ديوان الرقابة المالية والادارية

الحساب الختامي

Opinion Financial Statements

State Audit Administrative Control Bureau

2012

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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, 2012, summary of significant accounting policies and other explanatory clarifications.

Ministry of Finance 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 adopting 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 ISSAI, which requires that professional conduct rules shall be observed, and that planning and audit shall be 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 measurement for accounting policies adopted, reasonability of accounting estimations and evaluation of total presentation of the financial statements.

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

Basis of Qualified Opinion

Financial Qualifications

I. General Qualifications

1. MOF corrected errors and variations in the final accounts of 2012 at very high substantial values. MOF added clarification ‘25’ to the financial statements of 2012 under 'correction of errors and variations', where total corrections of cash balances, revenues, expenses and deposits reached about 675,157,000 NIS at absolute value (approximately 700 million NIS). These substantial errors -arose from duplicate expenses from previous year, refunds and other matters- form considerable percentage of total budget/spending of PNA, question the credibility of financial statements, 2011-2012, and beg the question about professional due diligence and accurateness of setting financial statements.
2. Inaccurate tying for details of clarification ‘10’ (borrowing from banks), where MOF tied the credit side of local loans account, so some transactions were recorded as they include entries (reschedule previous loans on maturity basis, modifications, exchange rate variation), which leads to inaccurate lending value, duplicate exchange rate variation and reevaluate clarification ‘10’ and then clarification ‘25’, where it is supposed to tie entries that represent loans borrowed during 2012.
3. Inaccurate tying for clarification ‘10’ (borrowing from banks) of bank accounts with minus credit (overdrafts), where opening balances of minus bank accounts were modified at the beginning of 2012, as well as the net modification amount (24,324,000 NIS), without clarifying or expressing these adjustments and respective impacts on final accounts.
4. Errors regarding tying of clarification ‘20’ (loan installments payment), where MOF tied transactions to the credit side of external loans as payments, which are not. They in fact are exchange rate variations and accounting adjustments, where the credit side of external loans has transactions resulted from exchange rate variation and reevaluation adjustment of loan balance at 613,768 NIS. The same wrong processing has been done for local loans, where it was regarded as an exchange rate variation (reevaluation of loan balance) and rescheduling (maturity). Variation between tying and recalculation undertaken by the Bureau reached hundreds of millions of NIS, so repayments were shown at unfair values.
5. Presentation and clarification of final accounts, 2012 did not include accounts of trial balance for which cash transactions were recorded as payments (about 5 million NIS), so the other end of accounting entries of these ledger accounts show bank accounts and transactions. Some examples include Israeli stamp deposits, re-lending the general debt department and road transport deposits.
6. There are cash transactions or revenues in exchange for intermediate accounts that have not been disclosed or included by final accounts, 2012. Examples include opening accounts and opening balances of the national committee grants, which affected cash balances, and caused incomplete and inaccurate register of receipts/payments, and wrong cash balance due to failure to observe double entry.
7. There are accounting errors in advance closing, so spending transactions were recorded without monetary impact, where impacts of which include reduced expenses by cancellation upon advance closing or expenses amplification, and then expenses will not be shown at real values.

8. There is not proper disclosure of effect of cheques to be drawn deposited in banks to cash balances, clarification ‘22’ (cash). This brought cheques with entries that do not meet definition of cash available for use in cash balance.

II. Qualifications on Tax/Non-Tax Revenues & Receipts, 2012

Local Taxes, Clarification ‘2’

- Income tax (tax files valuation)

1. There was not effective follow up to taxpayer files at income tax department, where total files entered into RMS for companies and individuals reached 139,626. Files that have been considered, estimated and followed up were 23,803, or %17 of total files. This percentage is very low and might help tax evasion by taxpayers, which badly affects collection of tax value and completion/accuracy of tax revenues.

- Income tax (deductions)

1. There are substantial variations in terms of deductions from some taxpayers (non-profit organizations), between value of salaries and wages disclosed in deduction lists presented to income tax department by some organizations, and those disclosed in financial report (taxpayer), which might lead to incomplete and inaccurate tax collection.

<u>Value added tax (clarification ‘2’, local taxes)</u>

1. There is not follow up to tax variations between sales 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 with lower value through clearance vouchers (I) greater than procurements disclosed in regular statements, where failure to follow up might lead to tax evasion and incomplete revenues.
2. 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 as at 21/02/2017, so failure to follow up effectively on monthly basis encourages taxpayers to present unbalanced statements in order to evade taxes, which leads to incomplete and inaccurate tax collection.
3. Tax files for taxpayers at value added tax department were closed despite there are financial dues, thus tax collection is incomplete and inaccurate.
4. Some tax files were closed at value added tax department but still active at the income tax department at the same time, which made taxpayers evade reconciling and paying due taxes.
5. There are bounced cheques missing from a value added tax department, where it was not possible to provide the Bureau with their whereabouts and reasons of loss.
6. Poor follow up procedures to clearance vouchers variations (I), deducted by Israelis unlike disclosed value of vouchers to the Palestinian tax departments by Palestinian taxpayers. It was found there were 953 clearance vouchers (P) deducted by Israelis at clearance meetings unlike value disclosed by Palestinians to tax departments, which resulted in deducting 7.054,401 NIS more than value

disclosed, and deducting the amount from clearance revenues to the benefit of the Treasury without verifying them.

