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Utilisation of the Hungarian SAO's Work in the Light of Auditing Public Procurements

Summary: In the last two years, the State Audit Office of Hungary has played a major role in uncovering irregularities in public procurements. 30-40 per cent of the public procurement legal remedy cases were initiated on the basis of recommendations provided by the office. As an audit organisation and the initiator of public procurement legal remedy proceedings, the SAO has an insight into the reasons of irregularities. The basis for good public procurement can and must be created by observing the relevant legal regulations regarding the internal control system. Whether public procurement procedures are conducted in the required manner depends on keeping appropriate records, collecting the right data in a targeted way as well as making thorough preparations. If a given organisation does not provide all the sufficient and required information or the information is not available on site, there is a very high risk of irregularities to occur. These risks can be reduced through the effective control of public finances – especially through the internal control system.

Keywords: public procurement legal remedy, State Audit Office of Hungary, internal control system, Public Procurement Authority
JEL codes: H 57, M 49

In 2015 the size of the national public procurement market was HUF 1,931 billion (Public Procurement Authority, 2016), which shows that, if it is compared to the more than HUF 17,000 billion central budget of Hungary, nearly 11 per cent of public funds are spent under public procurement. The primary goal of public procurement proceedings is to ensure transparency, objectivity, equal access and expediency in order to create a practice characterised by responsible spending (OECD, 2015). In 2015 this amount of HUF 1,931 billion was spent in Hungary in 14 thousand public procurement proceedings.

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THE ROLE OF THE SAO IN UNCOVERING PUBLIC PROCUREMENT IRREGULARITIES

The goal of the State Audit Office of Hungary is to contribute, through its audits, to the creation of a regular and efficient operating environment as well as a more effective and efficient management of public funds and public assets (Domokos, 2015; Domokos et. al, 2016). It has a major role in ensuring

that the audits are followed by consequences; therefore, if it uncovers any irregularity in its audits, using the options provided by law it tries to persuade the entities or persons concerned to adopt a law-abiding behaviour (Pályi, 2015; Németh, 2015). The legal grounds for this are provided by Article 1 (5) of Act LXVI of 2011 on the State Audit Office of Hungary (the SAO Act), which stipulates that based on its findings, the SAO may initiate proceedings with the competent authority against the audited entities and the persons responsible. In addition, the SAO Act provides that the SAO may initiate legal remedy procedures if authorised by specific legislation. The authorisation provided for in specific legislation for public procurement is specified in Act CXLIII of 2015 on Public Procurement (hereinafter: the new Act on Public Procurement), although the former act on public procurement, Act CVIII of 2011 (hereinafter: the old Act on Public Procurement) also contained this provision.

On the basis of point b) of Article 152 (1) of the new Act on Public Procurement, an ex officio proceeding of the Public Procurement Arbitration Board may be initiated by the State Audit Office of Hungary on the grounds that it has, in the performance of its duties, learned of any behaviour or default in violation of this Act. Such unlawful conduct or default especially include the unlawful bypass of the procurement procedure; the illegal amendment of contracts concluded as a result of a public procurement procedure; failure to apply the aggregation rules and division into lots as well as failure to meet administrative obligations (preparing the public procurement plan, publication of the notice). The organisations affected by public sector audits are all entities using public funds, and as such, they are all subject to the currently effective public procurement acts. As a result, if the SAO's audit uncovers any violation of public procurement rules and the deadlines for initiating a legal remedy procedure have not yet expired, the SAO will exercise its right to initiate public procurement legal remedies in every case.

Number of public procurement legal remedy proceedings initiated by the SAO and their connections

