closed off our audit. Furthermore, a variance was noted between the confirmation received and the balance shown in the accounts.

During the current audit, the variances issue was encountered again.

### 1.3 Payables

When testing the payables, the below weaknesses were encountered:

- From the seven samples chosen only three supplier statements were received by the time that the audit was concluded.
- The report we requested from the architect about the projects carried out during the year was not received.

The first weakness was encountered again this year. This was not the case for the last weakness as the report was received.

### 1.4 Income

In the prior year, the Local Council recorded an accrued income in respect of funds which would not be received since the Council has not applied for them on time. During the current year, no such weakness was noted.

1.5 Expenditure

During the previous audit, the following weaknesses have been highlighted:

- Actual expenditure in certain categories exceeded the budgeted expenditure.
- Purchase requests and purchase orders were not prepared regularly.
- Instances were noted where the procurement procedures were not properly followed.

All these weaknesses were encountered again this year.

1.6 Personal Emoluments

Last year, the following weaknesses have been highlighted:

- There were discrepancies in the tax deductions between the FS5s and the FS7.
- There were discrepancies both in the gross emoluments and in the tax deductions between the FS3s and FS5s.
- FS 7 provided to us was not signed.

This year no variances resulted between the different FSS forms.

1.7 Other Matters

In the prior year, it was noted that no meeting was held during the month of April. This was not noted again in 2022.

## **2.0 PROPERTY, PLANT AND EQUIPMENT**

- 2.1 During 2012, the Local Council outsourced the exercise of building the fixed assets register from scratch. One of the problems encountered in this exercise was the fact that the Council had no Sage backups of the accounts prior to the year 2008 since there was a change in the Council's accountant and apparently, he had the backups on his personal computer which were never given to the Local Council. We were given to understand that the procedure adopted was that the Council staff went around the Council premises and the urban areas within the locality to take note of the assets and then gathered all the relevant documents that could be found about the items of property, plant and equipment of the Council. As for the road resurfacing, the executive secretary contacted the architect who was responsible for the roads which were resurfaced by the Council from 1994 onwards and the costs connected to such works were taken from the final architect certification obtained. As for the Council premises, the Council listed all the assets present in the new civic centre and agreed them to the nominal ledger.
- 2.2 The method used by the Council created discrepancies in relation to the 2011 audited financial statements and the difference between the register and the nominal ledger has been accounted for as impairments through a prior year adjustment. The following were the variances noted:
- 2.2.1 The closing cost of property, plant and equipment as per the audited financial statements for the year ended 31<sup>st</sup> December 2011 amounted to €1,046,654 whilst the new opening cost as at 1<sup>st</sup> January 2012 amounted to €889,317. This means a difference of €157,337 out of which €1,108 represented a reclassification to under intangible assets.
  - 2.2.2 The accumulated depreciation as per the audited financial statements for the year ended 31<sup>st</sup> December 2011 amounted to €464,800 whilst the new opening accumulated depreciation as at 1<sup>st</sup> January 2012 amounted to €361,049. This means a difference of €103,751 out of which €330 represented a reclassification to under intangible assets.
  - 2.2.3 The resulting net figure after removing the reclassified amounts was €52,808. This amount has been passed as a prior year adjustment without an indication as to which assets the amounts written off related to.
- 2.3 Moreover, the new fixed assets register still lacks important details with respect to the new civic centre. A one-line item under the buildings category shows the total balance of all the construction works, electrical works and other expenditure incurred in the building of the new civic centre. It is understood that the Council grouped all the assets together as one asset since the civic centre was capitalised wholly. During our audit visit, we were then provided with an itemised list on MS Excel.
- 2.4 The method used for the building of the new fixed assets register as described above, creates several problems. There is no assurance that the costs taken for the individual items of property, plant and equipment are all correct. It is very possible that items have been left out from the register even though they are still in existence and in good condition. There is no assurance that the new calculation of the depreciation of the assets was carried out correctly by commencing the

depreciation calculation from the correct date. The new register still lacks sufficient details to ease the traceability of the different assets.