7. Poor follow up procedures by value added tax departments to Israeli outstanding clearance vouchers (I) with Israelis (254,584 NIS during 2012).
8. Unusual deductions from value added tax appeared in clearance meetings with Israelis, regarding vouchers belong to operators unregistered in tax database, along with vouchers that have been for more than six months and vouchers for closed files, without clarifying details of vouchers that were deducted from. The Bureau was not provided with procedures followed by MOF to verify authenticity of deductions by type, and this questioned validity of deductions and amounts transferred for net value added tax revenues in clearance meetings.
9. There is difference between net value added tax revenues in clearance meetings, January 2012 and details of clearance vouchers that have been cleared at 2,778,237 NIS. 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.

It should be stated that MOF did not respond to the Bureau observations regarding value added tax and clearance.

Customs & excise / clarification (2)

The Bureau reached the following observations and qualifications through the audit:

- **Collection and cheques 'customs and excise' – clarification '2', local tax, customs**

1. The accounting office, general customs and excise department failed to set bank reconciliations for bank accounts of the general department of value added tax, customs and excise. This has undermined control procedures over bank accounts, and the ability to reveal errors in books and bank records, which affect accuracy and fairness of revenue financial statements.
2. Lack of a record to prove cheques received and bounced at the accounting office, general customs and excise department. Thus, lack of control procedures over cheque proving and registering, plus the risk of unavailable protection for data against deletion or altercation, affected credibility and completion of revenues.
3. Lack of separation of powers at the accounting office, general customs and excise department, which leads to errors that are difficult to disclose and treat at the time they occur.
4. There are 2175 customs declarations for cigarette import and manufacture companies that have not been presented to customs department. Failure to follow up undelivered customs declarations leads to lack of control over imported and manufactured cigarettes, in addition to failure to disclose value of customs declarations for value added tax and income tax, which affects completion and validity of collection.

- **Revenues and deductions of clearance – clarification ‘3’. Qualifications on lending (local government entities, water, electricity, re-lending, clearance meetings), 2012, clarification ‘16’**

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

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

1. MOF failed to record accounting entry of electricity deductions for December 2012 (55,083,338 NIS), which reduced the local government lending item as part of clarification ‘3’ in the financial statements (deductions on behalf of PNA, electricity) as well as direct impact to clarification ‘15’.
2. The Israelis deducted water bought from Israeli companies from clearance revenues with values that do not match clearance voucher thereto. This caused unduly deduction of amounts, so the Treasury forfeited these amounts, which questioned validity and fairness of amounts deducted.
3. Failure to follow up cheques bounced of the West Bank Water Department (523) with total value of 31,191,567 NIS as at 28/12/2016. Thus, failure to take legal actions the Department to collect these cheques from local government entities and subscribers increased indebtedness.
4. Lack of separation of powers for cheque receipt and deposit at banks, registration and bank reconciliations of the West Bank Water Department, which might lead to errors that could not be disclosed when they occur.
5. The West Bank Water Department failed to follow up debts of local government entities, subscribers and individuals, which reached 1,127,420,906 NIS as at 18/12/2016 according to records of the Department. This deprived the Treasury from financial resources generated from water sale to local government entities, subscribers and individuals.
6. Failure to follow up collection of water subscription amounts from Mikorot Company to Palestinian institutions and individuals (fuel stations, hotels, citizens), who received water directly from the Israeli company, for which debts are directly deducted from clearance revenues (6,286,234 NIS as at 31/12/2012). MOF and the Department did not follow up collection of these amounts, which affected accuracy and completion of collection and clearance/water revenues.
7. The Israelis deducted 173,403,525 NIS from clearance revenues, 2012 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 2012 to guarantee provision of treatment as per Palestinian referrals, which questions validity and fairness of amounts deducted.
8. Lack of sufficient follow up to collection of amounts deducted from clearance revenues for electricity bills of local distribution companies. Failure of these companies to pay electricity bills to Israeli regional company, and failure to set restrictions to local companies and local government entities by the government to guarantee payment increase indebtedness and incur the Treasury additional financial loads.
9. MOF or the Palestinian Power Authority failed to ask the Israeli regional company to provide clearance vouchers (I) for electricity bought and details of which. Thus, MOF reliance on the annual statement from Israeli regional company of

total clearance deductions from local government entities impeded authentication of amounts in statements, and authentication that the Israeli company transferred tax value to the Treasury.