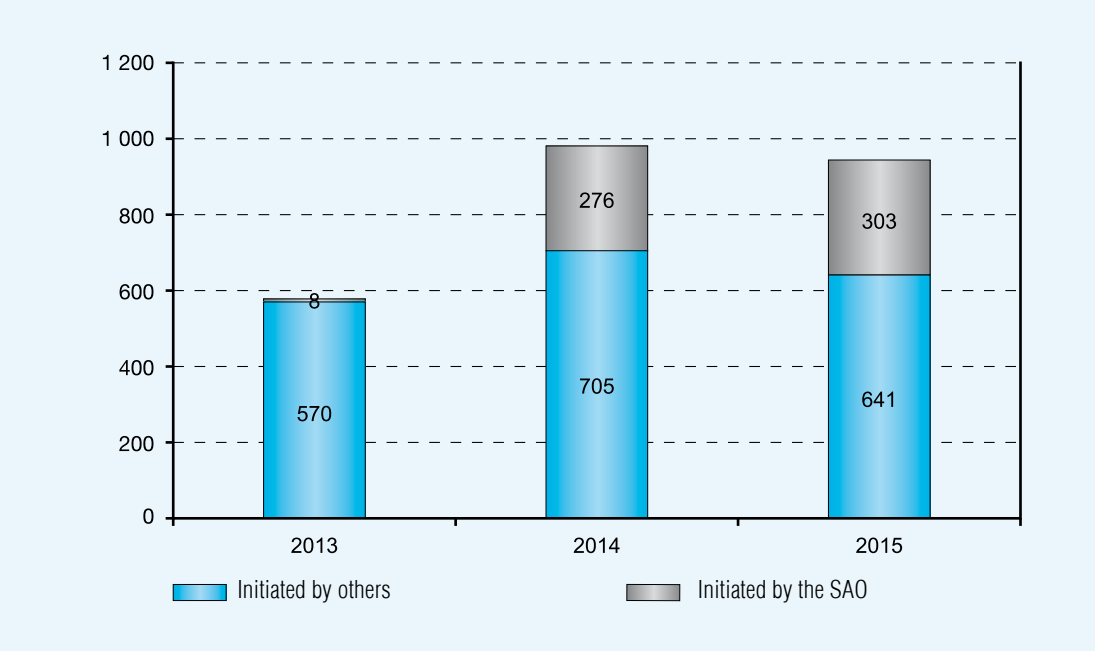
The State Audit Office of Hungary has an important role in uncovering omitted public procurement and applying the appropriate legal consequences. The data that can be accessed from the database on the website of the Public Procurement Authority (hereinafter: the Authority) illustrate the amount of legal remedy actions taken by the SAO (*see Figure 1).* 28 per cent of all public procurement procedures in 2014 and 32 per cent in 2015 were initiated by the SAO.

In order to interpret the data, it is important to know the operation of the Authority[1] and its power to open a procedure. For example, in 2014 there was an organisation that came under the scope of the SAO audits, where the SAO uncovered unlawful bypass of the public procurement proceedings in the amount of over HUF 8 billion and therefore initiated legal remedy at the Public Procurement Arbitration Board. The SAO initiated one single legal remedy procedure and the Public Procurement Arbitration Board divided the irregularities indicated by the SAO into 244 cases on the basis of additional documents – requested in its own powers.

The Authority typically conducts separate examinations in each procedure on the matters of fact that arise in them. In the first round, there were no meaningful examinations in these 244 procedures, and they were concluded with a refusal for further investigations. The reason for this was that according to the arbitration board, the SAO's petition for legal

Figure 1

NUMBER OF PROCEEDINGS CONDUCTED BY THE PUBLIC PROCUREMENT AUTHORITY BROKEN DOWN BY INITIATOR 2013 – 2015



Source: Public Procurement Authority

remedy had been received 30 days after becoming aware of the irregularity in public procurement. The different legal interpretations concerning the time of becoming aware of irregularities will be addressed in the section on extending the deadline for legal remedy. It is important to mention this issue at this point because after the refusal, the SAO made use of the possibility offered by law to contact the President of the Public Procurement Authority, who opened a procedure ex officio in his own authority – after being contacted by the SAO – in 95 cases against the same procurer. Thus, the number of proceedings in 2014 was strongly influenced by the fact that the SAO uncovered a large number of cases involving a high value in which a single audited entity failed to use public procurement, which represented a total of 244+95 legal remedy proceedings as statistical data.

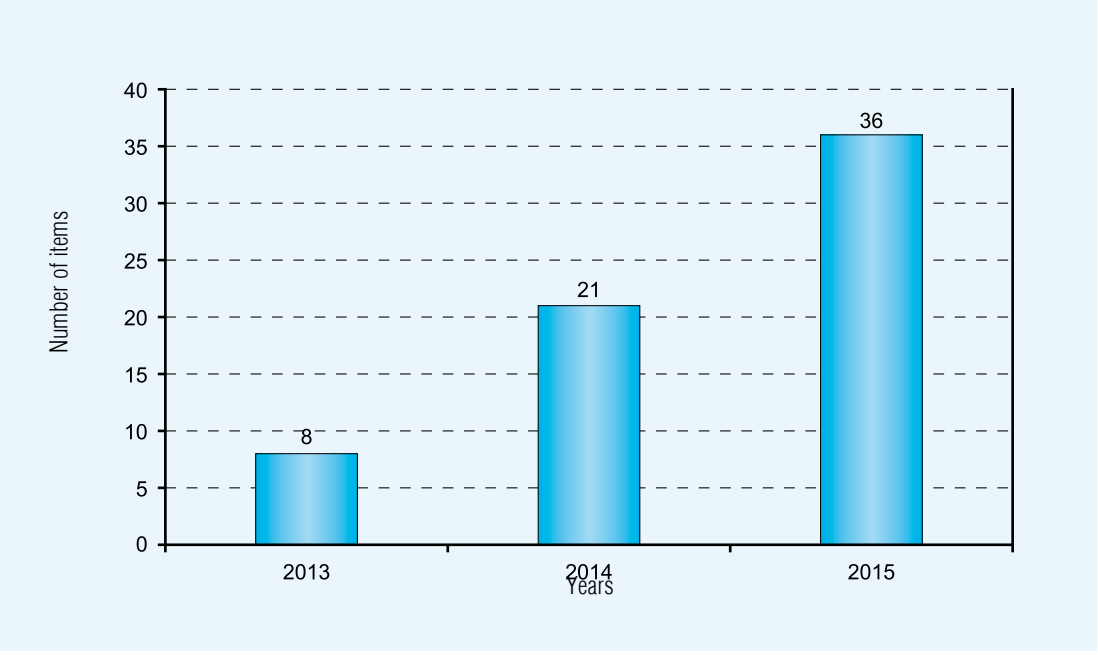
It is important to note that the results of these proceedings justified the SAO's indication: the arbitration board established in its resolution that there was no infringement of law only in 9 cases. In its condemning resolutions, the Public Procurement Arbitration Board not only established the infringement but – in view of the seriousness of the cases – imposed a total of more than HUF 17 million in fines.

