State of Palestine

State Audit &Administrative Control Bureau

President Bureau

دولة فلسطين

ديوان الرقابة المالية والإدارية

ديوان رئيس الديوان

State Audit & Administrative Control Bureau

Consolidated Financial Statements 'Final Accounts' Released by Ministry of Finance & Planning Fiscal year Ended 31/12/2013

Audit Opinion Report

March 2018

Audit & Control for Construction, Development & Good Governance Enhancement

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Table of Content

Introduction

The Bureau has audited the financial statements of the State of Palestine, which contain the 'budget vs. actual comparison' list, 'consolidated statement for the State of Palestine cash receipts and payments' as at December 31, 2013, summary of significant accounting policies and other explanatory clarifications.

Ministry of Finance (State of Palestine) Responsibility for the Financial Statements

In accordance with law 7/1998 on budgeting and financial affairs (and respective amendments as per decree 4/2008), Palestinian Financial Ordinance of 2005 for ministries and public entities (and respective amendments), amended Basic Law and law of State Audit and Administrative Control Bureau 15/2004, Ministry of Finance is responsible for preparation and fair presentation of the financial statements as set forth by the International Public Sector Accounting Standards (IPSAS) 'cash basis'. This responsibility includes set, enforce and retain internal control system for the purpose of preparation and presentation of fair and substantial error-free financial statements, whether arising from fraud or errors. Responsibility of management (MOF) includes selecting and following proper accounting policies, and undertaking reasonable accounting estimates depending on conditions.

Responsibility of The Bureau

- Responsibility of the Bureau includes express opinion on these statements based on the audit we carried out. The audit has been undertaken according to INTOSAI standards as well as ISSAIs, which require that professional conduct rules shall be observed, and that the audit shall be planned and undertaken in order to have reasonable confirmation whether the financial statements are free of substantial errors.
- The audit included procedures enforced to obtain audit evidence for amounts and disclosures contained in the financial statements, so procedures selected are based on discretion of auditors of the Bureau, including risk analysis for substantial errors in financial audit, whether arose from fraud or errors. When evaluating these risks, the Bureau takes into account internal control procedures applied at MOF regarding preparation and fair presentation of financial statements, for the purpose of setting proper audit procedures as conditions require, not to express opinion on effectiveness of internal control system of the State of Palestine. The audit also included appropriateness assessment of accounting policies followed, reasonability of accounting estimations set by MOF and evaluation of total presentation of the financial statements.

We believe that the audit evidence we obtained furnish proper and sufficient basis for our qualified opinion.

Basis of Qualified Opinion

Financial Qualifications

I. General Qualifications

- Through the review of modified financial statements, 2013 it was observed that the total non-cash receipts does not match the non-receipt payments total (clearance, third parties). Total receipts reached 1.645.993,000 NIS, whereas total payments was 1.625.940,000 NIS, which means that total receipts exceeds payments at 20.053.000 NIS.

- The Bureau expressed a qualification to MOF and other responsibility centers record of spending entries and bonds for accounts of revenues, expenses and banks against the opening balances account, which violates that double entry regulations and affects authenticity of revenues, expenses and cash.

- The Bureau expressed a qualification to MOF modification to clarifications of 2012 without mentioning and clarifying them in the financial statements, 2013 (the comparison column of financial statements, 2012). Table below shows that:

Clarification	Financial statements, 2012 mentioned in final accounts, 2013/NIS	Audited financial statements, 2012/NIS	Difference/NIS
Clarification (8): absentees properties – municipal dues	103,000,000	189,000,000	86,000,000
Clarification (8): absentees properties – paid	35,000,000	0	835,000,000:
Clarification (17): absentees properties savings – tax refund payments	35,000,000	0	35,000,000

- There are accounting errors in advances closing, where some responsibility centers made entries and closed advances despite there are not advances in the accounting system, which reduced expenses in the advances account upon closure, so actual value of expenses does not appear.

- MOF did not disclose some transactions that represent cash flows in the advances account (payments) as part of payments in the financial statements, 2013.

- There was not proper influence disclosure of cheques to be cashed deposited in banks in cash accounts (clarification 22, cash), which listed cheques with entries to which the ‘cash available to use in cash balance’ definition does not apply. This is evident in the bank accounts of the General Petroleum Authority, where total cheques to be cashed was 366.755,790 NIS as at December 31, 2013.

II. Qualifications on Tax/Non-Tax Revenues & Receipts, 2013

Local Taxes, Clarification (2)

1. Income tax (tax files valuation)

- There was not effective follow up to taxpayer files at income tax department, where the tax declarations that were not presented, 2013 raised compared to 2012. the rate is %81.5 of total declarations that should have been presented in 2013, whereas it was %79 in 2012, which increases tax evasion and reduces tax collection to the Treasury.

- Poor follow up procedures regarding record of income taxpayers indebtedness, which increased the indebtedness amount recorded for the benefit of the Treasury, without actual collection.

- Poor follow up procedures by income tax department to taxpayers with investment exemption, in terms of fulfillment of the investment exemption certificate terms, and check there are other actions that do not fall under investment exemption, which lead to incomplete income tax revenues and loss of amounts from the Treasury.

- There 3655 bounced cheques worth of 12,068,294 NIS at income tax department. Percentage of bounced cheques that have not been followed up reached %77, which makes it difficult to collect them due to legal status brought by limitation.

2. value added tax (clarification '2', local tax)

- Poor follow up to taxpayers who ceased presenting regular statements, where it has been observed that the number of taxpayers who failed to present regular statements increased by %43, 2013 (%41 in 2012), as per report taken from the Revenue Management System (RMS), which encourages tax evasion, affects collection by tax department and badly influences revenues to the Treasury.

- There is not follow up to tax variations between sales tax and procurement tax disclosed through clearance vouchers on one side, and disclosures of taxpayers in regular monthly statements on the other side. It was found there are taxpayers who have statements with less value for sales deals through regular statements than value of taxpayer sales through clearance vouchers (P). Additionally, there are taxpayers who have procurement disclosures through clearance vouchers (I) with value greater than procurements disclosed in regular statements, which leads to tax evasion and incomplete revenues (repeated).