- 2.5 Furthermore, since the above exercise was carried out, the fixed assets register was not being regularly updated. During 2017, another exercise to update the fixed assets register was carried out. Again, variances arose in both costs and depreciation that were written off without there being a real justification. The most material write offs related to the assets under construction as at 31 December 2016 amounting to €30,488 and the accumulated depreciation of the 'Special Programmes' category of €32,919. No justification was obtained for the former adjustment other than because no details were available about what the assets under construction were.
- 2.6 Due to the materiality of the amounts involved and the number of uncertainties in the new valuations of the Local Councils' property, plant and equipment, we had to qualify our audit report.
- 2.7 The current fixed assets register furthermore does not contain details of the costs, accumulated depreciation and grants of the assets fully written off. It only contains a description of some of these assets. Should the Local Council dispose of, or would need to write off, any of these fully depreciated assets, the information would not be available to pass the necessary adjustments in the accounts.
- 2.8 It is recommended that an exercise is carried out to identify the variances that arose between the accounts and the register during the two exercises that were carried out in 2012 and 2017, which variances were simply written off from the accounts. The register should include among other details, the detailed description of the assets, their identification codes, their locations and the category of the assets according to their nature. Assistance might be sought from the previous and current auditors of the Local Council, for any possible information that they might have which for some reason is not available at the Local Council. If the correct costs, accumulated depreciation and grants could not be recorded in the fixed assets register due to the change in the accounting policies in line with Directive 01/2017, then a separate register containing this information should be maintained that would then be used when reconciling the costs, accumulated depreciation and grants found in the fixed assets register with those found in the accounts and the financial statements.
- 2.9 Furthermore, we highly recommend that the Council obtains copies of the accounts' backups for the periods before the year 2008. Kindly note that the Council is obliged to have such backups available at its offices.
- 2.10 Following Directive 01/2017 issued by the Department for Local Government to Local Councils on the change in the accounting policies on depreciation, whereby the straight-line method is to be applied instead of the reducing balance method and the accounting policy on government grants, whereby the capital approach is to be applied instead of the income approach, we noticed from the limited procedures that we could carry out that:
  - 2.10.1 Items of property, plant and equipment whose useful life expired were not written off upon the adoption of the new depreciation accounting policy.
  - 2.10.2 The depreciation is not being worked out on the remaining useful life of the assets.

- 2.10.3 Grants received for specific projects, were allocated to several items of property, plant and equipment rather than those specific projects, clearly indicating that the allocation of grants to the respective assets was not properly carried out.
- 2.10.4 As at 31 December 2017, the Local Council had deferred income amounting to €101,363 relating to three different projects that were not yet carried out as of that date. Yet, we noticed that when the comparative figures were restated following the change in the accounting policy on government grants, these grants were still allocated against property, plant and equipment rather than left under deferred income. The projects were then completed in subsequent years.
- 2.11 We highly suggest that the exercise of applying the changes in the accounting policies is redone diligently and the necessary corrections made to the accounts through a prior year adjustment. Once the exercise is completed, the fixed assets register would need to be updated as well. When doing such an exercise, it is important to keep all the necessary workings to be able to reconcile the costs and accumulated depreciation as per updated fixed assets register to the figures shown in the note to the financial statements on property, plant and equipment. It is also to be ensured that grants are allocated to the correct projects given that some grants were capitalised before the projects were carried out and hence were allocated to projects which they did not intend to cover.
- 2.12 We noted that the net book value disclosed in the fixed assets register, consisting of property, plant & equipment and intangible assets, does not reconcile to the net book value disclosed in the financial statements by €55,336.
- 2.13 We recommend that the fixed assets register be updated in line with the information disclosed within the financial statements and that this be reconciled at year end to the amounts disclosed in the books as this might subsequently impact the depreciation charge accounted for.
- 2.14 As part of our audit procedures, we request a letter from the architect of the Local Council about the projects carried out by the Local Council during the year and their stage of completion. The reply noted that the project pertaining to the Learning Garden was 75% complete and nothing was reflected in the books in relation to this ongoing project. In this regard, an accrual of €205,913 was passed to reflect the progress of works in the books of the Council. In line with this, an amount of €30,032 was released from deferred income and a further €25,937 was accrued to recognize the grants allocated against this project.
- 2.15 During our discussion with the Executive Secretary, it was noted that for Measure 4.4 two additional invoices were issued by the contractor after year end; one of which replaced the last invoice issued in 2022 due to an update in the certification. Given that as per the architect's reply the project was completed by the end of the year, the following adjustments were passed to reflect the updated figures and to accrue for the remaining amount invoiced after the end of the year: the original invoice of €13,998 was reversed from the accounts' payable, the two new invoices issued in 2023 amounting to €10,507 were accrued for, and the additions in property, plant and equipment were reduced by the net effect of €3,491.
- 2.16 We recommend that the Council reviews its accounts thoroughly at year-end to ascertain that all accruals recorded in the books are complete and supported by adequate documentation. Reference should be made to the report received from the architect regarding the value of the projects and their state of completion.