Knowing how the Authority works, it is not surprising that the number of legal remedy actions recorded by the SAO are much fewer, although it is increasing. The SAO turned to the Public Procurement Authority in 8 cases in 2013, 21 cases in 2014 and as many as 36 cases in 2015 (*see Figure 2*).

Thus, the difference between the number of ongoing cases and the number of legal remedy proceedings initiated by the SAO is due to the fact that the SAO forwards the infringements

Figure 2

PUBLIC PROCUREMENT LEGAL REMEDY PROCEEDINGS INITIATED BY THE SAO



Source: Information on the professional activity of the State Audit Office of Hungary in 2015

detected by it broken down by audited organisations, while the Authority classifies them according to subject matter. The SAO submits a petition for legal remedy on the basis of the audit documents related to the sample items selected in the audit programme as well as the data and information made available during a particular audit. Since the Public Procurement Arbitration Board has the power to investigate whether any infringement of law occurred and, if justified, to establish such infringement and impose a fine, it is indispensable to uncover any material circumstances (matters of fact) – that may not be known to the SAO – during its procedure. When contacted by the SAO, the arbitration board may call upon the procurer and any other entities concerned (which are not audited by the SAO), in accordance with applicable regulations, to submit a full documentation. As a result, the arbitration board may have more information in a particular legal remedy case than the SAO, the initiator of the proceedings. Accordingly, it investigates a broader scale of data that provides the basis for the proceedings and the rulings established on them.

The audit documents that are available to the SAO and the conclusions that can be derived from them are sufficient to come to a substantiated suspicion of infringement. At the same time, during the legal remedy proceedings, the investigations of the Public Procurement Arbitration Board need to be concluded before the circumstances of the given case can be fully explored, on the basis of which the Public Procurement Arbitration Board can establish whether or not an infringement occurred as suggested by the SAO's indication.

The number of legal remedy cases initiated by the SAO has undeniably increased in the

past three years. The SAO opened legal remedy proceedings in 4.1 per cent of its audits in 2013, 8.9 per cent in 2014 and 16.7 per cent in 2015 because of irregularities in public procurement (in nearly every case because of the failure to conduct a public procurement procedure). It cannot be stressed enough that the primary goal of the audits is not to initiate legal remedy proceedings but to ensure that these audits have a meaningful outcome that can be used as a measure for the utilisation of auditing.

It has been shown above what factors should be taken into account in the statistical data that include the indications of the SAO and the proceedings of the Public Procurement Authority. Next we shall examine the factors that facilitate an increase in efficiency within the SAO.

Focus of the audits

The State Audit Office of Hungary carries out its audits on the basis of a predetermined programme with a clear target. In accordance with the audit programme – as part of evaluating regularity – the appropriate application of public procurement rules should also be audited, which means, for example, the observance of the aggregation rules in the case of procurements with the same subject matter. Thus, although the audits do not primarily focus on an itemised examination of public procurements, it may be incorporated into an audit investigating regularity components.

The effect of topic selection on the number of legal remedy proceedings initiated

The increase in the number of legal remedy proceedings initiated by the SAO in 2014–2015 largely depended on the topic selected by the SAO for audit. According to the analysis prepared on the basis of the data collected in the 2011 integrity survey (Szente, 2012), 23 per cent of the healthcare institutions and 12.5 per cent of the higher education institutions did not apply the provisions of the public procurement law; furthermore, the ratio of contested public procurement applications was extremely high in higher education and also quite significant in healthcare institutions. The analysis rated both groups of institutions as having medium risk. This suggested that if these institutions were to be audited by the SAO or a government audit authority, a significant number of the irregularities might be uncovered.

The data of the integrity survey also demonstrated to the SAO that the structure and operation of the internal control system were not in line with the increasingly higher level of state and EU resources (subsidies and tenders) utilised in the higher education group (Kisgergely et al., 2015). For this reason, the SAO audited all the public higher education institutions in the course of 2014 and 2015. The number of public procurement irregularities uncovered by these audits was quite high. In 2014, 13 out of the 21 legal remedy proceedings initiated by the SAO were conducted during the audit of higher education institutions.