- There is not follow up to taxpayer files who have unbalanced statements (amount paid is less than value of amount due for payment in regular statement), where reports and correspondence proved there are variations at millions, which encourages taxpayers to present unbalanced statements in order to evade taxes, and leads to incomplete and inaccurate tax collection (repeated).

- Some taxpayers were given quittance despite there were financial dues attached to them, in addition to clearance vouchers (P) not disclosed in regular statements, which leads to incomplete and inaccurate tax collection (repeated).

- There are tax files closed without final settlement, which amplifies indebtedness recorded in the system in case the amounts are not real, and also helps taxpayers evade tax if the amounts are real (repeated).

- Failure to follow up taxpayer files who closed tax files while they still have stock in possession, which leads to the risk of taxpayers selling/disposing assets or stock without tax vouchers and pay due tax.

- There are cheques received from taxpayers by the name of ‘guarantee cheques’, kept in the cheques safe not recorded in the register or in RMS to document cheques, issuers, beneficiaries and date of receipt. These cheques were originated from cases referred by the Customs Police to ensure that issuers would settle tax affairs, and without taking necessary actions by value added tax department to settle tax files or collect cheques duly, which badly influences due amount collection and helps tax evasion.

III. Revenues & Deductions of Clearance – Clarification (3). Qualifications on Lending (Local Government Entities, Water, Electricity, Re-lending, Clearance Meetings), 2013, clarification (15)

<u>Clearance revenues: audit of clearance (clarification '3') and clearance meetings</u>

The Bureau expressed qualifications on clearance revenues/deductions and lending due to the following reasons:

- Although the Bureau expressed qualifications to follow up procedures of clearance vouchers (P) variations in the final accounts, 2012, MOF failed to take actions necessary to follow up collection and reduce these variations. It was found that follow up procedures to the clearance vouchers (P) variations were poor, where Israelis deducted value unlike the value of voucher disclosed by Palestinian taxpayers to the Palestinian tax department. There were 1292 clearance vouchers (P) in 2013 deducted by Israelis in clearance meetings, unlike value of the voucher disclosed by Palestinian taxpayers to tax departments, which caused deduction of 12,559,525 NIS more than value disclosed in these vouchers, so the amount deducted from clearance revenues to the Treasury was not verified.
- Although the Bureau expressed qualifications to follow up procedures of clearance vouchers (I) variations in the final accounts, 2012, MOF failed to take actions necessary to follow up collection and reduce these variations. It was found that follow up procedures to the Israeli clearance vouchers (I) by value added tax departments were poor, where there were 983 outstanding clearance vouchers (I) with Israelis (14,941,209 NIS) in 2013.
- There is difference between net value added tax revenues in clearance meetings, 2013 and details of clearance vouchers (I) that have been cleared at 6,192,291 NIS to the Treasury. MOF failed to match amounts transferred for value added tax revenues in clearance meetings with details of amounts due for value added tax for cleared vouchers, which caused invalid due amounts to the Treasury.
- The Israeli stamp deposits account was not modified in clarification '3'-clearance revenues in March 2013 meeting- at 108,396 NIS, where this amount was recorded in 'road accident victims/insurance deduction/clearance' by virtue of entry 00/11100000/13/04006 on 24/05/2013, which reduced the Israeli stamp deposits account at the same amount, and amplified the 'road accident victims/insurance deduction/clearance' at the amount above in both clarification '3' (clearance revenues) and clarification '14.1' (goods & services).
- The Israelis uploaded water bill with an amount of 8,267,906 NIS in 2013 as salaries of the civil administration staff, water department, in addition to 982,397 NIS as delay interest, without follow up by Water Authority and MOF to these amounts, with associated increased cost of water, and deducting amounts unduly, so the Treasury lost them and validity/fairness of amounts deducted is questioned.
- The West Bank Water Department and MOF failed to follow up debts of local government entities, subscribers and individuals, which reached 571,785,176 NIS as at 31/12/2013 according to records of the Department. This deprived the Treasury from financial resources generated from water sale to local government entities, subscribers and individuals (repeated).
- Failure to follow up collection of water subscription amounts from Mikorot Company to Palestinian institutions and individuals (fuel stations, hotels, normal Palestinian citizens), who received water directly from the Israeli company, for which

debts are directly deducted from clearance revenues (6,286,554 NIS as at 31/12/2013). MOF and the Department failed to follow up collection of these amounts, which affected accuracy and completion of collection and clearance/water revenues (repeated).

- The Israelis deducted 240,659,835 NIS from clearance revenues, 2013 for the benefit of Israeli hospitals, without financial claims for these amounts at Ministry of Health, and without an audit of treatment vouchers by any Palestinian entity. MOH does not have lists or financial claims from Israeli hospitals for treatment in 2013 to guarantee provision of treatment as per Palestinian referrals, which questions validity and fairness of amounts deducted (repeated).
- There is not clear basis to calculate clearance deductions for wastewater treatment by Israelis despite qualification expressed by the Bureau, besides failure to follow up these deductions by Water Authority and MOF. It was found that the Israelis deducted 67,706,623 NIS from the Palestinian tax funds during 2013 in order to treat wastewater in the West Bank, including Israeli settlements on Palestinian lands, without clear basis to measure how to calculate amounts deducted, in addition to variation in amounts deducted during 2013, which casts doubts on fairness and authenticity of amounts deducted.
- Although the Bureau expressed qualification to deduction of 3,404,139 NIS under the item ‘agriculture’ in final accounts, 2012, it was found that MOF failed to take necessary actions to coordinate with Ministry of Agriculture to ensure the amount is deducted from clearance revenues, 2013 (3,051,612 NIS) under the item ‘agriculture’ without supporting document that show reasons of deduction and method of calculation.

IV. Sources of Municipal Income (Property Tax, Operational Licenses) / Clarification (4)

The Bureau expressed the following qualifications through the audit of property tax, 2013:

- The Bureau expressed qualifications to property tax revenues, 2013 (14,186,000 NIS) and property tax deposits, 2013 (99,936,000 NIS), as a result of confirmation from property tax department –in response to initial report of the Bureau on final accounts, 2013- that amounts mentioned in reports extracted from the property tax system are not accurate, and that all reports released by the property tax department contain fake and wrong figures.