10. Failure to follow up collection of amounts owed by individuals, institutions and companies directly provided with electricity from the Israeli regional company, which deducts amounts from clearance revenues. Thus, MOF and Power Authority were unable to follow up collection of amounts deducted from subscribers, which increased indebtedness against individuals and institutions to the Treasury, incurred the latter additional financial loads and deprived it from revenues.
11. There are huge variations at tens of millions between electricity clearance deductions in clearance meetings and statement of the national electricity distribution company for revenues of 2012. MOF and Power Authority did not clarify reasons of variations and details of deduction, and whether the amounts belong to previous debts, penalties against local government entities or any other reason, which casts doubts on value and authenticity of deductions.
12. Cumulative debts against local government entities and electricity companies to the Treasury (1,338,109.675 NIS as at 31/12/2013), which deprives the Treasury from financial resources generated by clearance revenues.
13. There is not clear basis to calculate clearance deductions for wastewater treatment by Israelis. It was found that the Israelis deducted 55,253,360 NIS from the Palestinian tax funds during 2012 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 2012, which casts doubts on fairness and authenticity of amounts deducted.
14. MOF failed to follow up letter of Water Authority regarding value of reimbursements (17,239,375 NIS) due to the link of settlements with wastewater plant of el-Bireh Municipality since 2000. Failure by MOF to communicate with Israelis regarding amounts due as a result of linking wastewater flowing from settlements incurred el-Bireh Municipality additional amounts, besides the Israelis' deduction from clearance revenues for wastewater treatment, and failure to take reciprocal actions (collect amounts for treatment from Israelis).
15. MOF failed to follow up deductions (22 million NIS) on which the Israelis rely as wastewater flowing from Hebron Municipality to Bir al-Saba'a area, taking into account they belong to Israeli settlements and military bases (Kiryat Arba'a, Kharsina), and these deductions were not approved by the joint water committee. Also, there was not any evidence that MOF followed up Water Authority correspondence to follow up unduly deductions done by Israelis as wastewater flowing from Palestinian cities, which is in fact from Israeli settlements in Hebron area.
16. The Israelis deducted 3,404,139 NIS from clearance revenues during 2012 in exchange for veterinary vaccines without explanation or clarification of reasons, volume of vaccines and method based on which the amount has been calculated and deducted from clearance revenues, and without corroborating documents (detailed vouchers, evidence and dates for amounts received).

It should be stated that MOF did not respond to BUREAU observations regarding value added tax and clearance.

- **Municipal revenue sources (property tax, operation licenses) – clarification '4'**

The Bureau reached the following qualifications through audit of property tax, 2012:

1. Property tax department, MOF failed to provide the Bureau with some prerequisites to audit property tax and operation licenses (specified in the scope), where the Bureau was not able to finish the audit of property tax department actions as the latter failed to provide necessary documents asked by virtue of letter 2021 dated 06/12/2016, and letter 1 dated 02/01/2017.
2. MOF recorded entries of property tax transaction fees based on bank statement, where it did not verify reasons of variations between the bank statement and reports of the property tax department, which might lead to inaccurate accounting records and invalid disclosures in financial statements.

Revenues of central budget institutions / clarification (5)
Revenues of Ministry of National Economy, 2012 / clarification (5)

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

1. 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.
2. It was found that balances in bank account where revenues of the ministry are deposited do not match total revenues collected, 2012 as stated in statement given by the ministry, and presented to the Bureau, which leads to inaccurate and invalid recording in the collection system.
3. Failure to match value of monthly revenues deposited in bank with accounting records in BISAN software.

Revenues of Ministry of Agriculture, 2012 / clarification (5)

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

- The Bureau was not able to audit and express opinion regarding veterinary medicine fees and account of the Green Palestine project, mentioned in clarification '5', due to Ministry of Agriculture failure to provide requirements of accounts audit, and failure to respond to correspondence of the Bureau.

III. Qualifications on Grants & Assistance 'Clarification 9'

The Bureau expressed qualifications on grants and assistance in clarification '9' due to the following reasons:

1. MOF clarified grants acquired during 2011 as acquired in 2012, so presentation of respective financial statements declared in clarification '9' was not accurate and fair.

2. Approval letters for grants presented by Arab states were not acquired. MOF asked for them as per letter 44 dated 15/03/2016, where MOF communicated on 28/09/2016 with Palestine's ambassador to the Arab League in order to provide grants from Arab states, but did not communicate with Arab states directly, and no response has been received.
3. Financial statements did not disclose in-kind grants to the State of Palestine in 2012, which might lead to incomplete grant accounts, and therefore declaration of grant balances with value less than actual, affecting validity and fairness of financial statements, 2012.

IV. Qualifications on Salary/Wage Expenses, 2012 'Clarification 13'

The Bureau expressed the following qualifications through the audit of salary/wage expenses:

1. Value of social security (civil, military) has not been disclosed as part of clarification '13', salaries and wages of 2012, which affects fairness and accuracy of financial statements presentation about actual commitment of MOF to the General Pensions Authority from the government's share, 2012. Additionally, accrued benefits for the favor of General Pensions Authority were not disclosed in the financial statements, 2012.

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

The Bureau expressed the following qualifications through the audit of salary/wage expenses: Borrowing (Internal/External Loans & Overdraft Accounts, Loan Payments)

1. Interest due on loan scheduling was not recorded on date of scheduling but at the start of 2013. Besides, record entries for interest due on loans were not set at year end, so entries of installments due in 2012 were recorded in 2013, which increased loan balances, reduced installments due, caused inaccurate recording of currency variation for these loans at year end reduced interest on local bank loans in clarification '19' (interest).
2. Failure to record maturity of external loans interest, which reduced balance of interest due on external loans.

VI. Qualifications on the Whole Amounts Paid for Fuel Marketing, Petrol Derivatives, 2011 ' Clarification 18'

1. Lack of clear accounting policy that shows findings of the General Petrol Authority (accounting basis applied) in the financial statements of final accounts set on cash basis, which affected validity of financial statements and caused unstable presentation of actions. MOF calculated fuel marketing payments as part of final accounts, 2012 in a manner unlike previous years.