- 2.17 It was also noted that in the case of Pjazza Tolfa, costs were capitalized, but the amount of funds released from deferred income was understated due to the total amount not having yet been received. Consequently, an adjustment was passed to recognize €79,578 representing the grants yet to be received.
- 2.18 During the year, it was noted that the Local Council accrued for funds in relation to projects that were in excess of the amounts that the Council was eligible to cover. As a result, the accrued income was reduced by €12,113 in the case of Measure 4.4 and €2,862 in the case of Measure 4.3.
- 2.19 Where grants are concerned, the principles of IAS 20 – Accounting for Government Grants and Disclosure of Government Assistance, are to be correctly applied using the capital approach in line with the accounting policy adopted by Local Councils. The Council should be aware of what costs have been capitalised for which the Council has received, or will receive, grants in accordance with agreements made, and should immediately reflect the related grants under the property, plant and equipment after considering the applicable terms and conditions as per agreement.

### **3.0 RECEIVABLES**

- 3.1 One sample was chosen to test the accounts receivable as at the end of the year, which sample covered 75% of the total accounts receivable before deducting the provision for doubtful debts. A variance of €34,558 was noted between the balance shown in the accounts and the confirmation received. The variance is mainly coming from the fact that the Council sent the invoices late and have not been yet recognised by WasteServ Malta Limited.
- 3.2 At the end of each financial year, during the process of closing off the accounts, the Local Council should ask for statements or confirmations from its customers to be able to reconcile the balances in the books of accounts with the balances confirmed by the customers and any variances found should be investigated. These statements or confirmations should be made available to the auditors during their audit. We further recommend that the Local Council issues its invoices on a monthly basis and that these are be sent to customers on a regular basis. This would also help improve its liquidity.
- 3.3 When checking the receivable balances older than two years, for which a provision for bad debts is to be recorded as per instructions issued by the Department, it was noted that €9,774 were not provided for. An audit adjustment was passed to increase the provision with this amount.
- 3.4 The Council must abide with the instructions received from the Department to at least provide for any balances older than two years. Based on the assessment, the provision for bad debts should then be adjusted accordingly.
- 3.5 During the audit, we noted that included within the prepayments was an amount of €3,000 representing a bank guarantee by the Local Council. A reclassification adjustment was passed to reflect the amount under the other receivables within the financial statements.
- 3.6 Care should be taken when posting the transactions in the books of accounts to ensure that each transaction is posted in the correct nominal ledger to ensure correct presentation in the notes to the financial statements.

#### **4.0 PAYABLES**

- 4.1 From the eleven samples chosen for the testing of the accounts payable, no suppliers' statements were received by the time we concluded our audit despite the regular chasing made. We could not satisfy ourselves through adequate alternative audit procedures as to the correctness and completeness of the accounts payable.
- 4.2 We recommend that the Local Council itself should ask its suppliers to provide it with statements at least at the end of the financial year, as we were given to understand that most of them do not send statements. Statements received are to be reconciled with the balances shown in the books of accounts. These statements are to be made available to the auditors during their audit.
- 4.3 When analysing the list of the accounts payable, we noted a negative balance of €1,790, representing a payment in advance to a foreign supplier. A reclassification adjustment was passed to reflect such balance under the other receivables.
- 4.4 It is important that any negative balances within the payables, are properly reclassified for presentation purposes to be shown under the correct category in the financial statements.
- 4.5 During our testing, we noted that an amount of €25,072 relating to Christmas activities in 2021 had been included as an expense in 2022 indicating that no accruals were taken in the prior year. A similar instance was noted when the invoice obtained to support one of the samples chosen for our testing, was dated in 2019 but was included in 2022 due to it having been paid during the year and not accounted for in the respective year to which it related.
- 4.6 From our testing procedures, we also found that invoices issued after year end but pertaining to social and Christmas events that took place during 2022, have been omitted from the books. Consequently, an adjustment was passed to accrue for such expenses with a total amount of €30,988.
- 4.7 Expenses should be accounted for in the year to which they relate. The Local Council should be aware of the services and products acquired for which no invoice would have been received by the end of the year, and an accrual is to be accounted for until the actual invoice is received.
- 4.8 All deferred income was being shown under as current liabilities. After our review of the projects to which such deferred income pertains to, it was agreed with the Executive Secretary that an amount of €301,861 is to be reclassified as non-current given that such projects were either still in the tender stage or yet to start the process and the projects not planned to be done during 2023.
- 4.9 We recommend that at the end of the year, an analysis of the timing of each project be performed to ascertain whether the deferred income relating to the project, is correctly classified in the financial statements.

