

0224 Summary of the audit made on the operation and financial management of the Hungarian State Railways Corp. in 1999 and 2000

In the past decade, the transport of goods by the Hungarian State Railway Corp. (MÁV Rt.) has decreased by 62%, the carriage of passengers by 20%, and the number of railway workers by 45%. The length of railway lines, projected to territorial units, exceeds the EU average by 60.3%, but its technical level is several decades behind the EU average. In 2001, MÁV Rt. transported 159.3 million passengers, and obtained an income equalling to the level of full-fare proceeds from 70.7% of the travelling passengers. 31% of the travellers bought full-fare tickets, while 39.7% travelled on some special discount fare. The part equalling to the amount of discounts was counterbalanced by the state with consumer price subsidies. The subscribed capital of the corporation amounting to HUF 188 billion has not changed since its transformation into a joint stock company in 1993. In 2001 the average number of employees at MÁV was 54,439. The net sales turnover was HUF 187.5 billion, of which the consumer price subsidies amounted to HUF 19.3 billion, and the production subsidy equalled to HUF 50.2 billion.

The SAO presented its first report on the national railway company in October 1995. In summary, it can be stated right at the beginning that the railway company, in spite of a number of steps taken, has not been able to eliminate its most important and characteristic problems of economic management in the period between the two audits.

The purpose of the present audit was to evaluate whether in the years of 1999 and 2000 the organisational and operational systems of the MÁV Rt. ensured the efficient discharge of its duties, and whether it met the requirements of the process of accession to the European Union. The audit was to check how the financial and economic management of the company could be qualified from the point of view of efficiency; furthermore, how the utilisation of the development and consolidation resources provided to it by the state in the period between 1995 and 2001, and how the level of its service providing activity could be rated; whether the Slovenian–Hungarian railway connection was realised and the investment allocations were utilised in accordance with the plans, and whether the findings and proposals of the earlier SAO audits were put to good use.

In the years between 1995 and 2001, the national railway company of the country arrived at the limits of its operational capability at a number of occasions, which was counterbalanced by partial revitalisation by the then prevailing Government. As of 1995, various reform concepts were made regarding the MÁV on a continual basis, and its organisational system was also modified. The prevailing governments regularly dealt with the financial management of the railway company and with the question on state role to be undertaken, but they could not reach a substantive breakthrough. Between 1995 and 2001, the budgetary financing of the MÁV Rt., including the events of revitalisation, exceeded the amount of HUF 655 billion, counted at current prices, nevertheless, the financial management of the company produced ever-increasing losses.

It became necessary to introduce a comprehensive reform to maintain the market position of railway transport and to stabilise and develop the financial management of the railway company. At the end of 1999, the Government approved the substantive elements constituting the comprehensive reform of the MÁV Rt. with the objective of transforming it into

a modern corporate enterprise that adapts to the market conditions flexibly, provides good quality services and operates properly, reliably, transparently, efficiently and in accordance with the expectations of the customers and the railway workers alike. This, however, was not realised, as the necessary state role could not be enforced in the course of budgeting for 2001 and 2002, and because in the meantime the concepts had changed at the supervisory Ministry. The measures aimed at improving efficiency were not implemented either, and in 2001 the EU guidelines were also modified with respect to the railways. In 2001, the Government withdrew its earlier decisions issued in connection with the railway reform, and, in order to meet the obligations following from accession to the EU and in order to improve the competitiveness of the MÁV Rt., formulated new objectives with respect to the railway reform.

In accordance with the provisions of the Act on railways, in February 1995 the first contract was made and entered into between the State of Hungary and MÁV., under which the State of Hungary transferred the assets in exclusive state property to the use of the MÁV. This contract provided, among others, for the public services and the financing of the basic service provisions. The activities and initiatives made between 1998 and 2001 by the Ministry of Transport, Telecommunication and Water Management and its legal successor the Ministry of Transport and Water Management, and by the MÁV Rt. to modify the system of financing and to make it accurate and clear and to renew the contract between the State and MÁV did not lead to results due to the limited budgetary possibilities and to the changes of the government concepts. The Government Decisions remained unfulfilled up until 2002. The existence of the contract between the State and the MÁV, in contrast to its objectives, did not influence the activities of the Hungarian State Railways.