2. Regarding calculation of fuel marketing payments, we observed through the review of tying final accounts, 2012 that MOF calculated fuel marketing payments based on difference between fuel bought by the Authority and fuel sales, and considering the variation as cash payments to market fuel in final accounts, which reached 554,910.000 NIS in cash payments statement. Record of procurement and sales in Petrol Authority is recorded on maturity basis. We also observed unstable calculation of and accounting policy (between 2012 and years before) in clarification '18' (fuel marketing payments in financial statements 2011 and 2012). Net receipts and payments was calculated in 2012 and considered fuel marketing payments, whereas this was listed in 2011 in the financial statements with an amount of 12,000,000 NIS (fuel transport expenses), not the net receipts and payments.
3. We would like to draw reader's attention to the fact that fuel bought by the Petrol Authority is paid for from the Authority's bank accounts (not separated from MOF, from which it deposits and withdraws). They are overdraft bank accounts or finance from Islamic banks. Withdrawals from these banks are shown in clarification '10' (bank withdrawals) and clarification '22' (cash).

VII. Qualifications on Bank Reconciliations & Accounts, 2012

Cash balance in clarifications '22, 25' is unfair due to the following reasons:

1. Bank reconciliations for Petrol Authority accounts are not done properly. Term start balance and term end balance were compared with bank statement without clarifying outstanding items (books and cash) in bank reconciliations. Inaccurate bank reconciliations of the Petrol Authority affect accuracy and validity of cash balances.
2. There are bank accounts without bank reconciliations set thereto. These are the bank accounts of consolidated revenues and expenses refunds at Bank of Palestine in NIS, USD, Dinar, Euro and Pound.
3. There is an error in recording the currency variation entry at end of 2012, which led to invalid book balance value of bank accounts.
4. MOF recorded revenues each month in collective entry without depending on revenue reports from ministries in question. Reliance on bank statement only upon recording collective entry of revenues by MOF without relying on revenue reports from centers of responsibility causes inaccurate revenue value, since it just depends on bank statement.
5. Opening balances have been loaded with book balance variation for bank account in order to compare ledger balance with bank statement, so some revenue items and expenses/reconciliations of these bank accounts were inaccurate.
6. Some bank accounts have approvals but not recorded on BISAN, where failure to record bank accounts on BISAN let to inability to prove payments made and their amounts to these accounts on accounting software, which substantially affected total receipts and payments.
7. There are spending vouchers released in 2012 and 2011 but still outstanding until date of audit (2017).
8. There are bank accounts (Cairo-Amman Bank) that have been added to BISAN software, but their transactions were not recorded in bank statement during

2012, which reduced receipts and payments, in addition to poor control procedures over accounts.
9. We have not been provided with files of some bank reconciliations, which is a limitation to audit scope.

VIII. Qualifications on Preparation, Execution & Supervision of 2012 Budget (Budget Comparisons)

- There are inaccurate and unfair budget comparison declarations due to failure to declare development expenses for each responsibility center in budget letter, 2012. Failure to declare development expenses for each responsibility center budget law affected transparency and need of for each responsibility center for development expenses upon setting budget, and due to lack of coordination between MOF and responsibility centers, which badly affected budget execution.

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

Qualifications below outline MOF deviation from IPSAS – cash basis:

1. Violations to accounting standard 1/4/9, where MOF did not declare cash entered from cash balance as at 31/12/2012, in compliance with IPSAS – cash basis.
2. There is not sufficient declaration for nature and reason of errors regarding clarification ‘25’ (correction of errors and variations), and correction itself in the financial statements. MOF corrected errors and variations in financial statements, 2012 ‘consolidated cash receipts and payments statement’ and in clarification ‘25’.
   Standards 1/5, IPSAS (compulsory standards) regarding error correction require declaration in observation attached to financial statements for the following:
   a. Nature of error
   b. Extent of correction
   c. The fact that comparative information was re-presented or it is not possible to do so.
3. MOF did not clarify reasons and details of adjustment and correction regarding each of the following amounts shown in clarification ‘25’ of final accounts set by MOF, 2012:

- Balance difference between financial statements and software-based balance (adjustments to 2011 in agreement with the World Bank) at 12,588,000 NIS.
- Value of opening balances entered on 01/01/2012 instead of 31/12/2012 at 2,844,000 NIS.
- Correction of bank balances at beginning of 2011 at 305,000 NIS.
- Duplicate amount in operational expenses in final accounts, 2011 at 264,995,000 NIS.

- Adjustment of deposit payment amounts (clearance) that have not been accounted for in 2011 statements at 90,193,000 NIS.
- Profits of unachieved losses from currency adjustment variation at 226,611,000 NIS.

4. MOF failed to observe timetable to set and present financial statements as per IPSAS (6 months).
5. Failure to disclose cash balances held by the State of Palestine as at 31/12/2012, which are not available for use by the State.
6. Failure to explain variation between budget and actual, where standard 1/9/8 requires clarifying reasons of variation between original budget and actual amounts, in order to clarify reasons behind these deviations. Additionally, there has been failure to observe article 1/9/12 of compulsory standards, IPSAS that state 'clarify substantial differences between actual amounts and estimated amounts will help users comprehend reasons behind neutrality cases and substantial deviations from budget approved by MOF'.
7. MOF violated many compulsory IPSAS – cash basis for financial statements framework for the State of Palestine. For example, failure to observe the following compulsory standards:

- Compulsory standard 1/4/13 on coordinated presentation.
- Compulsory standard 1/3/24 on payments made by third parties on behalf of the State of Palestine.
- Compulsory standard 1/10/23 on declaring rescheduled or canceled debt.

