

Accounting procedure and economic activity of Naval Headquarters in 2004

Audit report No. OSII-2-6/05/104 of August 12 2005

Summary

The SAO audited the economic activity in 2004 of Naval Headquarters, which lies in the area of government of the Ministry of Defence and is militarily organised, with the objective to evaluate the legality of Naval Headquarters' economic transactions, organisation of accounting and reporting, and functioning of internal audit systems. Naval Headquarters keeps a centralised accounting over militarily organised institutions Naval Base and Minesweepers Division. At the end of 2004, Naval Headquarters' assets formed EEK 136 million, incl. fixed assets worth EEK 112 million. EEK 96 million was allocated to the headquarters from the state budget in 2004.

Main observations and conclusions

In the functioning of accounting and internal audit systems, the SAO identified significant weaknesses in writing off ship's fuel and recording the ship's repairs in accounting. In the past few years, neither the Ministry of Defence nor the General Staff of Armed Forces has carried out audits of economic activities in Naval Headquarters. The SAO is of the opinion that this was partly possible because neither the Ministry of Defence nor the General Staff of Armed Forces has sufficiently fulfilled their surveillance function established in the Statutes. In other audited activities, the accounting of Naval Headquarters was organised pursuant to general accounting rules and the economic transactions carried out in compliance with relevant valid legislation.

The SAO brings attention to the following weaknesses:

In accounting and internal auditing

- In the SAO's evaluation, Naval Headquarters' control over the ships' fuel consumption was not satisfactory. Expenditure reports were not always checked and approved, nor the fuel consumption's accordance with the distance travelled by ships and the working time of the ships' engines analysed. In some cases the expenditure report was approved by the same person, who compiled it. In the SAO's evaluation, the fuel amounts written off on "Admiral Pitka" were significantly bigger than could be assumed taking into account the travelled distance and the working time of the ship's engines.
- Construction and repair work carried out on "Admiral Pitka" were not sufficiently recorded, as the data of the content, scope and price of specific works was missing from the acceptance of work acts. In the SAO's evaluation, the scope of work performed in constructing the washroom, rest area and steam room (sauna) is not in accordance with the paid sums.
- The plan for accounting policies and procedures needs to be supplemented pursuant to the requirements of the general rules of state accountancy. Commander of Navy has not yet approved the rules.
- No proprietary liability contracts were concluded in Naval Headquarters with persons, who are responsible for the registration and preservation of tangible assets
- The land on which the buildings and structures of Naval Headquarters are situated, has not been transferred to the Naval Headquarters from the Ministry of Defence. This is not in compliance with the principle of business entity established in Accounting Act.
- In many cases the data of state assets register is not in compliance with that of Naval Headquarters. Some of the fixed assets have not been entered into state assets register, some of the fixed assets that have been written off a long time ago still exists in the state assets register, and some of the fixed assets are shown in an incorrect acquisition cost, because repair work has not been added to it. Information on state assets is forwarded to the Ministry of Defence later than required, in turn, the ministry has delayed in forwarding the data to state assets register.
- Several completely decomposed buildings and structures exist and are registered in the Naval Headquarters' main territory, Tööstuse 54. Several buildings and structures are not in use because of their poor situation or the fact that they are not necessary to the headquarters.
- In 2000, the relatives of Admiral Johan Pitka presented the Estonian Navy with a 10.26 ha piece of land and an antique Russian silver coffee-tea set with an approximate value of EEK

1,200,000. The land has not yet been registered in Naval Headquarters or the Ministry of Defence, because it has not been clarified, whose property it is. The set, which, in the evaluation of the SAO, is of cultural value, has not been registered in state assets register.

In legality of economic transactions and financial management

- Naval Headquarters has carried out all the major acquisitions in 2004 pursuant to Public Procurement Act. In one case, no public procurement had been organised, and in five cases no declarations had been submitted to public procurement register.
- Salary guides are established with retroactive date, directives are amended very often and these have been established retroactively. In establishing wages, correct wage rates are not always respected.

Main suggestions

To the Minister of Defence

- Find out the owner of the piece of land presented to Estonian Navy and if it becomes clear that the owner is the state, formalise and register the land as state assets
- Adopt a decision on the completely decomposed buildings and structures situated in the Naval Headquarters' territory, Tõöstuse 54.
- Consider the exhibition of the antique coffee-tea set presented to Estonian Navy in Laidoner's house museum, because the set is of cultural value.
- Submit proper data to state assets register about state assets in Naval Headquarters.
- Develop rules would regulate exactly with who and on what conditions proprietary liability contracts will be concluded.

To the Commander of Naval Headquarters

- Significantly improve internal control on ships over write-off of fuel and spending money on ships' repair works.
 - For that, add a paragraph related to expenditure to the accounting policies and procedures and supplement it according to the requirements of the general rules of state accountancy (i.e. establish exact requirements for checking the documents and appoint persons to be responsible for the expenditure to be necessary, in compliance with the budget, in compliance with the terms and conditions of the contract, based on the principle of frugality, etc.), and establish the accounting policies and procedures.
 - By September 1, 2005 establish an internal audit system for checking the ships' fuel consumption. For that, lay down the maximum level of the ships' fuel consumption, procedures for checking the ships' refuelling, taking stock of fuel residue and checking the expenditure reports for fuel, etc.
- Make a suggestion to the Ministry of Defence and General Staff of Armed Forces to transfer or demolish the buildings that are not in use and are not necessary for the functioning of Naval Headquarters.
- Timely submit to the Ministry of Defence the data subject to registering into state assets register.
- Organise the internal audit system in such a way that the compliance with Public Procurement Act would be ensured. For this, establish the rules of procedure for carrying out procurements smaller than public procurement limits and notifying the state assets register about them, and appoint a person responsible for the organisation of public procurement.
- Amendments to the directives related to wages should be formalised timely and not retroactively.

To the Commander of the Defence Forces

- In the course of a departmental investigation, find out
 - why, when writing off fuel on "Admiral Pitka", significant non-conformities with the ship's travelled distance and working time of the ship's engines were identified,
 - whether it has caused damage to the state.
- Order an expert analysis from a construction supervision company with the objective to find out, whether the scope of construction of the washroom, rest area and steam room (sauna) on "Admiral Pitka" were in accordance with the paid sums.

- We ask the Commander of the Defence Forces to inform the SAO about the results of the implementation of the suggestions. We have forwarded our observations on the above-mentioned subjects to Central Criminal Police.

In a reply to the draft audit report, The Minister of Defence concurred with the suggestions of the SAO and gave an overview of the planned actions.

The Commander of the Defence Forces stated that the Commander of Navy has been given an order to carry out a departmental investigation on the fuel consumption of "Admiral Pitka" and in August, an expert analysis will be carried out over the construction of the sauna in the ship.

The Commander of Navy informed the SAO of the planned steps to be taken to eliminate the weaknesses. Development of procedures and rules has been started in order to monitor the ships' fuel consumption. Accounting policies and procedures were approved on August 8, 2005, and persons responsible for the organisation of public procurement in the navy will be appointed.

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