#### **5.0 INCOME**

- 5.1 During the year under review, we noted that the amount of €3,001 pertaining to the adjustment fund from the financial allocation has been accounted for under supplementary government income. The amount was reclassified together with the remaining amount allocated in terms of Article 55 of the Local Councils Act for presentation purposes.
- 5.2 Care should be taken when posting the transactions in the books of accounts to ensure that each transaction is posted in the correct nominal ledger, that will consequently lead to correct presentation in the financial statements.

## 6.0 EXPENDITURE AND TENDERS

- 6.1 It was noted that the Council has exceeded the budgeted expenditure for several categories, namely:
- 6.1.1 Public & Office Utilities (Category 2100) by €1,088
  - 6.1.2 Materials and supplies (Category 2200) by €5,785
  - 6.1.3 Rent (Category 2400) by €1,260
  - 6.1.4 Memberships (Category 2500) by €140
  - 6.1.5 Office services (Category 2600) by €2,401
  - 6.1.6 Travel (Category 2800) by €920
  - 6.1.7 Information Services (Category 2900) by €562
  - 6.1.8 Cleaning (Category 3000) by €13,822
  - 6.1.9 Professional Services (Category 3100) by €79,410
  - 6.1.10 Training (Category 3200) by €1,432
  - 6.1.11 Hospitality (Category 3300) by €118,218
  - 6.1.12 EU Projects (category 3700) by €8,482
- 6.2 The Financial Procedures applicable for Local Councils require Councils to draw up twelve (12) months budgets, three (3) years 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 note which areas in the budget need revising.
- 6.3 We recommend that the Council makes use of the reporting tools in hand to take corrective measures in the budget every quarter such that by the end of the accounting period/year such discrepancies would not materialise.
- 6.4 We noticed that the Council does not draw up purchase requests in line with the Local Councils Financial Procedures. With regards to the purchase orders, these are prepared for most of the purchases but there are still cases where these are not prepared. There appears to be no specific reason behind this practice.
- 6.5 It is understood that at times the urgency of matters might require that bureaucracy is reduced to the minimum possible, however we are still of the opinion that the necessary paperwork should have been done in line with the financial procedures.
- 6.6 From the samples chosen for the testing of the expenditure, no support was received for 65% of these to confirm that the procurement procedures have been followed. Accordingly, we could not assess whether there were any deviations from the requirements of the Local Councils Financial Procedures.
- 6.7 Not following the procurement procedures, would go against the Local Councils Financial Procedures that the Council should abide with. Therefore, we strongly recommend that the Council should maintain evidence that the procurement procedures have been followed and if there were instances where these were not followed, it should take immediate action to ensure that such occurrences are not repeated in the future.
- 6.8 We noticed that the Council does not draw up purchase requests in line with the Local Councils Financial Procedures. With regards to the purchase orders, these are prepared for most of the purchases but there are still cases where these are not prepared. There appears to be no specific reason behind this practice. It is understood that at times the urgency of matters might require that bureaucracy is reduced to the minimum possible, however we are still of the opinion that the necessary paperwork should have been done in line with the financial procedures.

- 6.9 The above issues go against the Local Councils Financial Procedures that the Council should abide with. Therefore, we strongly recommend that the Council takes immediate action to regularize itself on these matters and to ensure that such occurrences are not repeated in the future.

**7.0 PERSONAL EMOLUMENTS**

- 7.1 When reconciling the FS7 with the books, we noted that the social security contributions as per FS7 amounted to €9,876 whilst the social security contributions in the books amounted to €9,412, resulting in a variance of €464.
- 7.2 At the end of the financial year, before sending the annual forms, a reconciliation should be carried out between the different FSS forms to ensure that all the information disclosed therein tally. These forms should also be reconciled with the books of accounts.

**8.0 OTHER MATTERS**

- 8.1 No legal reply was received from the Council's lawyer up until the end of the audit. Due to this, we could not assess whether there were any potential contingent liabilities to be disclosed within the financial statements, other than the case mentioned in the respective note.
- 8.2 We recommend that the Local Council should inform its lawyer that such a request will be made by its auditors on an annual basis and explain that a response is required as part of the audit process.

### **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.