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SUMMARY

of the Audit on the Operation of the Hungarian State Holding Company in 2009 (1013)

In harmony with its legal mandate, the State Audit Office of Hungary (SAO) completed the audit of the 2009 activities of the Hungarian State Holding Company (hereinafter: HSHC). This was the third time that the SAO expressed its opinion on the activities of HSHC.

The aim of the audit was to evaluate if the practice of the property management system and activities was in harmony with the goals stipulated by the legislation, if the institutional system established for state property management and utilisation ensured the efficient functioning of the state assets and the preservation of its values.

The legal regulation of the institutional system established by the Act on State Property proved to be insufficient also in 2009 for the enforcement of the legislative purposes. Basic deficiencies remained in the legal regulation, the decision making processes and the assets' register and there was no impeachment, with the exception of the extraordinary termination of the Chief Executive Officer's employment. No comprehensive legal supervision took place in the course of the 2009 amendment of the individual chapters of the Act on State Property.

The decisions of the ministers of finance, exercising the shareholder's rights were made without considering the primacy of the state interests; former decisions were amended, revoked, repealed; the decision making processes were characterized by the lack of concepts and transparency. In case of significant matters the measures taken by the decision makers in connection with asset management did not serve the purpose of the Act on State Property, were not transparent enough and lacked the necessary effectiveness.

In 2009 the harmony between the analytical records and the general ledger accounting in the accounting and reporting system of the assets entrusted to HSHC, as well as the regulation and practice of the conciliation process were not adequate for monitoring the individual economic transactions/changes in the assets. The chartered accountant refused giving an opinion both in 2008 and 2009 as there were no authentic data available for an opinion on the report. The

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records of HSHC on state assets were not fully comprehensive. The development of the IT system supporting the single assets register was characterized by irregularities and professional errors. The unfavourable contract and the omission of initiating the amendment of the contract resulted in a detriment worth of HUF 72 million and the system has not been functioning ever since.

The accounting value of the assets entrusted to HSHC in 2009 was HUF 12,861 billion. HSHC managed the assets entrusted to it – i.e. with the property, the assets of the National Land Reserves (NLR) and the assets tied up in business associations – without approved medium-term asset utilization strategy. Decisions made at various levels and concerning individual asset elements were difficult to fathom thus the real reasons behind the individual decisions could not be determined. In certain cases (for example the contract of the so-called 'Fradi' football field worth of HUF 1.2 billion) the utilization measures were unfavourable for the state.

In the EU Treaty of Accession in 2003 Hungary was granted the opportunity to supervise its restrictive and prohibitive regulations concerning foreign citizens and legal entities purchasing land in Hungary for seven years that could be extended by another three years. At the end of the seventh year the extension of the moratorium is justified, however, HSHC did not receive any tasks concerning the moratorium in respect of NLR, neither in the regulations, nor in the medium-term asset utilization strategy approved by the Government at the end of 2009, or even in the 2010 asset management plan.

The efficient and expedient asset management of state owned companies was not realized. Decisions aiming at the increase of state ownership shares financed by budgetary funds were not deliberated in 2009 either. The increase of capital in case of MALÉV Co. Ltd. (Hungarian Airlines) and the Bábolna National Stud Farm Ltd (BNSF) all produced deficit. The State Holding Company transferred a loan worth of HUF 800 million to BNSF in the course of the emergency utilization unfoundedly, without concrete calculations. From this amount BNSF paid HUF 365 million to the liquidator, without legal foundation and there is no chance for the return of this amount. The resolutions of those exercising the shareholders' rights published in the course of the preparatory talks concerning the obtainment of majority shares made it impossible to enforce the claim of the Hungarian party concerning the payment of the bank guarantee of the loan that had been announced earlier and was in harmony with the privatization contract. Additionally, they were contrary to the principles stipulated in the Act on State Property. Those exercising the rights of the shareholders validated a bank guarantee worth of EUR 32 million (the equivalent of approx. HUF 9 billion) later. In case of the four priority headquarter building projects – i.e. MÁV Co. Ltd. (Hungarian State Railways), MTV Co. Ltd. (Hungarian Television

Corporation), Hungarian Post Co. Ltd. and the MVM Group (Hungarian Power Companies) – the expected efficiency improvement based on the earlier calculation was not realized; what is more, they resulted additional costs (for example, the maintenance of the unsold HQ buildings of MÁV Co. Ltd. and HSHC). In case of companies functioning with state support it were not only the decisions of the companies but the decisions of those exercising the ownership rights that did not meet the aspect of expediency as, due to the long-term stabile territorial requirements, purchasing a property is more advantageous than renting it. HSHC that earlier bought from MTV Co. Ltd. its former HQ building for HUF 6 billion, sold it for HUF 4.5 million in 2005. Due to the prolonged realization MTV Co. Ltd. paid a rent of HUF 16.22 billion until May 2010 and because of the fixed term contract, it is going to pay an additional amount of HUF 2.2 billion/year for 38 years (calculated on present value), i.e. altogether HUF 83.6 billion.

In the course of its former audits the SAO formulated recommendations. Some of the recommendations were implemented; however, not a single recommendation concerning individual responsibility was realized.

Apart from the utilization of the on-site audit findings, in our 2009 audit report we formulated recommendations for the Minister of National Development to supervise the regulations, establish coherency between the regulations, and to examine the issue of personal responsibility.

The SAO joined the investigations led by the Prosecutor’s Office in case of MALÉV Co. Ltd., the Sukoro real estate swap, the selling of the Moscow property and that of the Bábolna National Stud Farm Co. Ltd. In other cases the SAO informed the Public Prosecutor separately.