



**Summary**  
**of the Audit on the Financial Situation of the Local Government**  
**of Town Miskolc with County Status (1139)**

**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 2007-2010 and, where 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 Miskolc with county status**

The debt of the local government increased significantly in the audited period. The total debt increased from HUF 10.9 billion to HUF 32.0 billion between 2007-2010. The current budgetary balance showed a surplus in terms of operating resources of HUF 1.3 billion in 2007 and HUF 0.7 billion in 2008, while it showed a deficit in operating resources of HUF 0.3 billion in 2009 and HUF 1.4 billion in 2010. In the audited period the local government allocated HUF 30.9 billion to the completed developments. HUF 15.9 billion was spent on the implementation of development tasks in progress. The balance of the cumulative budget was continuously negative, resulting in a lack of cumulative resources amounting to altogether HUF 17.4 billion between 2007-2010.

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The preservation of the budgetary balance could be ensured with the involvement of external resources. The deficit in operating resources of 2009-2010 was financed by means of current account and revolving credits. The lack of development resources was managed by means of long-term development credits and issuance of bonds for development purposes.

At the end of 2010, the bank liabilities of the local government amounted to HUF 14.6 billion, EUR 19,524 thousand and CHF 54,043 thousand. The bank liabilities due in Forint consisted of long-term credits of HUF 10.0 billion, current account credits of HUF 2.4 billion and revolving credits of HUF 2.2 billion.

The local government's arrears to suppliers amounted to HUF 2.6 billion at the end of 2010, of which the amount of overdue arrears was HUF 1.8 billion. In the audited period, the local government undertook absolute guarantee in the amount of HUF 6.2 billion for two of its entirely owned economic enterprises. Its liabilities arising from the guarantee decreased to HUF 2.0 billion from April 2011. It did not have any payment obligations due to the guarantees. A further liability of HUF 0.5 billion arose due to the investment completed in the framework of a PPP construction, which resulted in a yearly repayment obligation exceeding HUF 36.0 million to be fulfilled throughout 15 years from 2011. The residue, the resource originating from the collection of receivables and the possible sale of tangible immovable assets provide a cover for the total sum of liabilities. Further bank liabilities due as of 2014 amount to HUF 9.8 billion, CHF 58.7 million and EUR 20.1 million, for the repayment thereof the revenue from the possible sale of the not mortgaged tangible immovable assets can be taken into account.

As a result of the active tendering activity, following the year 2010 the local government undertook commitments in the amount of HUF 15.2 billion, which were planned to be funded from bonds of HUF 2.6 billion, credits of HUF 4.5 billion, by EU subsidies of HUF 7.2 billion and domestic grants of HUF 0.6 billion, as well as from own resources of HUF 0.3 billion.

In order to improve the current financial situation, the local government took measures increasing its revenues and reducing its expenditures (lending out and selling real estates and other assets, increasing fees, augmenting the rate of estate tax, reorganising the institution and its tasks resulting in staff cut-backs, other austerity measures). The simultaneous impact of these measures improved its financial situation by HUF 2.7 billion.

The recommendations concerning regularity and expediency aiming at the improvement of financial balance and made in the course of the former SAO audit had been utilised.

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Regarding the financial risks arising at the local government, it can be concluded that the local government could not offset the revenues lost as a result of central measures with its arrangements to reduce expenditures and increase revenues. In 2009-2010, the operational risk of the local government was increased by the negative net operating income and the significant amount of overdue arrears to suppliers. The operation of the local government could be ensured only with financing difficulties, as it was necessary to borrow current account and revolving credits, as well as to utilise the interest revenues arising from the investment of bond resources. The financing of post 2010 investments is jeopardised by the obligation to ensure own resources and the additional cost of pre-financing EU resources. The long-term bank liabilities of the local government increased, the financing thereof is uncertain in the following three years and in the subsequent years in light of the immovable assets available, to be considered as a significant part of the cover, which resulted in the high risk of the feasibility of liabilities.

Consequently, financial risks jeopardise the financial management of the local government, and immediate measures need to be taken in order to rapidly restore the financial balance and maintain its long-term sustainability.

### **Recommendations for the Mayor**

- To take measures for the elaboration of an action plan to rapidly restore the financial balance of the operation 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.
- 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.
- 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.
- To present to the General Assembly the risks arising from the membership and management of the associations aiming at the development and

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maintenance of the local government, and influencing the financial balance thereof, as well as the measures aiming to reduce these risks.

**Recommendations for the Town Clerk**

- 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), the commitments of economic enterprises in qualified majority ownership and the influence thereof on the local government's liquidity, financial situation and equilibrium, and to inform the General Assembly at least every half year about the developments thereof.
- To ensure that in the future the proposals of the General Assembly on the commitments generating debt contain the resources of repayment, and present the effects of interest rate and foreign exchange risks to be expected at least in the following three years.