V. Revenues of Central Budget Institutions / Clarification (5)

1. Revenues of Ministry of National Economy, 2013 / clarification (5)

It was found that fees of precious metal checking/hallmarking, gold checking fees, mining and natural resources revenues, corporate registration fees were not fair, accurate and complete due to the following qualifications:

- Failure to set monthly detailed reports on ministry revenues, and failure to check validity of amounts deposited in bank accounts, where lack of monthly comparisons affects validity and completion of revenues/collection.
- Incomplete collection of examination and hallmarking fees for silver, platinum and rest of precious metals, where hallmarking is only limited to gold.
- Lack of an approved updated database of goldsmiths, which leads to failure to figure out production amounts, and also to the possibility of marketing some products without hall marking, which affects completion of hallmarking fees.
- It was found that balances in bank account where revenues of the ministry are deposited do not match total revenues collected, 2013 as stated in statement given by the ministry, and presented to the Bureau, which leads to inaccurate and invalid recording in the collection system.

2. Revenues of Ministry of Agriculture, veterinary medicine fees, 2013 / clarification (5)

A limitation has been observed in audit scope regarding veterinary medicine fees, 2013 due to the following qualifications:

- The expressed qualifications to opinion regarding proper accounting records of Ministry of Agriculture revenues, 2013 (4,345,983 NIS), due to Ministry of Agriculture failure to provide requirements of accounts audit, and failure to respond to correspondence of the Bureau.
- Ministry of Agriculture failed to undertake a warehouse inventory at general veterinary department, which leads to failure to ensure validity of credits and amounts recorded, and whether they match the actual stock kept in warehouses. This also impedes calculation of due amounts to be deposited in the Treasury account for vaccines and paid veterinary material, which leads to failure to ensure accurate and complete declared value of revenues.
- Amounts that appeared in revenue reports of the 'Green Palestine' project, 2013 did not match amounts recorded in BISAN software and amounts that appeared in the bank slip, besides revenue amounts of the 'Green Palestine' project mentioned in district departments reports that do not match amounts deposited in banks, which does not allow check authenticity, validity

and completion of these revenues. Thus, the Bureau expresses qualification to revenues of the 'Green Palestine' project, 2013.

3. Revenues of Ministry of Telecommunications & Information Technology, postal & stamp fees, 2013 / clarification (5)

The Bureau expressed qualifications to revenues of Ministry of Telecommunications & Information Technology due to the following reasons:

- Failure to calculate license fees (%7) of JAWWAL Mobile Co. and Pal Tel Co. of total telecommunications service operational deals by MOF or MOTIT, where value of license fees was recorded based on correspondence of the two companies to MOF regarding value of due fees, without checking validity of calculations, which leads to invalid amounts recorded and disclosed in final accounts, 2013.
- MOTIT does not have supporting documents for debit commissions collected from some companies, from which it is being paid for invoice collection at post offices, so we could not obtain all necessary approvals from companies, which does not confirm accuracy.
- MOTIT does not have a database for all businesses in telecommunications, which diminishes capacity to follow up, control and collect license fees.

VI. Qualifications on the Reserved Receipts / Clarification (8), Safe Refunds & Cash Refunds / Clarification (17)

The Bureau expressed qualifications to reserved receipts disclosed in clarification (8), and to safe refunds and cash refunds disclosed in clarification (17) in financial statements, 2013 due to the following reasons:

- Although the Ministry of Transport modified clarification (8) regarding reserved receipts, the amount paid in cash from the transport receipts account (%50) reached 27,558,254 NIS, not 27,934,000 NIS as disclosed in clarification (8). Thus, the cash payments were amplified at 375,764 NIS.
- Clearance with municipalities from the account mentioned above reached 2,242,572 NIS, and clearance with South Electricity Company reached 141,243 NIS, not 740,000 NIS as appeared in clarification (8). Thus, clearance from this account has been reduced at 1,825,815 NIS.
- Safe refunds and cash refunds were disclosed at clarification (17) at 27,934,000 NIS, which means that cash refunds were amplified at 375,746 NIS.
- Clearance with municipalities and South Electricity Company was not disclosed in clarification (17) on safe refunds and cash refunds at 2,424,572 NIS and 141,243 NIS respectively, which means that non-cash refunds were reduced at 2,565,815 NIS.

VII. Qualifications on Grants & Assistance / Clarification (9)

The Bureau expressed qualifications to grants and assistance disclosed in clarification (9) due to the following reasons:

- MOF disclosed grants acquired, 2012 as grants for 2013, which affects accuracy and authenticity of financial statements presentation of grants disclosed in clarification (9).
- MOF reduced Ministry of Agriculture grants in 2013 through recording a reverse entry for comparison purposes during 2013, which led to incomplete disclosure of all grants with value less than actual.
- the Bureau expressed qualifications to grants of Ministry of Education and the Palestinian Central Bureau of Statistics, due to record of balance circulated from 2012 in 2013 for grants, not cash, which affects accuracy and authenticity of financial statements.
- MOF failed to disclose grants and assistance from Arab funds to the State of Palestine, 2013. There are not agreements regarding grants from Arab states, and no confirmation letters were received from Arab states about grants and assistance to the State of Palestine, except for one response from the Kuwaiti Fund for Arab Economic Development, which presents balance of grants and assistance with value less than actual.
- Failure to disclose in-kind grants to the State of Palestine in 2013 in the financial statements, which led to incomplete grant accounts, so balances of grants and assistance were shown with value less than actual, which affected authenticity and fairness of financial statements, 2013.
- Payments of the revolving loan from Authority and Natural Resources Authority to the Palestinian Ministry of Health were recorded as a grant for Energy Authority, which amplified grants in clarification (9).
- MOF recorded 850,000 NIS as a grant instead of deposits in 2013, where the Turkish government transferred them to the Treasury account to be transferred to UNRWA account through MOF.