8. Failure to declare MOF's exemption from external loans at 106.5 million NIS, unlike article 1/10/25, IPSAS – cash basis.

X. Qualifications on Expenses Other Than Salaries (Operational Expenses, Transfers Expenses, Capital Expenses), 2012 'Clarification 14'

The Bureau expressed qualifications on the following spending items:

Financial reserves accounts (clarification 14.1)

1. Some advances disbursed from financial reserves allocations during 2012 (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.

Travel errands & outside official travels (clarification 14.1)

Flight tickets for treatment travels were spent and uploaded to 'travel errands & official travels abroad' account, which amplified it and caused wrong accounting classification.

XI. Observations on Quality of Financial Statements (Numerical & Accounting Errors)

Some of the following qualifications belong to comparative statements, 2011 mentioned in final accounts of 2012:

1. The license receipts amount (clarification '6'), 2011 listed in the 2012 consolidated statement does not match what is listed in the consolidated statement audited 2011, where it was found there is a difference of 1,133,000 NIS. This indicates that adjustments have been made to this item in 2001 consolidated statement after being audited by the Bureau without disclosing why. Furthermore, the 'other payments' amount in clarification '24', 2011 listed in 2012 consolidated statement does not match the 2011 consolidated statement.
2. Value of property tax and operation licenses receipts, 2011 listed in clarification '4' of the consolidated receipts and payments statement, 2012 does not match the value calculated (Bureau recalculation) after audit of this clarification.
3. Value of transport receipts and payments, 2011 listed in clarification '8' in the consolidated cash receipts and payments statement of 2012 does not match value calculated (Bureau recalculation) after audit of this clarification (variation equals 1,360,000 NIS).
4. Value of refunds and deposits payments, 2011 listed in clarification '17' does not match value that appears in the consolidated cash receipts and payments statement, 2012, where value of difference reached 15,597,000 NIS (almost 16 million NIS).
5. Value of fuel marketing payments, 2011 listed in clarification '18' does not match, where it appears in the clarification with 522,112,000 NIS, while the value in the consolidated comparative receipts and payments statement, 2011 appears at 12,000,000 NIS. Thus, value of fuel marketing payments, 2011 in clarification '18' does not match the value appearing in the consolidated cash receipts and payments statement, 2012 in terms of this item. It was found there is a difference at 510,112,000 NIS, which is 12,000,000 NIS according to the audited 2011 statements, and adjusted in comparative column in 2012 statements to 522,112,000 NIS.
6. Failure to attach clarifications to some items of the consolidated cash receipts and payments statement, 2011 which form a comparative year in the 2012 consolidated statement. Comparative clarifications regarding the 2011 final accounts were not published in the 2012 final accounts for clarifications '14.1' (goods and services), '14.2' (referrals and aids), '14.3' (capital expenses) and '14.4' (development expenses).
7. Failure to list share of the State of Palestine in the absentees' properties revenues (%20), 2012 in the fees clarification '5', despite there are evidence to this share in clarification '8' (held receipts).

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 31/12/2012, 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. The 2012 final accounts set by MOF included many errors as a result of failure to practice due professional diligence upon setting financial statements and different clarifications. Errors include, but not limited to, processing 18 payment clarifications, adjusting audited 2011 statements, adding a clarification to correction of previous errors and wrong calculation for the property tax and operation license payments clarification and transport and deposits receipts, 2011.
2. MOF delayed the release of final accounts, 2012 for more than three years (as of late 2012), which increased volume and number of subsequent events which BUREAU si supposed to audit as per audit standards.
3. All clarification-related details mentioned above are presented in detail in the management letter sent to MOF, 29/04/2017, where MOF and different centers of responsibilities were given the legal deadline to respond. BUREAU received their response to observations, where some observations listed in the management letter have not been responded to despite extension to deadline.
4. 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.
5. We draw reader’s attention that position of finance minister has been succeeded in 2012 by Dr. Salam Fayyad and Dr. Nabil Qassis. Likewise, the Accountant General position was assumed by Mr. Yusuf ez-Zummor and Mr. Yusuf Qaddah.
6. 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.

The aforementioned observations are not the reason for our qualification.

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 (م.و/س.ف/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 (م.و/س.ف/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 the State of Palestine
- 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 risk assessment of substantial 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 follows:

I. Qualifications on Compliance

1. General qualifications

1. Release of the financial statements, 2012 was greatly delayed by MOF, where they were presented to the Bureau forty five months after end of fiscal year, 2012, 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.

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

- Local tax/income tax, clarification '2'

The Bureau reached the following qualifications by end of field work through audit of income tax, 2012:

1. 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.
2. Tax installments were granted to taxpayers without documented approval of tax office manager. It was found that some tax offices violated instructions 11/2012 regarding tax installment, in addition to installments for tax due on taxpayers without approval of office manager or general manager to installment applications as per powers vested in them.
3. 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.

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

1. Poor follow up procedures to bounced 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 grant some taxpayers services 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. There were due-to-cash cheques received from taxpayers but not deposited in banks and not entered into RMS, which affected accuracy and completion of

revenues and cash, besides risk of misusing them by collection officer through delayed cheque deposit in banks.

4. There are bounced cheques kept in computer and collection department and income tax offices, which are not paid and entered into RMS. These poor control procedures regarding bounced cheques undermine confirmation of tax revenues accuracy/completion, in addition to risk of cheque loss without evidence to prove this in the system.

