



Summary
of the Audit on the Financial Situation of the Local Government
of Town Kecskemét with County Status (1138)

Relevance of auditing the local governments of towns with county status

The actual economic difficulties of Hungary can be attributed mainly to the disorder of public finances in former periods and 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 deficit on a cash basis, 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 justified.

The audit objective was to evaluate whether the local governments of towns with county status ensured long-term financial balance, whether the recommendations concerning regularity and expediency aiming to improve the financial balance, made in the course of the former audit of the financial management system were utilised. The audit covered the period of 2007-2010 and, if possible, we also tried to include the period until the last quarter before the on-site audit.

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

In the audited period, the total debt increased significantly, it rose from HUF 4.5 billion to HUF 16.0 billion between 2007-2010, of which the difference due to the change in exchange rates amounted to HUF 4.4 billion. The financial capacity of the local government (net operating income) was of a positive value. Its current budgetary balance (operating income) was positive, the surplus in resources was altogether HUF 6.7 billion. The surplus showed an increasing trend from 2007 to 2008, while it decreased continuously thereafter. The increase from 2007 to 2008 was caused by the growth in the revenues from local business tax, in the revenues and reimbursements from the VAT related to the purchase and sale of real estates and in the budget subsidy, while the significant decrease thereof can

be attributed to the reduction of the same resources. In 2007-2010, the balance of the cumulative budget of the local government was negative, except for 2009. Between 2007-2010, the lack of cumulative resources was altogether HUF 10.1 billion, 75.5% of which emerged in 2007 and 2008. The value of the local government's developments completed in 2007-2010 was HUF 29,613.4 million, and HUF 4,190.7 was spent on the implementation of development tasks in progress. The amount of the commitments related to the local government's development tasks in progress and carried over to the following years was HUF 5,449 million.

The preservation of the budgetary balance could be ensured with the involvement of external resources. The lack of development resources was managed by means of long-term development credits and issuance of bonds for development purposes. The bank liabilities of the local government amounted to HUF 16.0 billion at the end of 2010, of which the liabilities due in Forint amounted to HUF 3.9 billion, and those in foreign currency were CHF 56,443 thousand. The obligations to be expected, arising from bank liabilities (capital, interest and other costs) amount to HUF 4.8 billion and CHF 63,133 thousand from 2011, according to the conditions of the latest interest payment. The local government's arrears to suppliers amounted to HUF 1.1 billion at the end of 2010, of which only 1.9% had been overdue for more than 90 days. By the end of 2010, the local government undertook guarantees in the amount of HUF 12.2 billion for its economic enterprises, which may burden the local government if the economic enterprises do not fulfil their obligations. 90.2% of its liabilities due to the guarantee was linked to the construction of an adventure bath and a swimming pool, realised with leasing. The coverage thereof for 2011 was planned in the 2011 regulation on the budget. As the resource for the repayment of the liabilities to be expected in 2011-2013, the total liabilities at the end of 2010 and the own revenues planned in the 2011 budget can be considered. The resource of the liability to be expected from 2014 is not specified, for the payment thereof the amount of HUF 2.0 billion placed in deposit as bonds after the bond issuance and the tangible immovable assets of the local government can be taken into account. According to the information of the local government, additional resources to be considered are the own revenues of the local government. However, according to the downward trend, the operating income does not cover the fulfilment of the local government's liabilities, which amounted only to HUF 0.6 billion in 2010.

For the development tasks in progress, the local government undertook commitments in the amount of HUF 5.4 billion for the years following 2010, which were planned to be funded from own resources of HUF 3.7 billion, EU and domestic subsidies, as well as from available credits and bonds.

In order to improve the current financial situation, the local government took measures increasing its revenues and reducing its expenditures (lending out real estates, utilising free capacities, reorganising the institution and its tasks resulting in staff cut-backs and other austerity measures). The simultaneous impact of these measures improved its financial situation by HUF 3.3 billion.

In the course of the former SAO audit, no recommendations were formulated aiming at the improvement of the financial balance.

Regarding the financial risks at the local government, it can be concluded that in 2007-2010, the operational risk of the local government was reduced by the positive current budgetary balance and the minimal overdue arrears to suppliers. The local government could counterbalance only partly the set-back of revenues due to central measures by its own measures aiming to increase revenues. The role of economic enterprises in the provision of public utility tasks was dominant, and the tasks not implemented by a budgetary institution of the local government did not increase its operational risk. The cumulative budget of the local government showed a negative financial balance in 2007, 2008 and 2010. The lacking funds were ensured with the utilisation of the residue, borrowing and bond issuance. The coverage (credits, residues of former years originating from bonds, from EU and domestic subsidies, own resources) is available for the payments to be effected in the future, related to the development commitments, therefore it did not imply a risk in the financing of cumulative expenditures.

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, and the specific resources thereof were not determined and quantified. The absolute guarantee undertaken by the local government for its economic enterprises also increased the financial risk. The risk can be reduced by the fact that the tangible immovable assets of the local government can be utilised, if necessary, for the repayment of debt.

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

Recommendations for the Mayor

- 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 planned and those in progress and other expenditure obligations, as well as the overview of the structure of debt service.

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- To present to the General Assembly every half year the current financial situation of the local government and its economic enterprises 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, as well as to present 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.
 - To 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 follow continuously the foreign exchange, interest and repayment risks to be expected in the future and the risks of the off-balance-sheet items (guarantee and contingent liabilities) and to inform the General Assembly at least every half year about the developments thereof.