VIII. Qualifications on Salary/Wage Expenses, 2013 / Clarification (13)

The Bureau expressed the following qualifications through audit of salaries and wages:

- Value of social security (civil/military) was not expressed as part of clarification (13) on salaries and wages, 2013, which affects fair presentation of financial statements about actual commitment of MOF to the General Pension Authority, from the government share in 2013. Additionally, cumulative dues to the General Pension Authority were not disclosed as part of financial statements, 2013.
- MOF reduced the 'permanent personnel' account no. 211101 in the advances account no. 13100 by mistake to 8,268,719 NIS, so to close advances of central financial management (external yards), which reduced the 'permanent personnel' account and increased balance of the advances account in the amount above, taking into account that advances account is not disclosed in the financial statements, 2013.

IX. Qualifications on Clarification (18) Regarding the Net Cash Flows of the General Petroleum Authority, 2013

Net cash flows of the General Petroleum Authority was disclosed at 187,259,000 NIS, based on amounts received and spent from bank accounts of the Authority, without clarifying payables and receivables details of these accounts (debits, credits, fuel transport, bank withdrawals, bank commissions/interest. Fuel support grants,…).

X. Qualifications on Public Debt/Borrowing (Internal/External Loans & Overdraft Accounts, Loan Payments) / Clarifications 10, 19, 20 & 22

The Bureau expressed the following qualifications through audit of borrowing (internal/external, loans and overdraft accounts, loan payments):

- Failure to record interest due upon scheduling loans, 2012 but recorded early 2013 due to unavailable budget allocation, which reduced interest of local bank loans in accounting records, 2013.
- Failure to record maturity of external loans interest, which reduced the loans due to external loans account in accounting records, 2013.

XI. Qualifications on Bank Reconciliations & Accounts, 2013

The cash balance of clarifications (22, 24) is unfair due to reasons below:

- MOF disclosed value of cash recorded in clarification (22) in financial statements, 2013 at 1,567,873,000 NIS, total cash controlled by the government was disclosed in the same amount and the cash available at banks was disclosed in the same mentioned amount, without specifying cash value regarding projects, grants and restricted deposits associated with bilateral agreements, whether at the year start or end.
- There are bank accounts for which bank reconciliations were not prepared, which are the consolidated revenue accounts and expense refunds at Bank of Palestine in NIS, USD, Dinar, Euro and Pound.
- MOF recorded revenues on monthly basis in cumulative entry without depending on revenue reports from ministries in question. Depending on bank statement only when recording cumulative entry by MOF without using revenue report from

responsibility center, which leads to inaccurate revenue value as it depends only on the bank statement (repeated).

- The opening balances were uploaded with book balance variation of the bank account in order to match the ledger balance with bank statement, so some revenues and expenses of these bank accounts (with reconciliations) were not accurate.
- There are bank accounts that have approvals but not entered into BISAN. Failure to enter bank accounts into BISAN means failure to prove payments out and amounts in for these accounts in BISAN, which significantly affects total receivables, payables and cash (repeated).
- The Bureau was not provided with files of some bank reconciliations.
- The Bureau expresses qualifications to balance disclosed in clarification (24)/other payments at 107,000 NIS, where this amount does not represent any account in the trial balance.

XII. Qualifications on Preparation, Execution & Supervision of 2013 Budget (Budget Comparisons)

The Bureau expressed qualifications to the budget preparation and enforcement, 2013 due to the following reasons:

- Failure to include some responsibility centers in clarification (1.2.1) and repeated inclusion of some others. Responsibility centers were included in the clarification in terms of entities addressed by the report, despite they are mentioned in the general budget law, 2013, which leads to unclear data regarding entities mentioned in the financial statements, and thus unreliable data.
- The Bureau expressed qualifications to unfair and inaccurate clarifications of budget comparisons due to failure to disclose the development expenses item for each responsibility center in the budget letter, 2013. Failure to disclose development expenses for each responsibility center affected transparency of disclosures and need of responsibility centers to development expenses when the general budget is set, and brought lack of coordination between MOF and responsibility centers, and badly affects budget execution (repeated).

XIII. Qualifications on MOF Compliance with Financial Statements Framework, International Public Sector Accounting Standards (IPSAS), Cash Basis, Compulsory

Qualifications below outline MOF deviations from IPSAS, cash basis:

- Violation to IPSAS 1/4/9, where MOF failed to disclose cash entered out of cash balance as at 31/12/2013, as stated by IPSAS, cash basis.

- MOF failed to observe timetable (6 months) to set and present the financial statements as per IPSAS.

- Failure to disclose cash balances kept by PNA as at 31/12/2013, which are not available for use by PNA.

- Failure to explain variation between budget and actual, as required by standard 1/9/8: 'to explain reasons of variations between the original budget and actual amounts, in order to explain the reasons behind these variations'. Additionally, there has been a failure to observe article 1/9/12 of compulsory standards of IPSAS, which state that 'explaining significant variations between actual amounts and estimated amounts will help users comprehend reasons behind cases of neutrality, and significant deviations from the budget approved for MOF'.

- MOF violated many compulsory IPSAS, cash basis about setting financial statements of the State of Palestine. For example, cases of noncompliance included the following:

  - Compulsory standard 1/4/13 on consistent presentation.
  - Despite that MOF disclosed the reclassification of accounts in accounting policies regarding consistent presentation, 2013, the Bureau expressed qualifications to MOF inability to present estimated financial statements again, against what has been previously (financial statements, 2012). Standard (1/1/19) on comparison information: 'when presentation or classification of financial statements items is modified, the comparison amounts should be reclassified'.

XIV. Qualifications on Expenses Other Than Salaries (Operational Expenses, Transfers Expenses, Capital Expenses), 2013 / Clarification (14)

The Bureau expressed general qualifications on expenses other than salaries/clarification (14):

The Bureau expressed qualifications to expenses other than salaries due to failure to clarify payments at 430,000,000 NIS for liabilities of the Petroleum Authority (from US grant) to Baz Company, for fuel and gas provided, without disclosing the amount stated in the modified financial statements of fiscal year, 2013.

