



**Summary**  
**of the Audit on the Activities Related to the Exercise of Proprietary**  
**Rights over State Property in 2010 (1128)**

**Objectives and scope of the audit**

The State Audit Office of Hungary (SAO) audited the 2010 activities related to the exercise of proprietary rights over state property in compliance with its legal obligations. During the audit it was assessed, whether the establishment of the new ownership structure and the implementation of legal amendments were in line with the respective regulations; moreover, whether the legal regulation was explicit and sufficient. Special attention was paid to the decision-making system of the Hungarian State Holding Company and to the audit of the financial management of the property it was entrusted with. The audit covered also the utilisation of the findings of the 2010 SAO audit.

As regards the exercise of proprietary rights, the year 2010 brought several significant changes. The owners' decision-making processes in relation to state property, as well as the implementation of these decisions involved two governmental cycles and two different organisational structures. Besides the Hungarian State Holding Company (HSHC) the Hungarian Development Bank (HDB) and the National Land Fund Management Organization (NLFMO) also became managers of state properties.

**Main findings**

Due to the legal amendments, it was necessary for the HSHC to transfer state properties stipulated by law to HDB and NLFMO. The handover-takeover procedure between HSHC and HDB was fully completed by the end of 2010. In case of NLFMO the procedure was much slower as the operational conditions (e.g. headquarters, filling up of the staff) were established by 2011. This was related to the fact that – instead of tendering – NLFMO ensured the cultivation of lands only by short-term contracts of agency.

The amendment of the Act on State Assets in 2010 made it clear that the Minister of National Development is responsible for the management of state property, while the National Asset Management Council – operating independently of HSHC – was dissolved and – with the set-up of the board of directors and a supervisory board – the operational structure of HSHC was modified in compliance with the Act on Business Associations.

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The Act on State Assets and the Act on the National Land Fund do not contain explicit stipulations regarding the exercise of proprietary rights over real estates subject to joint property management with the involvement of HSHC and NLFMO. (The land area belongs to NLFMO, the landed property belongs to HSHC, while a third party is entitled to use it). In case of these properties a law interpretation problem arose in 2010 (it was not clear who is entitled to the revenues resulting from the utilisation of the properties and who should bear the burdens thereof), which hindered the effective operation of the property managers.

HDB started with the comprehensive screening of the 40 companies taken over in 2010 and succeeded in saving roughly HUF 40 million per month by removing the boards of directors and further downsizing. According to the Act on HDB, as a general rule, HDB cannot transfer the proprietary rights of its shares in the 40 companies managed. However, it is possible though, provided that before the transfer HDB consults the entity entitled. The act however does not specify who the entity entitled to the transfer and the consultation is. (Until August 2011 no such transaction took place).

The 2010 legal amendments affected mainly HSHC – as the manager of the overall majority of state property – that recorded assets entrusted to it worth HUF 13,355 billion at the end of 2010. With the amendment of the Act on State Assets in June 2010, a progress could be seen as regards the decision-making process of HSHC – within that, the regulation of tasks, competences and responsibilities. Previously, proprietary rights over state property were exercised by the National Asset Management Council, while it was supervised by the Minister of Finance. Pursuant to the legal amendment, the Minister of National Development supervising state property became entitled to exercise proprietary rights over state property due to the Hungarian State, too. For the year 2010 HSHC did not have either a textual, signed property management plan including detailed stipulations, or an effective property management strategy in place, therefore there were no references when taking decisions. Throughout the operation of the Council until June 2010, HSHC did not put the necessary emphasis on the preservation and economic operation of state property when performing its tasks related to the management of assets entrusted to it. For example, the Council did not take a decision on the transformation of the Museum of Fine Arts ‘public benefit association’ into a non-profit company, therefore the Court of Registration ordered the compulsory final settlement thereof. The conclusion of the quality assurance and the project management contract of the ‘EVEREST project’ were approved before a decision on the framework contract’s fate – whether it will be ceased or remain effective – was taken. In case of MOKÉP-Pannónia Ltd. a piece of real estate was accepted as coverage, even if the sale

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thereof had been already decided upon. The Council did not reminded the REORG Trading and Finance Co. Ltd. – operating at a loss – of its capital settlement obligation; following that – in order to avoid further deficits – HSHC's board of directors decided on the liquidation of the company. HSHC's board of directors operating from the middle of June 2010 aimed to reduce the negative effects of decisions taken in relation to the companies before the second quarter of 2010.

