



Summary
of the Audit on the Financial Situation of the Local Government of
Town Békéscsaba with County Status (1129)

Relevance of auditing the local governments of towns with county status

The current economic difficulties of Hungary can be attributed mainly to the disorder of public finances in former periods and to the high total debt. The year 2010 demonstrated that part of the risks is not connected to the central budget, but to the local level of public finances. Due to the financial management difficulties, the increase in the cash flow deficit, as well as the dangers resulting from indebtedness in the local government system, the State Audit Office of Hungary decided to audit the financial situation of local governments. The risk analysis carried out by the State Audit Office of Hungary (SAO) showed that firstly the audit of local governments operating at the middle level – mainly those of counties and towns with county status – is reasonable.

The audit objective was to evaluate whether the local governments of towns with county status ensured long-term financial balance and whether the recommendations concerning regularity and expediency to improve the financial balance – made in the course of the former audit of the financial management system – were utilised. The audit was carried out in respect of the years between 2007-2010 and, when possible, we also tried to cover the period until the end of the last quarter before the on-site audit.

The financial equilibrium of the local government of town Békéscsaba with county status

The debt of the local government of town Békéscsaba with county status increased significantly in the audited period. The total debt increased from HUF 1,780 million to HUF 7,973 million between 2007-2010. The current budgetary balance was positive in the years 2007-2010, altogether an operating surplus of HUF 2,968 million was generated. The total cost of the developments completed in the audited period amounted to HUF 10,149 million. The expenditure for the development tasks in progress on 31 December 2010 amounted to HUF 4,784 million, while the amount of the commitments for the period after 2010 was HUF 20,520 million. The planned cost of submitted applications under evaluation was HUF 3,246 million, out of which a cost of HUF 46 million incurred until 2010. The

balance of the cumulative budget was continuously negative, a lack of cumulative resources amounting to altogether HUF 7,020 million evolved between 2007-2010.

The balance of the current and cumulative budget showed a deficit of altogether HUF 4,052 million. The preservation of the budgetary balance could be ensured with the involvement of external resources. In order to manage temporary liquidity problems, current account credit as well as in 2010 wage credit and liquid credit were borrowed. The lack of development resources – besides the utilisation of the accumulated net operating income and residue – was managed by means of long-term development credit and issuance of bonds for development purposes.

The bank liabilities of the local government amounting to HUF 7,973 million at the end of 2010 originated from one bond issuance, the borrowing of six long-term credits, one one-time liquid credit and the current account credit. As a result of these, the local government has to effectuate a capital repayment and interest payment of ¹taken the extent of the interest of the first half of 2011 for a basis. The local government's arrears to suppliers amounted to HUF 543 million at the end of 2010, out of which the amount of overdue arrears was HUF 187 million. Out of the arrears to suppliers, HUF 335 million (62%) was due at the Hospital. HUF 679 million of receivables recorded in the balance sheet and HUF 1,896 of negotiable immovable assets – out of which HUF 41 million is mortgaged in relation to bank liabilities – can be considered for the fulfilment of all the liabilities to be expected in 2011-2013. Following 2014, the expected liability is HUF 34 million and EUR 2.2 million after the long-term credits, while it amounts to CHF 29.4 million after the bonds. For the repayment thereof, the resources to be considered are the own revenues, according to the information of the local government. The operating income accumulated in 2010 did not even cover a repayment obligation of HUF 9 million.

Besides the increase in local government liabilities, the liabilities of companies of qualified majority ownership can also influence the financial balance of the local government. From 2011, the companies have to repay liabilities of HUF 56 million and arrears to suppliers of HUF 79 million.

The amount of the commitments of the local government's development tasks in progress on 31 December 2010 was HUF 20,520 million. As a source for that, EU funds of HUF 13,986 million (68%), national subsidies of HUF 2,083 million

¹HUF 632 million, CHF 2.0 million and EUR 2.4 million in the period 2011-2013,

(10%), bond resources of HUF 2,165 million (11%), credits of HUF 303 million (1%) and own revenues of HUF 1,983 million (10%) were planned to be utilised.

In the years 2007-2010, the local government accounted for a depreciation of HUF 5,995 million after the tangible assets, while it spent only a fraction thereof, HUF 1,931 million (32.2%), on renovation. The local government spent HUF 8,468 million on replacement of assets (reconstruction, renovation) from the cumulative expenditure realised between 2007-2010. The amount spent on the replacement of assets exceeded the accounted depreciation by 41%.

In 2007-2010, the local government showed an expenditure saving of altogether HUF 2,714 million as a result of institutional reorganisation, changes in tasks and austerity measures. 90% (HUF 2,174 million) of the quantified amount of revenue increasing measures was shown at the Mayor's Office. The measures of the local government to reduce expenditure and increase revenues – according to our financial analysis – resulted in a total amount of HUF 4,888 million between 2007-2010, thus improving the financial situation.

The SAO audited the financial management system of the local government as a whole in 2009. Of the recommendations made in the course of the former audit of the financial management system, all of those concerning the improvement of the financial balance were utilised (i.e. 3 recommendations on regularity and one on expediency).

Regarding the financial risks at the local government, it can be concluded that the negative net operating income in 2010, as well as the increase of the daily average current account, liquidity and wage credits, augmented the financial risk. The proportion of voluntary tasks basically did not influence the safety of the operation of the local government. The structure of tasks carried out by business associations is clear, transparent, and it did not increase operational risk. In the audited period, the balance of cumulative revenues and expenditures of the local government showed a deficit, the source of which was ensured by the utilisation of the residue, bond issuance and borrowing. Due to the negative net operating income in 2010, ensuring the coverage of development commitments increases the cumulative risk. The General Assembly decided to involve further external resources in 2011 in order to ensure the coverage for the payments related to the development commitments to be effected in the future, which implies further cumulative risk. The fulfilment risk of bank and other liabilities was increased by the fact that the coverage for the repayment of liabilities due on 31 December 2010 was indicated in own revenues, but the resources thereof were not quantified. The risk can be reduced by the fact that the 2010 receivables (HUF 679 million) and the tangible immovable assets of the local government (HUF 1,896 million) can be utilised, if necessary, for the repayment of debt service.

Consequently, the financial balance of the local government is ensured on the short term.

Recommendations to the Mayor on the improvement of the financial balance

- To take measures for the elaboration of an action plan to restore the financial balance of the operation on the medium term and ensure the long-term sustainability thereof. The action plan should contain the exploration of possibilities increasing revenues, the comprehensive review of the investments in progress, those planned and other expenditure obligations, the overview of the structure of debt service, as well as the review of institutional financial management and structure, and voluntary tasks.
- To present to the General Assembly every half year the current financial situation of the local government and its business associations in qualified majority ownership, as well as a financing plan on the whole scope of liabilities for at least three years with the quantified indication of resources.
- To examine the availability of internal and external resources necessary for the developments in progress and those planned by the local government and from this aspect evaluate the investments of the local government, provide for the inclusion of resources ensuring the operation of facilities established by means of investments in regulations on the budget.

Recommendations to the Town Clerk on the improvement of the financial balance

- To ensure that in the future the proposals on the commitments generating debt contain the resources of repayment, as well as interest rate and foreign exchange risks to be expected. To follow continuously the commitments of business associations in qualified majority ownership and the influence thereof on the local government's liquidity, financial situation and equilibrium.