The Bureau expressed qualifications to the spending items below:

<u>Financial reserves account (clarification 14.1)</u>

- Some advances disbursed from financial reserves allocations during 2013 (clarification 14.1) have not been closed, where spending as advances and failure to attach necessary documents might lead to violation of control procedures over spending, under the pretext that the spending is done as an advance, so spending is done illegally. Besides, failure to close them as per corroborating documents until audit date, despite expiry of purpose, impedes checking actual spending for designated purpose. It also means that unclosed advance balances will accumulate, which impedes MOF ability to follow up closing them.

<u>Transfers & aids (clarification 14.2)</u>

- Payments through State of Palestine to local government units were amplified at 68,023,058 NIS, and payments through third parties to local government units were reduced at 316,434 NIS.
- Through audit of modified financial statements, 2013 and despite the failure to include the amount to be modified (606,788,515 NIS) in the error list and preliminary report released by the Bureau, we confirm the calculation non-cash errors in the social security benefits account in the aforementioned value, due to clarification of the difference between debit and credit of the social security benefits cash account and pension salaries account (as cash transactions). Audit of the aforementioned two accounts revealed that cash flow of the social security benefits cash account reached 19,510,981 NIS, and that the pension salaries account reached 314,118,369 NIS, while MOF disclosed cash flows of the two accounts at 940,417,867 NIS in the financial statements.
- Flight tickets for treatment purposes were bought and uploaded to the ‘errands & official trips abroad’ account, which amplified this account and thus led to a wrong accounting classification.

Qualified Opinion

In our opinion, and except for effects of matters mentioned in the 'Qualified Opinion Basis' paragraph above, the financial statements fairly present, all substantial aspects concerned, the financial status of the State of Palestine as at 31/12/2013, and financial performance in 'consolidated receipts and payments statement', 'budget vs. actual comparison list' for the year ended that date according to IPSAS (cash basis).

Emphasis of Matter & Reiteration of a Matter or Case

The Bureau emphasizes the following matters:

1. MOF delayed the release of final accounts, 2013 for four years (as of late 2013), which increased volume and number of subsequent events which the Bureau is supposed to audit as per audit standards.
2. All qualifications-related details mentioned above are presented in detail in the management letter sent to MOF, 23/11/2017, where MOF and different centers of responsibilities were given the legal deadline to respond. The Bureau received their response to observations, where some observations listed in the management letter have not been responded to despite extension to deadline.
3. Limited financial resources and unavailable liquidity of the State of Palestine. We draw attention to that lack of resources and scarce liquidity affect capacity of the State of Palestine to undertake financial duties and responsibilities.
4. We draw reader's attention that position of finance minister has been assumed in 2013 by three: Dr. Nabil Qassis, Dr. Salam Fayyad and H.E. Shukri Besharah. Likewise, the Accountant General position was assumed by Mr. Yusuf Qaddah and Mr. Ahmad es-Sabbah.
5. ISSAI and INTOSAI standards were modified in 2016 in terms of opinion of independent auditor, where this modification applies to financial statements for fiscal years after 15/12/2016.
6. All qualifications-related details mentioned above are presented in detail in the final report 'management letter' sent to MOF, March 2018 besides other qualifications that have not been mentioned in qualifications above.

The observations above are not the reason for our qualifications.

Qualifications on Compliance & Other Legal/Regulatory Criteria

Reporting and compliance with other legal/regulatory criteria:

MOF and State of Palestine shall observe the following laws, regulations and decisions:

- General supplies law 9/1998
- Public debt law 24/2005
- Precious metals hallmarking and control law 5/1998
- Tourism law 45/1965
- Natural resources law 1/199?
- Industry law, 2012
- Traffic law 5/2000
- Decree law 5/2012 on general budget, 2012
- Government works bidding law 6/1999
- Civil service law 4/1998 and amendments
- Budgeting law 7/1998
- Civil defense law 3/1998
- Palestinian financial ordinance for ministries and public entities, 2005 and amendments
- Council of ministers decision 22/2010
- Council of ministers decision (ف.س/و.م/12/92/12/2009) on approving civil defense service fees
- Council of ministers decision 1/1999 on fees of hallmarking, analysis and examination of precious metals and licenses thereto
- Council of ministers decision 17/2008 on licensing regulations issued by the General Petrol Authority
- President decree 18/2007 on fees exemption to citizens in southern provinces
- Council of ministers decision (ف.س/و.م/13/63/01), 2010 on selling government vehicles
- Council of ministers decision 23/2010 on monthly salaries for prisoners
- Council of ministers decision 17/2010 on executive regulations regarding allowances for official errands and courses abroad, Palestinian security forces
- Council of ministers decision 335/2005
- Instructions 11/2012 on tax installments
- Executive regulations of civil service law 2/1999
- Paris Economic Protocols
- General supplies instructions
- Any other laws, regulations, codes or decisions regulating actions of PNA
- Recommendations of the Jerusalem technical committee approved by council of ministers regarding Jerusalem bonus (salaries).

Management Responsibility for Compliance

In addition to set and present the aforementioned financial statements, the management is also responsible for ensuring execution of financial transactions and information contained in the financial statements according to governing legal provisions.

Responsibility of the Bureau

In addition to express opinion on the aforementioned financial statements, our responsibility also includes express opinion on whether financial transactions and information contained in the financial statements are in agreement with governing legal/regulatory rules. This responsibility incorporates undertaking procedures in order to acquire audit evidence whether State of Palestine expenses and revenues have been used in purposes designated by Palestine Legislative Council and council of ministers. Such procedures include substantial risk assessment of non-compliance. We believe that audit evidence we acquired are adequate and proper to provide basis for our qualified opinion.

Basis of Qualified Opinion on Compliance

The Bureau expressed qualifications on compliance with applicable laws, regulations, codes and decisions as below:

I. Qualifications on Compliance

1. General qualifications

1. Release of the financial statements, 2013 was greatly delayed by MOF, where they were presented to the Bureau forty four months after end of fiscal year, 2013, and 32 months after deadline set forth in the Bureau law and the general budget law.
2. Failure to enforce some previous recommendations given by the Bureau, which led to continuous weaknesses and frequent previous practices.
3. Poor control procedures over revenues/fees regarding calculation, record and collection, in addition to lack of effective role played by internal control units regarding regular audit over these revenues/fees.