In 2015, when the audit of higher education institutions was concluded and the SAO began to audit the healthcare institutions that belong to the central subsystem (hospitals, special healthcare centres, etc), the number of legal remedy proceedings began to increase in this sector (13 of the total of 36 legal remedy cases were related to institutions with a healthcare profile). Since daily operation and the performance of daily tasks result in a shortage of stocks all the time at these institutions, they need to replace the missing items through purchases and, above a specific limit, through public procurement. Because of the constant utilisation of stocks and the time pressure, these institutions involve a higher risk of irregularities in public procurement.

Extending the deadlines for initiating proceedings

With the amendment of Act CVIII of 2011 on Public Procurement on 1 January 2015, the deadline for legal remedy was extended from 30 days to 60 days after an irregularity becomes known, making it possible to carry out a more in-depth investigation in the course of the audits and take legal remedy action within the deadline. After this amendment, the SAO submitted petitions for legal remedy in connection with irregularities in accordance with the new 60-day deadline. By applying the amendment of the legislation mentioned above, the Office exercised its right to take legal remedy action even in cases in which the public procurement irregularity had occurred before 1 January 2015. The arbitration board rejected the petitions on the grounds that for infringements that had occurred before 1 January 2015 the then effective deadline, that is, 30 days should be used for taking legal remedy action. According to the SAO's position, the regulation pertaining to the deadlines that are open for initiating legal remedy is a procedural rule that should be applied as of 1 January 2015 irrespective of the time of the infringement; therefore, the SAO has 60 days to take legal remedy action.

In order to endorse its position, the State Audit Office of Hungary contested the rulings of the arbitration board in court. In its final ruling, the Metropolitan Court of Public Administration and Labour found the arguments of the SAO to be appropriate and ordered the arbitration board to carry out the proceedings in every case.

The extended deadline was kept in the Act on Public Procurement that became effective as of 1 November 2015. In accordance with this legislation, the State Audit Office of Hungary may initiate legal remedy proceedings within 60 days after an infringement becomes known.

The other important amendment of legislation affected the objective limitation period applying to infringements. Before 31 December 2014, it was possible to take legal remedy action ex officio within three years after an infringement was committed. From 2015, this period of limitation is 5 years if the infringement involved a failure to conduct a public procurement procedure. If the contract is concluded without mandatory public procurement, the five-year period begins at the time the contract is concluded or – if there is no contract – from the time of the first delivery. This provision on the extension of the limitation period significantly affects the work of the SAO as it generally carries out its audits retroactively for a period of 1 to 5 years or in some cases even for a longer period. Therefore, the amendment enabled the SAO to initiate a meaningful procedure for a wider range of cases uncovered by it.

For the calculation of the subjective deadline it is important to address the time of "becoming aware of any irregularity" – since they are interpreted differently by the SAO and the Authority. In the course of the audits carried out by the State Audit Office of Hungary, the audited institution often makes available to the auditors all the documents to be audited at the very beginning of the audit. However, the auditors – going from one sample item to the next – may be able to find an item only several weeks later that suggests an infringement committed in public procurement. It may also be the case that the relevant documents made available are insufficient.

It also needs to be taken into account that several other entities concerned may submit documents to the Public Procurement Arbitration Board responsible for carrying out the legal remedy procedure initiated by the SAO that were not available at the audited organisation at the time of the on-the-spot check, and therefore, the SAO was not able to con-

sider them for the irregularity uncovered by it.

Thus, on the basis of the above, the State Audit Office of Hungary considers the date of an irregularity becoming known when the relevant documents give rise to the suspicion that an infringement in public procurement has occurred.

Legal remedy actions taken by the President of the Public Procurement Authority

Since the mission of the State Audit Office of Hungary is to take effective action in order to protect public funds and public assets, it contacts the president of the Authority in cases where it is unable to exercise its right to open legal remedy proceedings in order for the Authority to investigate a potential infringement within its own powers. The President of the Authority may initiate legal remedy proceedings once they become aware of any irregularity in public procurement. This is provided for both in the old and the new Act on Public Procurement.

The SAO exercised its right to contact the President of the Authority both in 2014 and 2015. Once notified by the SAO, the President of the Authority – after examining documents that were not in the scope of the audit – initiated ex officio proceedings of the arbitration board in 95 cases in 2014 and 7 cases in 2015 within its own powers. In both years there was an extraordinary reason for action. In 2014, the SAO contacted the President of the Authority in order to endorse the legal consequences stemming from several irregularities that occurred repeatedly involving a high value but which were rejected because of the different interpretation of the time of irregularity becoming known. In 2015, the Office notified the President of the Authority in order to endorse the legal consequences following from the irregularities uncovered by it because the petitions submitted within the 60-day deadline were rejected.