In 2010 HSHC provided a subsidy for the corporate portfolio in the amount of HUF 3.2 billion. Three companies were granted shareholder's loan in the total amount of HUF 18.8 billion, while cash capital increase was implemented also in case of three companies, in the amount of HUF 27.2 billion (a substantial proportion of which affected MALÉV Hungarian Airlines). The total amount of dividends resulting from the corporate portfolio in 2010 was HUF 31.5 billion. In 2010 the Council and the board of directors decided upon free transfer of assets in the total amount of HUF 1,045.8 million, concerning 106 pieces of real estates. In 2010 the number of sales was low. The most significant one was a landed property in Győr purchased by Audi Ltd. for a gross amount of HUF 6,500 million. Throughout the sale the criteria for the public call for proposals were being met continuously and they were completed only after the governmental decision.

The basis for the transparency and efficiency of state property management is a reliable, credible single register of properties. When HSHC was founded, the initial inventory of properties and balance sheets were not complete, consequently, the total amount of properties it was entrusted with could not be ascertained, either. Due to the unregulated data provisions and the lack of and integrated IT system, no up-to-date data base could be extracted from HSHC's 2010 registers. The data cleansing procedures serving as a basis for the set-up of the new recording system (e.g. filtering duplicated entries, cross-checking data with the land registry) accelerated at HSHC. Several working papers had been prepared in relation to the new recording system, however, there is not a detailed and approved professional concept yet.

It is a task of HSHC by law to keep records of the state property in its entirety, which was not the case in 2010. The Act on State Assets does not apply to real estates being property of NLFMO, that is not obliged to provide HSHC with data on its assets. The activation of public road and railway investments representing high asset value was cancelled from 2007, so they were indicated in the ledgers of the state-owned share companies and not in state property records.

The control system of HSHC was amended in the second half of 2010, however the tasks of the control directorate are not fully regulated. The control functions –

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such as internal audit, control activities of the supervisory board and the proprietors – are not divided.

The SAO report prepared in 2010 on the audit of 2009 activities of HSHC formulated 14 recommendations for the Minister of National Development. Out of these recommendations, 4 were effectuated, 7 were in progress and 2 were partly effectuated. The implementation of one of the recommendations was made impossible by legal changes. Internal examinations initiated by the Minister of National Development were either closed (e.g. the repurchase of MALÉV or the completion of the terms of contract in case of the sale of the football pitch of Ferencváros Athletic Club) or still in progress (unfavourable transactions regarding the headquarters of political parties, unauthorised conclusion of contract in case of the Kisalföld Forestry Ltd.) while the procedures initiated by the prosecution and investigation authorities are also carried out. A public prosecution procedure is being carried out in relation to the property management of the Bábolna Group and the sale of the commercial representation office in Moscow. The investigation authority is carrying out an inspection in the case of the Ferencváros football pitch real estate and the 'EVEREST' recording system of state assets. The above procedures were not yet closed in 2011.

### **Recommendations**

SAO recommended the Minister of National Development and the Minister of Rural Development to initiate clear statutory regulations as regards the exercise of proprietary rights over real estates subject to joint property management with the involvement of HSHC and NLFMO; as well as the amendment of the Act on the National Land Fund in relation to data provision obligations, with the aim of meeting the requirements of a single register of properties as stipulated by the Act on State Assets. We also recommended the Minister of National Development to provide for the amendment of the act on HDB, so that the entity entitled to the transfer of proprietary rights and competent in consultations is specified; to provide for the elaboration of the detailed professional (data administration) requirements for the single, credible and integrated register of state properties; as well as to request HSHC to fully regulate the operation of its control system.