- MOF failed to take actions necessary to require centers of responsibility to present monthly revenue reports, unlike provisions of article (39) of the Palestinian financial ordinance for ministries and public entities, 2005 and amendments, which require them to set and send monthly revenue reports to the financial controller at the responsibility center, and send these reports to the general accounts department, MOF after necessary audit conducted no later than end of the first week of the following month.
- Unlike provisions of the financial ordinance and amendments, MOF failed to require all centers of responsibility to enter cash grants, assistance and donations into BISAN, and require them to record all grants spent and set bank reconciliations for their bank accounts on monthly basis.

II. Qualifications on Compliance Regarding Tax/Non-Tax Revenues & Receipts, 2013

- Local tax/income tax, clarification (2)

The Bureau reached the following qualifications by end of field work through audit of income tax, 2013:

- Tax installments were granted to taxpayers unlike income tax law and regulations. Thus, failure to observe the income law tax and regulations on presenting written installment application and paying cash deposit no less than %20 of due amount, besides failure to observe installment powers vested in tax offices as per income tax department instructions caused unlawful installment that might lead to default.
- Failure to observe income tax and regulations regarding calculation of installments interest and delay penalties to taxpayers when setting installments, which caused violations to income tax law and failure to use tools set forth in law in order to ensure tax collection within designated deadlines.

- Tax departments granted companies not registered at them quittance without opening tax files and ensuring activities these companies undertake, which leads to failure to follow up the non registered companies and failure to collect tax to the Treasury.

- Failure to complete legal actions against taxpayers with liabilities estimated in absentia or without agreement, and consider these amounts as absolute debts and follow up collection duly, due to no objection by taxpayers to tax estimation, which makes the latter fail to settle files and pay due tax.

- Local tax/income tax, clarification '2' (collection)

1. Poor follow up procedures to bounced and rejected cheques at income tax offices. It was found there were poor follow up to bounced cheques and take legal actions against taxpayers who hold bounced cheques, in addition to services provided to some taxpayers despite these cheques, which caused failure by taxpayers to pay due tax and increased income tax indebtedness, hence revenues were incomplete.
2. Poor follow up procedures to collect taxpayers' indebtedness recorded in the Revenues Management System (RMS), income tax office, which increased indebtedness to taxpayers to the Treasury, thus tax revenues were incomplete.
3. Income tax departments failed to follow up files of taxpayers who ceased presenting tax declarations, and those who do not settle tax files, which increases number of taxpayers who do not settle tax conditions and, in turn, increases tax evasion.

- Local tax/income tax, clarification '2' (tax files estimation)

1. Estimation officers failed to undertake field visits to locations of taxpayers business at least once every three years as per instructions given by general department.
2. There are tax declarations presented by taxpayers that have not been considered and settled by estimation officers with taxpayers, where failure to consider tax declarations presented by taxpayers and follow up settlement with taxpayers during the legal deadline set forth in law undermine control procedures for tax declarations follow up. This lead to tax declarations being kept in the taxpayer file archive and failure to estimate, and badly affects number of files estimated and tax collection.
3. Failure to calculate delay penalty against taxpayers who fail to present tax declarations as per law.
4. Failure to follow up files estimated in absentia or with disagreement (04, 03) and failure to consider objections presented by taxpayers. This caused failure to observe law through following up files of ceasing taxpayers, and poor follow up procedures to objections they present, which made these years outstanding without settlement, and without collecting value of tax due
5. Failure to follow up files of taxpayers who ceased presenting tax declarations despite that files are effective at value added tax department, which increased tax files that have not been settled, thus tax evasion also increased.
6. Signing estimation agreements in blank with taxpayers without filling notification of estimation with value of taxable income.
7. Poor tax file estimation procedures due to lack of corroborating documents for tax file settlement/estimation. Thus, lack of corroborating documents, failure to verify actual revenue items and failure to obtain corroborating documents from taxpayers about expenses caused the absence of clear standards in order to comprehend value of taxable income upon estimation, and inability of the Bureau to recalculate.

Qualifications above constitute violations to the income tax law and related regulations and instructions

- Value added tax / clarification (2.3)

The Bureau reached the following qualifications through the audit of value added tax, customs and excise, 2013:

1. Lack of a procedure guide for the customs and excise department, which leads to personal discretion by staff and intentional/unintentional errors and violations.
2. Lack of control procedures over banderoles printing, which ensure technical specifications and serial numbers. This leads to possible fraud and manipulation, and inability to differentiae counterfeit from original ones issued by MOF, so state revenues will be inaccurate and incomplete.
3. Failure to impose penalties against taxpayers who do not present regular statements within legal deadline, which leads to lack of commitment to present and pay due tax thereto.
4. Some value added tax offices granted taxpayers reservation annulment and exemption from tax file opening in RMS due to practicing commercial actions without registering at tax departments, which increases tax evasion and leads to inability to follow up ceased and unregistered taxpayers.
5. Taxpayers were given clearance vouchers without presenting source deduction certificates issued by income tax department, unlike related instructions.
6. There are bounced cheques worth of more than 13 million NIS at value added tax department, which makes it difficult to collect them as they become legally obsolete.
7. Some value added tax offices received drafts from taxpayers, unlike the Palestinian financial ordinance, 2005 and amendments, besides failure to establish value of these drafts in RMS and lack of follow up thereto.
8. Some taxpayers were given quittance despite there were due debts, bounced cheques and warnings from RMS against their files.
9. Failure to follow up files of taxpayers with cases referred from customs police and warnings.
10. Some taxpayers were given clearance vouchers without presenting source deduction certificates issued by income tax department, which leads to tax evasion and amounts loss from the Treasury.
11. Failure to follow up bounced cheques at value added tax department, and failure to take any legal action in order to collect them
12. There are cheques received from taxpayers but not recorded in books or RMS, which brings the possibility of losing them or difficult retrieval in order to verify security cheque of taxpayer, in addition to poor follow up procedures to files associated with cheques.