5. Balances of bounced cheques in RMS do not match with actual number of bounced cheques in custody of income tax offices, which caused incomplete cash rights and government revenues, in addition to the risk of losing cheques and poor control procedures to follow up bounced cheques.

6. Failure to process bounced cheques for which value was received in cash or with other cheques from RMS, which amplified the number of bounced cheques at income tax department and inaccurate tax liabilities.

7. Income tax office, Bethlehem received Israeli cheques from taxpayers and have not been recorded in RMS, where tax installments through Israeli cheques not given by taxpayers made it difficult to pursue them legally and follow up cheque collection if bounced from banks.

8. Income tax office, Jericho received cheques issued by banks that are being liquidated in the Palestinian territories, which impedes collection of cheque value and brings losses to the Treasury.

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

1. Failure to impose delay penalties against taxpayers who do not present deduction lists and do not deposit due tax in monthly basis.

2. Failure by non-profit organizations to present annual financial statements audited by an auditor, and violating the income tax law 8/2011, article 7.19, so value of salaries/wages disclosed in financial statements does not match what was disclosed and presented through deduction lists of employee salaries at income tax department, in addition to failure to verify whether income of these institutions is generated by non-profit actions.

3. The collection to computer department accepted deduction lists presented by non-profit organizations without auditing lists they present, which led to failure to verify authenticity of calculating value of due tax to be deposited to the Treasury account.

4. Lack of corroborating documents for the disburse of transport allowance and university student exemption, so the Bureau could not verify authenticity of exemptions given, which are stated in the income tax law.

- 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. There are delay penalties that have been calculated to taxpayers but were not entered into RMS, which undermined follow up procedures to collection of penalties, so taxpayers were acquitted and their tax files were settled without collecting penalties imposed against taxpayers.
5. Failure to process and estimate some previous estimated tax years despite that years after were estimated by officer, with previous tax years left without processing or estimation, which leads to failure to collect tax due on taxpayers for non-estimated years.
6. Some files of taxpayers who ceased to present tax declarations to income tax office, Jericho were estimated in absentia (04) at zero value. Estimation officer estimated files of taxpayers who ceased to present tax declarations in absentia based on personal discretion at zero value tax, which disagrees with the basic objective of of estimation in absentia for taxpayers who ceased to present tax declarations.
7. 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.
8. Failure to follow up files of taxpayers who ceased to present 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.
9. There are agreements with taxpayers that are not entered into RMS, in addition to an agreement unsigned by office manager, unapproved by the audit and not entered into RMS.
10. Signing agreement in blank with taxpayers without filling notification of estimation with value of taxable income.
11. Estimation of tax files by some employees who are not estimation officers.
12. 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.

- Income tax, clarification ‘2’ (source deduction & disclaimer)

1. Taxpayers were given disclaimer certificates and source deduction certificates despite they failed to pay and settle due tax, and based on personal pledges from taxpayers, and despite they failed to observe these pledges after obtaining the services. These violations might lead to increase tax evasion and funds lost from the Treasury, especially that disclaimer certificates are among tools that could be used to require taxpayers to settle tax.
2. Income tax office, Jericho failed to use application forms to get source deduction or disclaimer, which led to poor control procedures over granting source deduction and disclaimer certificates.

- Income tax, clarification ‘2’ (closed files)

1. Some taxpayer files were closed despite there is not file closing application, tax commitments, failure to settle some tax years and collecting value of tax due before closing files.

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

- Tobacco & liquor excise / clarification '2'

The Bureau reached the following qualifications by end of field work through audit of tobacco and liquor excise, 2012:

1. Lack of approved procedure manual at the excise and tobacco department, which ensures consolidated and regulated actions/procedures, which leads to personal discretions by staff and intentional and unintentional errors/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.

- Excise & Customs – collection & cheques / clarification '2' (local tax-customs)

1. Cheques received from companies are kept in the safe at accounting department, and not deposited into the bank account as stated by the Palestinian financial ordinance.

2. There was a violation against the Palestinian financial ordinance, article (35): the department received cheques from tobacco company in exchange for fees due, without setting receipt voucher, cheque receipt notification or record them in the received cheques register.

3. The general customs, excise and value added tax department, accounting division failed to set receipt voucher or minutes for received cheques receipt from regional value added tax offices, which makes it difficult to verify authenticity of book records of received cheques.

4. Cheques received from companies are kept in the safe at accounting department and not deposited in its bank account as per the Palestinian financial ordinance, hence a violation to article (36) thereto. 897 cheques were kept at the safe of accounting department, general customs, excise and value added tax department, and were not deposited at its bank account, where the cheques officer only deposits the payable cheques in bank at the end of each month according to maturity date, and cashed and not due cheques are not deposited at the bank in the payable cheques account.

5. Lack of control of the excise and tobacco department over tobacco factories. It was found that the department calculated the manufactured tobacco mix tax based on list presented by companies of raw material imported through customs statements, and volume of raw material manufactured, without supervise actions of these factories, verify actual production volumes and verify raw material bought from local market or Israel as per clearance vouchers.

6. Lack of supervision and control over warehouses of cigarette and tobacco mix import companies and tobacco mix factories, hence bringing the risk of invalid calculation of customs variations value, in addition to the risk of storing and monopolizing cigarettes and tobacco mix by companies in order to sell at high prices.

