Structure of internal audit system, organisation of accounting (incl. disclosure of financial information) and legality of transactions in Vormsi Commune in 2004 and 2005

Audit report No. OSV-2-6/06/73 of 9 August 2006

Summary

The purpose of the audit was to assess the conformity of the organisation of accounting in Vormsi Commune with the legislation and instructions regulating the accounting, the conformity of the commune's economic activities with the regulating legislation and functioning of the internal audit system implemented for the purposeful and lawful use of the commune's funds. The audit does not give an assessment to the annual accounts of 2004 and 2005 but lists important observations regarding the organisation of accounting and functioning of the internal audit system as well as the legality of transactions in the audited areas.

In the opinion of the NAO the commune's internal audit system should be improved in order to ensure the legality of activities and avoid important risks, errors and misuse of funds. There are shortcomings in the organisation of accounting of Vormsi Commune which have led to significant errors in financial reports. In several cases both state and commune legislation has not been followed when concluding economic transactions.

Of the audited transaction classes, the NAO did not identify nonconformity with transactions and significant errors in accounting regarding long-term financial investments (holding in AS Haapsalu Veevärk).

Main observations

- There are shortcomings in the commune's internal audit system, among other things the requirements for the disposal of commune's legislation and other documentation and information established in state and commune legislation have not been met. Keeping and disposal of the document register has not been carried out pursuant to the Public Information Act. Also, the accounting policies and procedures of Vormsi Commune Government are not in compliance with the underlying legislation. Additionally, with regard to makng transfers from bank accounts, the so-called principle of the separation of duties as well as requirements for inventories and their recording in accounting have not been respected.
- There are certain shortcomings in the organisation of accounting of Vormsi Commune which have led to significant errors in the accounting of tangible fixed assets and loan claims. The weakness of the accounting of tangible fixed assets can be seen, for instance, in the fact that in the audited period Vormsi Commune Government recorded the building of Hullo canteen, leased on the basis of financial lease contract, in its balance sheet as fixed assets. The shortcomings in the accounting of loan claims lie in the fact that the financial statements of Vormsi Commune Government have not correctly recognised the loan claims assumed from the non-profit association Vormsi Fund, in the amount of 98,000 kroons.
- Vormsi Commune Government has exceeded its competence in adopting decisions on granting the use of the commune's assets and on their transfer. When awarding grants, the Vormsi Commune Government has not acted pursuant to the procedure for the payment of grants established by the Council. Vormsi Commune Mayor has exceeded his competence by purchasing and selling the shares of Hansa Interest Fund and Hansa Money Market Fund and concluding a loan agreement with Hansapank in 2005.

Main proposals

To the Council of Vormsi Commune

- Plan systematic monitoring over the activities of Commune Government and authorities managed by it.
- Assess the conformity of the procedure for the possession, use and disposal of the assets of Vormsi Commune, incl. its competence to adopt decisions, with the commune's actual needs and in the case of nonconformity change said procedure.

To Vormsi Commune Government

- Bring the accounting policies and procedures into conformity with the legislation they are based on and in accounting follow everything established in said policies and procedures and legislation.
- Carry out inventories in required manner and frequency and record the results of the inventories in financial statements.
- Register in document register all documents required by the Public Information Act and disclose the required information regarding the document register, commune's legislation and other required documents and information.

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In a letter of reply to the draft audit report of the NAO, both the Council of Vormsi Commune and Commune Government concurred with the NAO's proposals. The Council of Vormsi Commune considers it relevant to change the out of date procedure for the possession, use and disposal of the assets of Vormsi Commune. According to the letter of reply of Vormsi Commune Government, the Council of Vormsi Commune is preparing a new draft of said procedure.

Letters of reply of the Council of Vormsi Commune and Commune Government have been appended to the audit report.

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