III Clearance revenues & deductions / clarification '3', in addition to qualifications on lending (local government entities, water, electricity, re-lending) & clearance meetings 2013 / clarification '15'

The Bureau expressed the following qualifications through the audit of clearance revenues/deductions:

1. Failure by the Israelis to sell water as per price agreed with the West Bank Water Department in 1998.
2. Failure o follow up bounced cheques at the West Bank Water Department as at 31/12/2013 (433 cheques, 14,931,480 NIS), where legal actions have not been taken to collect them from local entities, individuals and subscribers, which amplifies and cumulates indebtedness of the local entities, individuals and subscribers (repeated).
3. Lack of separation of powers for cheque receipt and depositing in banks, registration, set of reconciliations of West Bank Water Department, which leads to possible errors and failure to early discover (repeated).
4. Lack of control procedures over cheque receipt from local government entities, and failure by the West Bank Water Department to use approved special forms to receive cheques from local government entities, which might lead to possible collected cheque mismanagement, and thus affecting accuracy of completion of revenues.

IV. Sources of Municipal Income (Property Tax, Operational Licenses) / Clarification (4)

The Bureau expressed the following qualifications through the audit of property tax, 2013 by date of field work end:

- It was found through the audit of Ramallah and Nablus property tax departments there is not a special register for received and bounced cheques from property taxpayers. It was observed there are cheques received from taxpayers and bounced cheques kept at property tax offices, but do not have special register for numbers and related data, which leads to risk of loss without being able to discover so.
- There are cheues received from property taxpayers kept at property tax offices, and have not been deposited in banks for collection despite their maturity, which leads to lack of control procedures for cheques receipt/deposit, besides legal obsoleteness, lack of demand duly, failure to deposit due amount for the benefit of the Treasury in due time and risk of collection staff's complicity with the one responsible for delay of cheques deposit in bank.
- It was observed through the audit that Ramallah property tax department violated the financial ordinance of ministries and public institutions by receiving cheques not issued by taxpayer in question, which leads to poor control procedures over cheque receipt. Moreover, accepting these cheques increases the risk of accounting errors, so this would badly affects authenticity and accuracy of liability accounts of taxpayers.
- Ramallah property tax department violated the financial ordinance of ministries and public institutions regarding revenues collection, where it was found that taxpayers were allowed to pay due tax in installments.

- Nablus property tax department violated the Palestinian financial ordinance, article 35.6, which states that collection officers shall scrutinize cheques before receipt, and shall ensure that requirements were fulfilled, such as they shall be released to order of receiving department, and shall bear maturity date. It was found there are cheques received but not deposited for collection, and do not have names of beneficiaries and maturity date.

V. Revenues of central budget institutions / clarification (5)

1. Revenues of Ministry of National Economy (gold examination fees, corporate registration fees), 2013 / clarification (5)

The Bureau expressed qualifications on gold examination fees and corporate registration fees due to the following reasons:

1. Failure of the Ministry to keep bank deposit receipts (cash payment vouchers at banks) in serial groups according to number of bank account where deposits are made, and according to sequence of events. Deposit receipts of service are kept in files of the company or entity receiving service, unlike the Palestinian financial ordinance for ministries and public entities, 2005 and amendments, article (8).
2. Failure to set bank reconciliations for these accounts, unlike the Palestinian financial ordinance for ministries and public entities, 2005 and amendments, article 39.3.
3. Poor procedures to regulate deposit receipts distribution to departments and entities in question, Ministry of National Economy, which is a violation to the financial ordinance, article 1.6. It was found that there is not a register for bank receipt books (handed and received), which includes data of books (date of receipt/handing, entity received, serial numbers of books delivered). It was noticed there are cases of receiving/handing to regional and general departments without specifying serial numbers for deposit receipt books handed.
4. Bank deposit receipts for revenues collection was issued by citizens to Ministry of National Economy, where it was found there has been distribution of deposit receipts to law firms, and deposit receipt books were distributed to law firms without specifying handing date, so payment order was not made through the Ministry and its competent department.
5. The precious metals examination and hallmarking fees were only limited to gold, unlike the precious metals hallmarking and control law 5/1998, articles 2 and 3, and unlike the council of ministers decision 1/1999 on fees of hallmarking, analysis and examination of precious metals and licenses thereto. Thus, failure to hallmark all precious metals would lead to mismatch of metal specifications with approved specifications, so consumers would not be protected against precious metals that do not fit approved Palestinian specifications, and incomplete fees collection of silver, platinum and other precious metals, meaning that the Treasury will not receive these revenues.
6. Failure to issue executive regulations for the precious metals hallmarking and control law 5/1998, unlike article (29) therein.

2. Revenues of Ministry of Agriculture (miscellaneous, Green Palestine project, veterinary fees), 2013 / clarification (5)

- The Ministry failed to undertake annual inventory of veterinary vaccines, material and treatments from 2012-2016. The Bureau was not provided with any supporting inventory minutes.
- The Ministry failed to set monthly reports and revenue comparisons, and to ensure distribution of the actual amounts of revenues value in its bank accounts.

3. Revenues of Ministry of Telecommunications & Information Technology (profession practice licenses, telecommunications licenses), 2013 / clarification (5)

- Failure to follow up licenses and correct status of some telecommunications companies and institutions, as per the wired and wireless telecommunications law 3/1996, article 7, and the council of ministers decision 2/2010 on revenue tariffs of frequencies and crafts.

4. Revenues of Ministry of Information (profession practice licenses, media licenses), 2013 / clarification (5)

- Lack of a law or regulations issued by council of ministers to collect license fees.

VI. Qualifications on Salary/Wage Expenses, 2013 'Clarification 13'

The Bureau expressed qualifications on salary/wage expenses due to the following reasons:

1. There are recruitment decisions not signed by the minister of agriculture, unlike provisions of the amended Basic Law 2003, article (7), which vests the minister – or authorized representative- powers to manage all ministry affairs.
2. There are day-to-day basis employment contracts not signed by the competent minister or authorized representative (ministers regarding their ministry and associated departments as per the effective civil service law, article 1), but signed by the department manger where staff in question work.
3. Ministry of Agriculture recruited day-to-day basis staff (part time) in order to avoid procedures set by civil service law in terms of employment procedures, and then they are turned in to full time status according to an internal announcement, under the pretext they are the most eligible and prioritized for employment when the Ministry obtains financial appropriations.
4. Variations were observed in value of wage paid to day-to-day basis staff from value agreed in recruitment contracts, where it was found that some staff were paid monthly salary more than agreed in contracts.
5. External yards advances, central financial department were closed on exceptional basis, without supporting spending documents and approval of the finance minister to recommendation of accounts manager, Ministry of Finance to close advances of the central financial department.