7. Lack of a register of customs cases referred to the excise and tobacco department by the customs police, where this led to failure to verify follow up and close of all cases, plus failure to verify amounts listed in the revenue deposit with value of amounts for cases closed.
8. Failure to undertaken regular inventory of cheques kept at the general customs, excise and value added tax department, accounting division, which leads to poor control procedures over cheque keeping, storing and maintaining, plus losing some of them.
9. Payable cheques are deposited in banks without setting a list approved by senior management for cheques discharged from the accounting department safe and deposited in banks, which makes it difficult to compare cheques deposited in banks with cheques discharged from the safe, thus failure to verify completion.
10. Failure to set list and entry/discharge vouchers for cigarettes and tobacco mix confiscated by the customs police, which causes absence of control procedures and failure to verify volumes kept in warehouses and potentials of using them.

- Value added tax / clarifications '2, 3'

The Bureau reached the following qualifications through the audit of value added tax, 2012 by date of field work end:

1. Cheques that have not been given by taxpayers or given from entities that have nothing to do with tax file were received, which constitutes a violation against the Palestinian financial ordinance (36/6-a). it was found there were bounced cheques that have been received from taxpayers, but not withdrawn from their accounts and given by others.
2. Failure to record delayed regular statements penalties against taxpayers who do not present regular statements within legal term, and failure to follow up their files.
3. Some taxpayers were given quittance despite there were due debts, bounced cheques and warnings from RMS against their files.
4. Failure to follow up files of taxpayers with cases referred from customs police and warnings.
5. Some taxpayers were given clearance voucher (P) despite there were bounced cheques to their names.
6. Taxpayers were given clearance vouchers without presenting source deduction certificates issued by income tax department, which might lead to tax evasion and loss of amounts from the Treasury.
7. There is not anything to prove from viewpoint of the Bureau's auditors that value added tax staff have verified authenticity of zero statements and refund statements before stamping them, which might bring the risk of stamping some statements without verifying them.
8. Failure to follow up bounced cheques at value added tax department, and failure to take any legal action in order to collect them.
9. There are cheques bounced and rejected by the bank for which value has been collected, where they were not processed with RMS, which amplified number and value of bounced cheques on the system, in addition to inaccurate debts to names of taxpayers.
10. 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.

It should be mentioned that MOF has not responded to observations of the Bureau regarding value added tax and clearance

- Clearance revenues & deductions / clarification '3', in addition to qualifications on lending (local government entities, water, electricity, re-lending) & clearance meetings 2012 / 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, 1998.
2. The Israelis uploaded water bill with an amount of 8,694,743 NIS in 2012 as salaries of the civil administration staff, water department and deducting them from clearance revenues without providing the West Bank Water Department with staff number, work nature and value of monthly salary.
3. There are 91 bounced cheques with value of 3,495,568 NIS according to bank statement that are not in the safe of the West Bank Water Department and not recorded in books. Thus, failure to match balances of bounced cheques listed in bank statement with books an actual possession in the safe, besides failure of the Department to justify variations that appeared in the cheque inventory minutes set on 29/12/2016, which brought risk of cheque losing and bouncing without paying out their values.
4. It was found that MOF failed to follow up letters sent from head of Water Authority to MOF on 10/07/2010 and 31/07/2011, regarding correspondence with the Israelis on reimbursements to the State of Palestine at 168,717.419 NIS for violations against water pipes in 'C' areas (Israeli-controlled) as per interim agreement, article 40.24.
5. 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.

- Sources of municipal income (property tax, operational licenses) / clarification (4)

The Bureau expressed the following qualifications through the audit of property tax, 2012 by date of field work end:

1. There are deletions and adjustments in the valuation records set by general property tax department, without clear documenting of staff name who did that and date of deletion/adjustment, in addition to unclear data in records due to multiple deletion/adjustment, which are so many that they impede data reading and tracking.

III Revenues of central budget institutions / clarification (5)

- Revenues of Ministry of National Economy (gold examination fees, corporate registration fees), 2011 / clarification (5)

The Bureau expressed qualifications on gold examination fees, 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 as per number of bank account where deposits are made, and according to sequence of events. Deposit receipts for employment 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 (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, article 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.

IV. Qualifications on Salary/Wage Expenses, 2012 'Clarification 13'

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

1. Disburse the Jerusalem bonus to a school staff in al-Ezaryia, unlike recommendations of the technical committee of the higher Jerusalem committee.
2. There is variation in value and type of Jerusalem bonus disbursed to staff of Dar al-Aytam Industrial School, Jerusalem branch.
3. Jerusalem bonus was disbursed (510 NIS) to heirs without legal basis.
4. Failure to provide the Bureau with the corroborating documents for Jerusalem bonus disbursement for a sample of some government entities.
5. Failure to provide the Bureau with the Jerusalem bonus disbursement decision for staff holding Palestinian IDs at an institution, unlike recommendations of the technical committee of the higher Jerusalem committee.
6. Failure to provide the Bureau with the Jerusalem bonus disbursement decision for staff of the Jerusalem Waqf department, where it was found it is given to staff holding the Palestinian ID, unlike recommendations of the technical committee of the higher Jerusalem committee.
7. There is not a control and supervision over Jerusalem bonus disbursement by General Personnel Council, which brought exceptional decisions to disburse the bonus to some staff groups without legal reference, despite it has been agreed from legal and jurisprudence point of view that exceptions could not be given on a wide scale. This increased expenses as salaries to staff of the State of Palestine.