The corporate level total expenses of MÁV in the period between 1999 and 2001 exceeded its total revenues, its losses increased from year to year, and the cost-effectiveness of its management deteriorated continuously. One of the reasons for this was that the officially authorised inland tariff increases and the pace of state subsidy increases, with the exception of the tariff increase in 1999, did not reach the level of actual inflation. In the period between 1999 and 2001, passenger transport qualifying as the basic railway service produced losses, and its budgetary subsidy was not sufficient for it to break even.

The company did not exceed the planned amount of losses in any of the years, and no comprehensive screening was held in its cost management with the aim to explore reserves. In 2000, the overhead costs that could not be charged on the products directly or be transferred increased at a rate twice exceeding the increase of direct costs. The large increase was connected basically to the reform process. For expert activities and tenders HUF 147 million was spent in 1995 and HUF 923 million in 2000. In the case of the contracts made with experts selected to make audits, the filed documents were incomplete, the provisions related to contracting and the keeping of contracts on file, as well as several stipulations of the orders issued by the Director-General on filing were not observed.

The financing of the company, and, within that, the financing of the basic services related to passenger-transport, was determined by the losses arising each year. Although the steps of financial rehabilitation moderated the asset-reducing effects of the losses, they did not alter the fact that the MÁV was not able to pay even the interest charges on the credits that were necessary to ensure safe operation.

Lacking profits and realised depreciation, the company financed its investments and renewals basically from external resources. In the years between 1995 and 2001, the losses

of MÁV without financial rehabilitation exceeded even the accounted amount of depreciation, therefore there was no coverage in the proceeds of the company even for a part of the operational costs; the value of amortisation could not be used for renewing the assets.

The cumulative consequence of the postponement of developments and the insufficient maintenance work necessary to preserve the existing level was the introduction of an increasing measure of speed limits due to reasons of transport safety, as well as the degradation of the good running order of the vehicles and the increase of the maintenance costs.

In the years from 1995 through 2001, the MÁV paid an amount of HUF 180 billion at current prices for railway line investments and renewals, and an amount of HUF 123 billion for entrepreneurial railway investments and renewals, counted at current prices. 74% of the railway line investments were financed from the state budget, 9% from credits drawn by MÁV and 4% from EU subsidies. In the case of the entrepreneurial railways the same proportions were 6%, 69% and 4%.

On the railway line ensuring connection between Slovenia and Hungary, by temporarily opening the railway to traffic in December 2000, regular inland traffic, and in May 2001, regular international traffic started, but technically and financially the investment, contrary to the plans, has not been completed yet.

As the real estate tenancy contracts are not registered centrally, no reliable information is available on the ceded rights limiting the ownership, and the rents are not increased in accordance with inflation either. In some cases the selling price was identical with the recorded value, which was determined as far back as in 1993, at the time MÁV was transformed into a corporation.

The level of service provision by the MÁV Rt. was low in the transport of passengers and goods alike, together with the secondary services, with the exception of the InterCity and the Ro-La services. As a partial result of the quality control system that has been gradually introduced since 1997, some quality indicators (like running according to the schedule) changed favourably primarily in the field of passenger transport.

The activities directed at amending the Act on railways with the aim of solving the questions long awaiting solution in connection with the operation of branch railway lines, and, connected to that, with the development of the regional centres and their authorisation to operate railway lines have not been completed. No market research was made, and no accurate efficiency calculations were prepared in connection with the determination of the cost estimates and income data related to the branch-lines with small traffic.

In addition to utilising the audit findings, we have proposed to the Government that, in addition to taking into account the requirements of accession to the European Union, it should make an overall evaluation of the progress of the railway reform made so far, paying special attention to the institutional, service providing and financing systems, and, furthermore, that it should ensure the consistent implementation of the reform by taking the steps necessary to that end.