Evaluation of the number of legal remedy proceedings

It can be seen from the above how the criteria and legal framework of public procurement influenced the number of public procurement legal remedy proceedings when the audited entities were selected on the basis of risk analysis and the focus questions of the audit programme were identified. This was exacerbated by the ongoing development of the audit indicators of the SAO as a self developing organisation.

As a result of the combined effect of all these factors, the value of purchases involved in the legal remedy proceedings initiated by the State Audit Office of Hungary came close to HUF 12 billion in 2014 and HUF 2.6 billion in 2015. The aggregate amount of public procurement fines imposed in these cases was over HUF 25 million in 2014 and 11 million in 2015. It is easy to see that the size of the amount affected by legal remedy proceedings in public procurement is not necessarily in line with the number of proceedings initiated nor with the total amount of fines imposed. The value of the work performed by the SAO or the performance achieved in one particular year compared to another cannot be expressed by means of one (the number of public procurement proceedings) or another indicator (the amount affected by legal remedy proceedings), nor by a third one (the amount of public procurement fines imposed), although this is one of the areas in the audits of the SAO that is easy to quantify. It must be borne in mind that the SAO is not responsible primarily for uncovering irregularities in public procurement and, therefore, does not identify the focus of its audits in accordance with this; furthermore, the composition of the audited entities may also result in large deviations in data. Nevertheless, the figures amply demonstrate that the SAO can considerably influence the number and the dynamics of legal remedy

proceedings in public procurement, so it has a crucial role in ensuring accountability.

TOOLS ASSISTING THE REGULAR EXECUTION OF PUBLIC PROCUREMENT PROCEEDINGS

The legal framework for public procurement has been in place in Hungary ever since the first public procurement act was adopted in 1995. Still, even two decades have not been enough for the organisations and budgetary institutions to become able to conduct their procurement procedures as contracting authorities in a regular manner. The audits of the SAO point out from time to time that several budgetary institutions suffer from considerable shortfalls in the area of public procurement and that there is much room for improvement as far as the practical application of the rules is concerned.

When performing its audits, the SAO often saw that the audited organisations try to provide various reasons for the failure to meet their public procurement obligations. It is audits, the SAO may not exercise any equity with respect to the audited entities, thus the reason for irregularity is irrelevant from the point of view of the audit findings. The SAO reports contain factual findings and present the irregularities in an objective manner. After presenting the main infringements uncovered in the course of the audits, this paper will present problem-solving proposals that facilitate the creation of "good practice" while responding to the most frequent problems.

Typical infringement of law uncovered by the SAO

According to the Act on Public Procurement, the entities that are obliged to conduct public procurement proceedings include the Ministry, the central purchasing body appointed by the Government, the state, every budgetary institution, public foundations, local governments, local and national minority local governments and partnerships as well as entities conducting procurement procedures on the basis of subsidies. The definition of the range of contracting authorities shows that all the potential users of public funds must conduct public procurement proceedings when the amount involved reaches a particular limit as defined in law. This means that the State Audit Office of Hungary is entitled to audit all the contracting authorities that are subject to the Act on Public Procurement.

The experiences gained in public sector audits show that there are several typical irregularities that often emerge at the majority of the audited institutions.

In the case of infringements of an administrative nature, the contracting authority does not commit an irregularity in connection with a particular public procurement procedure, or it is not the failure to conduct a procedure (bypass) that results in violation of the Act on Public Procurement, but the problem is that the contracting authority fails to fulfil certain administrative obligations. The most frequent irregularities uncovered by the SAO include the failure to register the required data in the contracting authority's list and the failure to publish the notice on the amendment and the performance of contracts. Certain audited entities did not prepare the public procurement plan within the deadline or failed to prepare this plan altogether.

Another typical irregularity is that after an otherwise regular public procurement procedure and conclusion of the contract, the affected contracting authority amends the contract in such a way that it violates the Act on Public Procurement. In this case, the contracting authority commits an irregularity in connection with conducting a particular public

procurement procedure that typically violates the principle of equal opportunity, fair competition and equal treatment through unlawfully amending a contract concluded on the basis of a public procurement procedure or unlawfully evaluating the offers.

The most frequent infringement uncovered by the State Audit Office of Hungary in its audits is the failure to conduct a public procurement procedure where the contracting authority subject to conducting this procedure violates all the basic principles by executing purchases that reach the limits specified by law without a public procurement procedure.

In many cases, the contracting authority commits this violation by executing a purchase that in itself reaches or exceeds the limit stipulated by law. However, based on the experiences of public sector audits, the most frequent and typical irregularity is that the contracting authorities ignore the aggregation rules as required in the Act on Public Procurement. In other words, they fail to take several purchases together, each of which is under the value limit in itself – but should be calculated together because the subject of the procurement is the same – and instead of conducting a public procurement procedure they continue to execute purchases even when the public procurement limit is reached or exceeded.