It should be mentioned that MOF did not respond to observations of the Bureau regarding Jerusalem bonus

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

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

1. 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 (24) of this law.
2. Failure by MOF, public debt department to conduct a study about financial market in 2012, 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.
3. 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.
4. 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, article 40.

5. Approval was obtained from council of ministers for some local loans retrospectively in 2012, unlike the public debt law 24/2005, article 11 on borrowing.
6. MOF granted a guarantee to a company without necessary financial feasibility studies to verify ability to fulfill commitments. This company works in agriculture and it is insolvent, where there has been default to pay loan installments during 2011, 2013 and 2014, and the Treasury had to bear the remaining amount. MOF collected the amount on 05/02/2017, where the public debt department confirmed in its response to the management letter containing the Bureau's observations there is a recommendation from the public debt department at the time not to pay the guarantee.
7. There are special provisions in the loan agreements with banks, and there are variations in the contract conditions at some other banks, which might bring the risk of preferential treatment.

VI. Qualifications on Compliance of Bank Reconciliations & Accounts, 2012

The Bureau expressed qualifications on bank reconciliations 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 commitments to the Treasury from outside the budget. This is 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.

VII. Qualifications on Compliance of Expenses Other Than Salaries (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:

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

1. Spending is done from the financial reserves account for expenses that do not agree with nature of spending; not resulted from emergency conditions that have not been taken into account upon setting the general budget, 2012, unlike the decree law 6/2012 on general budget, article 9.9. It was found through analysis of the financial reserves ledger account that total disbursements reached 14,208,543 NIS, of which there is 10,093,115 NIS as expenses not generated from emergency conditions (%71 of total financial reserves account). Rents, flight tickets, personal travels, social benefits, treatment cost for staff at MOF, some responsibility centers and people with regulatory or government positions. Bonuses for official errands were spent from the financial reserves despite there is an allocation to that end in each of the responsibility centers.
2. Some expenses were spent from the financial reserves without recommendation from budget general manager, unlike the decree law 6/2012 on general budget, article 9.9.
3. Some financial reserves-related expenses were spent without all necessary corroborating documents, unlike the financial ordinance for ministries and public entities, 2005 and amendments, article 55 (1/b), clarification '14.1'.

<u>Errands & official trips abroad account (clarification 14.1)</u>

MOF focused in spending from the errands and official trips abroad account only on institutions and unions, taking into account spending has been done without following regulations to organize and control it. Also, support lists were not approved by council of ministers, and there were not clear criteria in order to know how to allocate amounts for these institutions and unions, with transparency, integrity and fairness guaranteed. There are not clear criteria to determine institutions eligible for government support, unlike the financial ordinance for ministries and public entities 43/2005 and amendments, article (66).

<u>Furniture account (clarification 14.3)</u>

Some disbursements were made without invitations to tenders or quotations, unlike the general supplies law 9/1998 and respective regulations, in terms of failure to invite to tender or quotation, where procurement was done directly.

<u>Land procurement account (clarification 14.4)</u>

- A land was bought for the benefit of a Palestinian university, but was not registered in the name of the Treasury of the State of Palestine. it was registered in the name of the university in question by virtue of an exceptional approval by minister of finance Dr. Salam Fayyad, instead of register in the name of state entities or acquisition for the benefit of third parties.
- Study subsidies were spent from the university contribution account, which caused incorrect classification.

Jerusalem-related expenses account

Spending was done from the Jerusalem-related expenses account in the form of advances, which caused failure to attach necessary corroborating documents, so control procedures for spending were ignored under the pretext this was an advance. This resulted in disbursing some advances that are not obligatory to the Treasury.

Miscellaneous general expenses account (clarification 14.2)

1. Failure to close advances spent during 2012 despite the designated purpose is expired, unlike the financial ordinance for ministries and public entities, 2005 and amendments.
2. An advance for Yasser Arafat Foundation has been exceptionally closed without corroborating documents in exchange for covering expenses of a meeting at the Arab League. It was exceptionally closed by approval of finance minister Dr. Salam Fayyad without any corroborating documents, unlike the financial ordinance for ministries and public entities, 2005 and amendments, article 55 (1/c).
3. Contracting was done directly with some removal companies to load and transport assistance given from Arab states to Gaza Strip, 2012 based on finance minister approval, unlike the general supplies law 9/1998, article 12.
4. There were errors in the accounting guidance (nature of expenses) for some expenses that have been loaded to the 'miscellaneous and general expenses' account, where some disbursements were loaded onto the 'miscellaneous and general expenses' account, despite they are not related to nature of account, besides that some expenses have their own accounts.
5. Spending was done from the 'miscellaneous and general expenses' allocation without recommendation from the budget general manager, unlike the decree law 6/2012, article (11) on the general budget law, 2012.

Social benefits (clarification 14.2)

Benefit bonuses were spent from the social benefit allocations in 2012, and loaded onto responsibility centers without approval from staff authorized to spend in these centers, unlike the financial ordinance for ministries and public entities, 2005 and amendments, article (43).

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, 2012, and financial performance in 'the consolidated receipts/payments statement', the 'budget vs. actual comparison list' for year ended that date are in agreement with governing legal and regulatory rules.

Counselor Eyad Tayyem
President
State Audit & Administrative Control Bureau

Ramallah
27/07/2017