VII. Qualifications on Compliance of Public Debt/Borrowing (Internal/External Loans & Overdraft Accounts, Loan Payments) 'Clarifications 10, 19, 20 & 22'

The Bureau expressed qualifications on borrowing due to the following reasons:

1. Regarding MOF failure to pay loans acquired from the Palestine Monetary Authority, MOF violated decree law 2/2013 on general budget of the fiscal year 2013, which states that ‘borrowing from the insurance and pensions fund or from the monetary authority shall not be resorted to in order to finance enforcement of the general budget’, and violated the Palestinian Monetary Authority law 2/1997, article 36, which states that the amount shall be regarded an advance to be paid within three months that could be renewed for another three months and so on, provided it shall be paid within twelve months.
2. Failure to form the high ministerial committee headed by the minister, with the governor and director general of the Capital Market Authority as members, which undertakes tasks and powers vested in by the public debt law 24/2005. Failure to form this committee violates article (2) of this law.
3. Failure by MOF, public debt department to conduct a study about financial market in 2013, in order to reveal emergency developments and cost of loans and investments as stated by law, unlike the public debt law 24/2005, article 1.5.
4. Government structures failed to provide the public debt department with all debt statements every six months, unlike the public debt law 24/2005, article 6.
5. There are not so far any regulations to organize public debt payment, and there are not executive regulations and subsidiary legislations for the public debt law given by council of ministers, so there are not decisions given by the minister and monetary authority governor to enforce provisions of executive regulations, unlike the public debt law 24/2005, articles 29 and 40.
6. Approval was obtained from council of ministers for some local loans retrospectively in 2013, unlike the public debt law 24/2005, article 11 on borrowing.

VIII. Qualifications on Compliance of Bank Reconciliations & Accounts, 2013

The Bureau expressed qualifications on bank reconciliations and accounts due to the following reasons:

1. There is not approval by the financial controller for some bank reconciliations. It was found there are reconciliations set without the financial controller approval, unlike the financial ordinance for ministries and public entities, 2005 and amendments, articles 140.4 and 85.2.
2. There are expense and zero bank revenue accounts that have been disclosed (minus balance), where an interest was set to their balance, which brought liabilities to the Treasury from outside the budget. This constitutes a violation to the public debt law and the financial ordinance for ministries and public entities, 2005.
3. There are zero bank revenue accounts, for which balances, or part of them, were not transferred daily to the general revenues account to cover the public expenses account, which led to failure to use cash effectively and incur additional cost to the

Treasury due to the current overdraft accounts, which could be reduced if balances of the zero revenue accounts at banks are transferred to the public expenses account on daily basis.

4. There are bank accounts that do not have bank reconciliations set. These accounts are the consolidate
5. ed revenues accounts, expenses refunds to Bank of Palestine (NIS, USD, Dinar, Euro and Pound), and the cumulative revenues account at Bank of Palestine (NIS), unlike the financial ordinance for ministries and public entities, 2005 and amendments, articles 124 and 85.3, which leads to inability to discover the differences and errors between books and bank statements, and, in turn, affect authenticity of accounts.

IX. Qualifications on Expenses Other Than Salaries, 2013 (Operational Expenses, Transfers Expenses, Capital Expenses)

The Bureau expressed qualifications on expenses other than salaries (operational expenses, transfers expenses, capital expenses) due to the following reasons:

Goods & wages (clarification 14.1)

1. MOF spent from allocations of some responsibility centers without approval of authorized representatives, unlike the general budget law, 2013.
2. Spending was done from the rentals account without sufficient supporting documents and legal reference to spend in some cases.

Transfers & aids (clarification 14.2)

1. Part of the financial reserves was spent without all supporting documents, unlike the financial ordinance for ministries and public entities, 2005 and amendments, article 55.1.b (clarification 14.2).
2. Financial reserves allocation was used for expenses not originated by emergency conditions or do not have special nature, unlike the general budget law, 2013, article 9.8.
3. Spending was done from financial reserves allocation without recommendation from the budgeting general manager, unlike decree law 2/2013 on the general budget, article 9.
4. Spending was done without legal basis, which leads to lack of transparency caused by conflict of interest upon spending.
5. Assistance (e.g.: rentals for some staff from Gaza) was spent despite that such spending was suspended by H.E. Mr. President.
6. MOF spent for a great number of institutions and federations in a way violates the financial ordinance for ministries and public entities 43/2005 and amendments, article 66.
7. Some expenses were spent to beneficiaries as advances despite they have previous unclosed advances, unlike the financial ordinance for ministries and public entities 43/2005 and amendments, article 43. For example: support to sacred places, support to NGOs and financial reserves. All of which means that some advances are spent for items not mandatory for the Treasury.

Development expenses (clarification 14.4)

1. MOF spent some advances from the general projects accounts, where some of these advances are exceptionally closed without adequate supporting documents, which makes it impossible to authenticate spending.
2. MOF carried out spending as advances, not current expenses, in 2013 without justifications.
3. MOF spent from allocations of some responsibility centers without approval from authorized representatives, unlike the general budget law, 2013. For example: spending from allocations of Ministry of Social Affairs, Ministry of Education, ….
4. Some expenses were carried out without invitations to tenders or price quotations, unlike the procurement ways set in the general supplies law 9/1998 and respective regulations.

Qualified Opinion on Compliance

With the exception of the aforementioned qualifications, as stated under the '**Basis of Qualified Opinion on Compliance**' title above, all material aspects considered, we see that actions and transactions contained in the financial position of the State of Palestine as at December 31st, 2013, and financial performance in 'the consolidated receipts/payments statement' and the 'budget vs. actual comparison list' for year ended that date are in agreement with governing legal and regulatory rules.

Counselor Eyad Tayyem
Chairman
State Audit & Administrative Control Bureau

Ramallah
09/10/2017