# Management of public procurement in AS Riigi Kinnisvara

**Executive summary**

The Government decided to establish AS Riigi Kinnisvara (Public Limited Company Government Real Estate, hereinafter referred to as "GRE") in June 2001 with the aim of relieving government authorities from the burden of managing the premises they use (and constructing new buildings). The buildings and registered immovables of government authorities were to be transferred to GRE, which would then lease the necessary buildings and premises to government authorities. As of the moment, the Ministries of Justice, Finance and Internal Affairs have transferred buildings and registered immovables to GRE.

GRE is required, in addition to the maintenance of buildings and premises leased to government authorities, to improve these and, where necessary, to organise the construction of new buildings (premises) on the account of its own or borrowed funds. When GRE was established, it was thought that it could manage these operations, especially procurement, better than government authorities. The objective of the audit was to find out whether the activities of GRE have been sufficiently regulated in that regard and whether these have been in accordance with the needs, interests and financial possibilities (payment of the growing rent) of government authorities and with the Public Procurement Act.

The purpose of the audit was not to assess the management or the efficiency of the business operations of the company or the conformity of the past activities and their results with the objectives specified at the time of foundation. The management of public procurement by the GRE was mainly assessed on the basis of procurement projects implemented in 2002.

**Main findings**

**Findings related to the operational goals of GRE**

The assets of GRE have grown more than ten times in two years – at the time of foundation in summer 2001 the Government set the company's share capital at 81 million kroons, which, by virtue of government investments in its share capital, had grown to 923 million kroons as of September 1, 2003.

The transfer of the buildings of government authorities to GRE has not entailed the termination or considerable reduction of investments (construction, renovation) within the government areas of the Ministries.

Investments in buildings used by government authorities made by GRE [1] are to be covered inevitably by the government in the form of growing rental payments. Investing through GRE defers some public expenditure[2], but, on the other hand, leaves the government without any alternatives in the coming years – the government may choose not to invest, but the government authorities must pay the rent.

The rental expenditure of authorities leasing buildings and premises from GRE have increased and will continue to grow considerably (multiple times) in the next few years, due to moving into new buildings or repairing the buildings and premises currently in use.

The Ministry of Finance has not made calculations concerning the increase of rental expenses of government authorities leasing premises from GRE after 2004, since management expenditure, unlike investments, is planned for one year at a time only.

GRE has fulfilled its obligations assumed under investment agreements made upon transfer of assets from government authorities both as regards the selection of objects to be constructed and renovated and the time limits of works. Also, it has taken account of the authorities' requests concerning the volume, time limits and estimated cost of works to the extent possible. Co-operation with government authorities as tenants has been constructive.

The SAO thinks that the rules of GRE concerning the establishment of cost-based rent for government authorities lack formality – the rent calculations do not show whether and how much GRE gains or loses, in financial terms, from leasing the buildings or premises to government authorities.

**Findings related to procurement management**

On the whole, the procurement activities of GRE are quite well managed – the audit demonstrated only a few shortcomings. The company's management has regulated the procurement activities of GRE in an

adequate manner.

**Main proposals**
**To the Minister of Finance**

- To estimate the growth of rental payments government authorities resulting from the lease contracts they have entered into (and from the already signed investment agreements) and to set clearer restrictions on government authorities in this regard: for example, to provide, where appropriate, by means of a Government Decision, that normally the increase in rental expenditure is not to be covered from additional allocations from the state budget, but by means of reducing other management costs, and also to provide for the possibility of derogating from this rule and the procedure for allowing derogation.
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- In his capacity as the Minister running the Ministry, which exercises the rights of the founder of GRE, to adopt a position on the profit margin to be applied by the company in lease contracts made with government authorities in cases where the rent is determined on cost basis (the profit margin limit), and to demand, through the Supervisory Board of GRE, its application.
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- To assess the situation of establishing the standard costs of workplaces in government authorities[3] and, where necessary, to request further consideration of the relevant issues in the Government.
- Given the extent of public property transfers and the extensive obligations assumed by the government under investment programs, to draft proposals to amend the legislation (whether the modification of the act regulating government participation in legal persons governed by private law or the adoption of a separate act), providing for the principles of transferring public property to GRE and the necessary specifications as regards the management and reporting of that company.

**To the Ministers of Justice and Internal Affairs and the Director General of the Customs Board acting as the Director General of the Tax Board**

- To raise in GRE the issue of the need to set out, in the annexes to the lease contracts concerning objects for which the rent is calculated in cost basis, the composition of the rent broken down by types of cost, and the company's profit margin (expected profit made on a specific object).

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The Minister of Finance announced that in principle he agrees with all the proposals addressed to him, to the exception of the proposal concerning the initiation of the legislative amendment procedure with the aim of providing for the principles of transferring public property to GRE and the necessary specifications as regards the management and reporting of that company. The Minister noted that the implementation of proposals requires careful preparation and that the Ministry does not have a specific timetable for the changes to be made. The Minister informed about the completion of the draft of the new Government Participation in Legal Persons Governed by Private Law Act; the Act would provide for a number of additional possibilities of improving the direction of and control over public undertakings.

The Ministers of Justice and Internal Affairs and the Director General of the Customs Board acting as the Director General of the Tax Board announced that they agree with the proposals addressed to them.

The Chairman of the Management Board of GRE announced that he agrees with the positions of the SAO, to the exception of the opinion that it would be reasonable to lay down the principles of transferring public property to GRE and the necessary specifications as regards the management and reporting of that company in the form of amendments to the relevant laws.

The responses from the persons mentioned above have been reproduced at the end of this report.

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