The opinion of the audited entities

In this section, we shall examine the most general objections based on the subjective opinion of the audited entities in order to offer possible solutions as well.

One of the most frequent "reasons" mentioned by the audited entities for the failure to conduct public procurement proceedings was the lack of resources. However, based on the audit documents, it was possible to establish in many cases that a budgetary institution was continuously making payments during the year (that is, it was continuously executing purchases). As for the lack of resources, the State Audit Office of Hungary established that the main problem in the majority of cases was that the proceedings were not prepared appropriately. The identification of the procurement volume and the procurement regime, the development of the evaluation criteria and the assessment of the market can and must be conducted whether or not there are sources available. If the procurer can launch a well-prepared public procurement procedure immediately after the resources have been made available, the above problem can be eliminated in numerous cases.

The other pretext often mentioned by the procurers is that they do not conduct public procurement tenders because they do not receive the necessary permission from the managing body on time. However, in many such cases the SAO established that the public procurement tender was not announced for months even after the permission was received. In some cases the application for permission was submitted when the contract expired. Thus, the steps that are necessary for conducting an effective public procurement procedure were not taken in time. Therefore, this has nothing to do with well-planned public procurement and we believe that preparation is crucial, as we suggested before.

There was a procurer who argued in connection with public works that the procurement had to be executed in order to eliminate a life-threatening situation, so they had to bypass the public procurement procedure. The elimination of a life-threatening situation does not constitute an exception. If a procurement like this becomes necessary, the procurer should choose the optimal procedure from among those provided for in the public procurement act. These options include an accelerated procedure, a negotiated procedure

without publication or a procedure with at least four bidders in the case of a procurement with a low estimated value.

In several cases, the procurer claimed that there was no point in conducting a public procurement procedure as only a single bidder was able to meet the requirements of the contract. The fact that a particular bidder is able to execute a procurement due to its technical specifications or because exclusive rights should be protected does not exempt the contracting authority from conducting a public procurement procedure. Negotiated procedures without publication can be regularly used by inviting the bidder that is able to deliver.

As for centralised public procurement, the procurers mentioned the lengthy processing time as a reason that prevents them from conducting the required procedure as well as the fact that they cannot choose from among a variety of goods and they often do not get what they want. As for the excuses mentioned in connection with centralised public procurement we need to note that it must be assessed at the time of planning whether in a particular case speedy and simple procurement or a public procurement procedure optimally aligned with the needs of the procurer but which requires more time is in the interest of the contracting authority.

Another frequent reason for failing to conduct a public procurement procedure concerns the issue of procedural deadlines, which are believed to be too long but which should be considered when conducting public procurement proceedings. According to the State Audit Office of Hungary, the risks arising from possible delays in the procedure can be minimised by proper planning and selecting the procedure that is optimal for the procurer.

It was quite common among be audited entities that they failed to conduct public procurement procedure for the following reason: they were afraid that the tender would turn out to be unsuccessful or that nobody would submit an application, which would simply result in loss of time. Another problem mentioned by them was that potential bidders were not motivated to submit a bid because of the long payment deadlines prescribed by law.

These examples show that the reasons for not conducting a public procurement procedure are unfounded. According to the experiences gained by the State Audit Office of Hungary, in many cases the lack of necessary expertise and information leads to irregularities. In most cases, the lack of information means the lack of data on the own financial management of the contracting authorities collected, classified and assessed in due time (Benedek et al., 2014). Another significant risk is represented by the fact that the shortcomings in the control environment directly pave the way for irregularities, leaving the procurers to struggle with the difficulties mentioned before.

The role of the internal control system in support of public procurements

The basis for good public procurement can and must be created by observing the provisions of Government Decree 370/2011 (XII. 31.) on the Internal Control System and on the Internal Audit of Central Budgetary Institutions. This is supported by the fact that the principles to be applied for public procurement can be aligned with the basic principles of the internal control system (*see Figure 3).*

A budgetary institution creates and operates the appropriate internal control system and defines the competencies and responsibilities as well as the conditions for accountability. One of the pillars of the internal control system is the control environment, some of which is included in statutes enacted by the National As-

Figure 3

RELATIONSHIP BETWEEN INTERNAL CONTROLS AND PUBLIC PROCUREMENT

PRINCIPLES OF THE INTERNAL CONTROL SYSTEM	BASIC PRINCIPLES AND REQUIREMENTS OF PUBLIC PROCUREMENT
regularity, level of regulation	**public procurement regulation** [Article 27 (1)–(2) of the Act on Public Procurement] **purchasing regulation** [Point *b)* of Article 13 (2) of the Government Decree on the Implementation of the Act on Public Finances]
waste, abuse and improper utilisation should be avoided	**principle of fair competition, transparency and publicity** [Article 2 (1) of the Act on Public Procurement] **equal opportunity and equal treatment** [Article 2 (2) of the Act on Public Procurement] **good faith and fair dealing** [Article 2 (3) of the Act on Public Procurement]
principle of economy, efficiency and effectiveness	**the principle of effective and responsible management** [Article 2 (4) of the Act on Public Procurement]

Source: own editing

sembly and decrees created by the government and various ministries, and some of which is provided for in the internal policies of budgetary institutions. The control environment is ensured in the area of public procurement by the creation of public procurement and purchasing policies complemented by the annual public procurement plan.

