Summary of Session 1. Financial audits of companies owned by local authorities
Three excellent presentations

• Dr. Walter Wallmann: The audit of local authorities’ participations
• Júlia Valastyánne dr. Vízhányó: Audit of companies owned by local governments
• Azat Valeev: Audit of companies with state participation: the experience of the Accounts Chamber of the Republic of Tatarstan
Common topics

• Mandate of the audit organizations
• Companies owned by the local governments constitute a big asset
• Special risk related to these companies.
• Special methodologies developed by the audit organizations
• The advisory activity of the audit organizations
• The utilization of the audit findings
Mandate of the audit organizations

• **Hungary:** – SAO was enabled to audit companies with majority local government ownership by the Act on the SAO since 2011

• **Hessen:** Based on the recommendation of the CoA the Hessian parliament decided on 18 July 2014 to amend the HGO to ensure that the CoA is granted information and inspection rights.

• **But:** In the case of 39 private-law participations of the Hessian cities, the audit rights were only partly granted despite the existence of the legal requirements mentioned.
A special mandate in Tatarstan

- According to the Federal Law «On auditing activities», joint-stock companies are subject to annual mandatory audit by auditing organizations, and audits of state unitary enterprises are carried out on an initiative basis.
- The Law «On the Accounts Chamber of the Republic of Tatarstan» stipulates that executive bodies must send to the Accounts Chamber the reports and conclusions of auditing organizations.
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Companies owned by the local governments constitute a very big asset

- The nominal value of shares owned by the Republic of Tatarstan is 150,5 billion rubles
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Annual volume of **dividends** on the shares owned by the Republic of Tatarstan *(million rubles)*
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1. What are participations of local authorities?

Example: Spin-off ratio of loan liabilities

In relation to the respective ratio, the spin-off ratio describes the part of the overall liabilities that is allocated to the participations.

Source: Own calculations based on the financial statements of the municipalities selected, as of September 2015
2. Particularities which have to be taken into account

Liabilities in the annual financial statements and consolidated financial statements

Example - The city of Hanau: The difference in liabilities was € 451m.

Source: Own calculations based on the holdings' reports and the annual financial statements as of January 2012
Special risk related to these companies.

• Tatarstan: *Creating the annual audit plan is based on the results of risk assessment*

• Hungary: Audits were focused on the most risky areas: asset management, financial status and internal control systems, local government associations
Special methodologies developed by the audit organizations

- The Accounts Chamber of the Republic of Tatarstan created Guidelines on conducting audits of state (municipal) unitary enterprises, joint-stock companies with state (municipal) share in the authorized capitals.
- Integrated approach for conducting audits of companies with state participation: fiscal, compliance and performance audits.
- To facilitate data collection and to identify the most vulnerable areas of activity associated with high risks of violations and shortcoming, 50 special forms were created.
Innovative methods – Hungary

New ways of organising audits: Thematic group audits, complex audits, new methods of sampling and analysing. Thematic group audits enable the audit of local government operations covering the most important areas, enabling comparison in many aspects. These are audits performed on the basis of uniform programmes, the methods applied ensure the efficient performance of the audits.
Analyses for summarizing the findings of the thematic audits (Hungary)

• The “Analysis II. on the experiences of the operation of local government-owned companies” was based on the experiences of the audits conducted between 2011 and 2014 at a total of 106 companies.

• The risks to financial management and operational risks at the companies can be significantly reduced by strengthening the setup and operation of internal controls.

• The analysis showed that the SAO helps local governments and their enterprises the most by focusing on realistic risks, both in its findings and its suggestions.
Advocatory activities of Tatarstan

• The Interdepartmental Coordinating Board on the issues relating to the state financial control
• was established In the Republic of Tatarstan
• Guidelines on the activities of the Audit commissions of joint-stock companies with the share of the republic in the authorized capitals
• Guidelines on improving the state (municipal) property management
Advocatory activities in Hesse

- Participation management shall be an organizational unit in the local authority. Functions: strategic and operational management of holdings, including support of mandate-holders (preparation and follow-up of the representatives delegated to the supervisory board by the local authority).

- The Court of Auditors has recommended this comprehensive approach. This recommendation led to a legislative procedure.

- The consolidated annual financial statements (consolidated financial statements of local authorities) in Hesse were required to be prepared for the first time for the year 2015 by the 30th of September 2016.
Conclusion from Hesse

• Spin-offs that used to be part of the municipal administration must be legally permitted and reasonable from an economic point of view.

• A spin-off is accompanied by a loss of control - also with regard to the risks of the company.

• This also leads to a loss of information for politicians and citizens.

• This loss of control could be reduced by implementing an adequate holding's management, the loss of information could be reduced by implementing consolidated financial statements, extended annual financial audits and information obligations.

• Local authorities should insist on risk-adequate profit distribution
Utilization of audit results 2.

- **Proactive Communication**: SAO News portal, E-Press Conference, best practices seminars

Direct value added:
- internal controls of audited entities/municipalities is better regulated and operated
- goals set by law can be achieved

Indirect value added:
- entities/municipalities not subject to an audit take on the „best practice” → voluntary compliance
- The fact that SAO is strongly committed to audit internal controls
- The dissuasive effect of the number of thematic group audits as a result of risk based selection
Utilisation of audit results 1.

Audit reports are sent to the President, Parliament and Government of the Republic of Tatarstan for making management decisions.
Thank you for your kind attention!