Once the internal control system has been created, it has to be operated with the help of control activities, an information system and a monitoring system. The goal of operating the internal control system is to prevent waste, abuse and the improper use of resources. The Act on Public Procurement lists the protection of fair competition, transparency, publicity, equal opportunity and equal treatment as factors that can prevent abuse, waste and improper use. Good faith and fair dealing helps to drive back these kinds of conduct in a general sense. The goal is to spend public funds in an economical and effective way as well as to ensure compliance, which are enabled by both the set of rules.

If budgetary institutions deem public procurement to be risky, they should take the necessary measures – as the fifth pillar of the internal control system – in order to manage the risks. Risk management is made possible by the Act on Public Procurement itself by providing several different procedures for the procurers to choose from. The risks can be minimised by knowing the options provided for by law as well as by good planning and preparation.

Regulations and the control environment

It is mandatory to conduct public procurement procedure in the cases prescribed by law, for which the leader of the budgetary institution

is responsible. According to the Act on Public Finances, the leader of the budgetary institution is responsible for performing public functions in accordance with the provisions of legal regulations, the deed of foundation and the provisions of the internal policy as well as for fulfilling the obligations stipulated by law for budgetary institutions.

The internal policies must be prepared in accordance with Government Decree No. 368/2011 (XII. 31.) on the Implementation of the Act on Public Finances. Regular public procurement must be ensured in the public procurement/purchasing policies, which should provide for the tasks, competencies and responsibilities pertaining to public procurement and purchasing procedures as well as the rules of procedure. It is important to define a regulated framework of procurements even for items that are under the public procurement limit; therefore, in order to ensure regularity of public procurement it is necessary and mandatory to prepare a purchasing policy. Obviously, the budgetary institutions have more room for manoeuvre, but the system of responsibilities and the basic procedural rules cannot be spared.

One of the indispensable elements of compliance with the public procurement regulations is the annual public procurement plan that contains the scheduled procurements for the given year. The annual public procurement plan can provide meaningful assistance for regular operation if it is constantly updated in accordance with the provisions of the public procurement act by introducing newly identified needs or discontinuing public procurements that are no longer relevant.

Control activities, information system (up-to-date records) and monitoring

The basis of regular and effective public procurement is good preparation, which means a structured collection, analysis and assessment of appropriate information. Good public procurement practice should be based on accurately exploring public procurement needs, which should be given a strong emphasis. In general, budgetary institutions do not devote ample attention to this process, which may lead to irregularities later.

Planning must include assessment of the market environment and the own needs of the procurer and identifying the relationship between these two. For example, if the assessment of the market environment makes it obvious that only a single bidder will be able to execute the procurement, the procurer should be ready to conduct the public procurement procedure in the form of a negotiated procedure without publication by inviting the bidder that is able to deliver. In the same way, it can be determined in the planning period whether a centralised procurement procedure will be sufficient for a particular procurement, which is fast and simple but allows for a narrower range of choice, or whether a public procurement procedure optimally aligned with the needs of the procurer, but requiring more time and can be conducted individually is in the interest of the contracting authority. The preliminary assessment of the needs and the market ensures that the public procurement plan will include the most suitable procedure that fits the procurer's needs the best.

The optimal preparation of the procedures also includes the identification of the volume of procurement, the selection of the suitable procurement regime and the development of the evaluation criteria. The steps can be performed in advance irrespective of whether the sources are available, thereby mitigating the risks that may arise from the lack of resources, lack of time and the need for obtaining the necessary permissions.

If any other procurement becomes necessary in addition to those that have been scheduled, the procurer may choose from the proce-

dures provided for by the public procurement act. One of these options is an accelerated procedure, a negotiated procedure without publication or a procedure with at least four bidders in the case of a procurement with a low estimated value.

Up-to-date and accurate records must be or recommended to be kept for both planning and monitoring procurements as part of the internal control system, which can provide assistance for planning the procurements and preparing or even amending the annual public procurement plan. Such records include the registration of commitments and contracts as well as analytical records.

Most of the irregularities in public procurement are uncovered when the SAO audits the sample items of non-personnel and accumulated expenditure and the records for financial management (such as the registration of commitments, supplier analytical records). In a large number of cases, the procurer failed to establish or was not careful enough to establish that certain procurements had already exceeded the limit for procurement without public tendering – because of the similar or same nature of the goods/services/works project – and therefore, public tendering would have been mandatory. This otherwise typical mistake can definitely be traced back to the lack of continuous monitoring.

If it is constantly monitored which similar or same procurements will probably reach the public procurement limit, using the aggregation rules, this violation can be avoided. The constant monitoring of the supplier analytical records can be used for this, on the basis of which it can be identified for certain procurements with similar or the same subject matter whether particular suppliers have already supplied anything in the given year. This makes it possible to amend the annual public procurement plan on time, if required; the necessary public procurement procedure can then be scheduled and preparation work can begin in time.

Another general problem in public procurement is when expiring contracts that have been concluded under public procurement are renewed or extended irregularly, without conducting public procurement proceedings. The procurers often fail to monitor the expiry date of contracts and hence they do not know when they will expire. In many cases they realise in the last moment or even after the expiry of the contract that they should have invited a public procurement tender for the supply of particular goods and/or services. Since the goods and/or services are needed continuously, they enter into a new agreement without public procurement, contrary to the provisions of the Act on Public Procurement.

The examples referenced above demonstrate that – especially in the case of large organisations – it is extremely risky, if not impossible, to prepare a well-founded public procurement plan and to conduct a successful public procurement procedure in a regular manner in time without keeping up-to-date records on the contracts.

Risk management system

The Act on Public Procurement makes it possible to conduct public procurement proceedings under several different procurement regimes. Each of the special procedures offer a simpler, faster and less complex way to conduct public procurement procedures as compared to the basic proceedings. Knowing that specific facilitating conditions and possibilities can be applied under each regime can considerably mitigate the risk of public procurement irregularities.

It often happens that the procurers use the services of public procurement advisers or specialist lawyers for the documents to be submitted only during the legal remedy proceedings. It is much better to use expert advice

when the procurements are being prepared if the procurer's own institution does not have the required expertise for conducting public procurement procedures. This can enable the procurer to choose a procurement regime that best suits their needs and to establish appropriate evaluation criteria; in other words, to conduct the procedures efficiently and in a regular manner while taking into account their own needs.

CLOSING THOUGHTS

The fundamental objective of public finance controls is to promote the regular, economical, effective and efficient management of the funds and assets of public finances. The control of public finances – which extends to all subsystems of public finances – is supported by three pillars. In public procurement, these three pillars include the internal control system of the organisation subject to public procurement; the Public Procurement Authority competent in and responsible for assessing and sanctioning irregularities; and the government audit body (the body responsible for supervision of compliance at local governments) authorised to initiate legal remedy proceedings at the competent authority as well as the State Audit Office of Hungary responsible for the external audit of entities using public funds. At the same time, these pillars represent a kind of "line of defence" for acting against irregularities in public procurement.

The leader of the organisation subject to public procurement is responsible for establishing and operating the internal control system. Any possible shortcomings or irregularities in the operation of the given organisation should be uncovered by the internal auditor, who should provide feedback to the manager of the organisation. We are convinced that the regularity of public procurement must be ensured at this level. Public procurement procedures conducted in a professional manner should be based on well-established and well-operated internal controls. The level and operation of the internal controls and the regularity and effectiveness of purchasing and public procurements are closely related.

The second pillar includes the organisations performing government auditing tasks, such as the Government Audit Office (KEHI), the Directorate General for Audit of European Funds (EUTAF) and the Hungarian State Treasury (MÁK). Although there is a wide range of organisations that are entitled to initiate proceedings ex officio if any irregularity is detected in public procurement, it is mostly the KEHI and the EUTAF that may encounter irregularities in public procurement when performing their tasks.

The last line of defence is the SAO, which has general competence in auditing public funds (Németh, 2016). As the main auditing body, the SAO is only subject to the National Assembly and law, and its role is to ensure independent external auditing.

Although in the last few years the SAO has been given an important role in indicating irregularities in public procurement, and as a result, in making sure that the organisations can be held accountable and that they can be persuaded to adopt a law-abiding behaviour, the detection of irregularities in public procurement is not its primary audit task. The main focus of the audits is the internal control system and the compliance with the regulations pertaining to asset management and asset preservation, and irregularities in public procurement constitute only one particular criterion in the system of audits.

The State Audit Office of Hungary – representing the highest level of controls in public finances – perform its tasks well and effectively if it can filter out the irregularities that cannot be detected by the lower-level controls.

The volume of irregularities uncovered by the SAO shows that the operation of lower-level controls in public procurement is inappropriate at the audited organisations. By initiating legal remedy proceedings after shortcomings have been detected and by making its experiences public, the SAO wishes to contribute to the effective, economical and transparent utilisation of public funds. By driving the audited organisations to exhibit lawful conduct and presenting "good practices", it tries to ensure that it really acts as a third line of defence in performing its duties and that the irregularities in public procurement are managed primarily at the first two levels of public finance controls.

Note

[1] The Public Procurement Authority is mentioned in this paper every time when it acts as a separate entity and there is no need to differentiate the Public Procurement Arbitration Board working within the Authority in terms of its responsibilities and functions.

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