Acquisition of cars by rural municipalities and cities and by companies where they have shareholding

How do local authorities and their companies acquire vehicles and recognise these acquisitions?

National Audit Office's report to the *Riigikogu*, Tallinn, 5 October 2011

Summary of audit results

The National Audit Office (NAO) audited the acquisition of cars (incl. purchasing and leasing) in ten local authorities, their agencies or companies owned by them. The audit focused on whether the auditees have adhered to the Public Procurement Act in acquiring cars and whether the obligations assumed upon leasing have been recognised in the accounts in accordance with the General Rules of Accounting of the State.

Having analysed an extract of the traffic register prepared for the NAO by the Road Administration regarding acquisitions of vehicles by local authorities and their companies through 2008 to 2010, the NAO chose the auditees taking into account the number of acquisitions and the recognition of the acquisition of the acquired vehicles in the public procurement register. The number of acquisitions audited by the NAO included automobiles and minivans (hereinafter cars), while other vehicle types (buses, tractors, trucks, motorcycles, trailers, etc.) where not covered by the audit.

Through 2008 to 2010 local authorities and their companies made car lease payments and compensated for the use of personal automobiles on average in the total amount of 6.6 million euros a year. Fuel expenses amounted on average to a total of 16 million euros a year and insurance expenses to a total of 1.2 million euros a year.

The reasonableness of expenses relating to the use of cars by the public sector has always been of interest to the public. Taxpayers have legitimate interest in whether vehicles purchased for taxpayers' money for the performance of official functions correspond to the official functions in terms of the price and accessories and that unreasonable expenses relating to vehicles are precluded.

According to the latest practice, the public sector (incl. local authorities) largely prefers to lease cars instead of buying them at once. This involves the additional risk that the incorrect recognition of the accounting of leased cars may affect the correctness of the accounting indicators of the entire public sector.

As a result of the audit the NAO found that nine auditees out of ten had disregarded the Public Procurement Act to a significant extent upon acquisition of cars. With regard to obligations assumed by leasing cars the NAO found that these have been recognised in the accounts in accordance with law to a significant extent and that no prohibited obligations have been assumed, although the contracts contained some aspects that could be interpreted in different ways.

Main findings of the NAO:

- Upon leasing cars by way of operating lease, the widespread standard contracts have some elements that refer to finance lease: for instance, the lessee cannot terminate the contract without additional expenses and even if it is impossible to use the car, lease payments still have to be made. Although local authorities and their companies have wanted to lease cars mostly by way of operating lease, the main leasing companies in the market do not virtually provide such service and local authorities have been unable to sufficiently

negotiate with the leasing companies to make certain that the contract complies with the desired terms and conditions.

■ Upon organising procurement procedures, the auditees had often settled with the standard tenders of leasing companies, although these did not comply with the announced procurement criteria. For instance, if the procurement criteria do not specifically refer to the permissibility of a floating interest rate, the contracting authority cannot award a contract where the interest rates fixed in the contract differ from those of the tender, because the interest rates have changed in the meantime. By accepting the terms and conditions of a public contract is such a manner, the cars acquired by the Tallinn Municipal Police Department became notably more expensive than specified in tenders. This harms the interests of other tenderers operating in the market.

■ Upon acquisition of cars, the activities of the auditees were non-transparent, above all, in a situation where the price of the car did not exceed the threshold of organisation of a procurement procedure arising from the Public Procurement Act, but the general principles of the Public Procurement Act had to be followed. In the event of such purchases the auditees were often unable to justify the car selection criteria and whether and how the existing terms and conditions of competition were taken advantage of. Since in many events the process was not understandably documented, such practice involves the risk that the true intention behind quite a few acquisitions was to make a purchase from a specific dealer by precluding competition.

■ At the level of the council of a local authority or the supervisory board of a company belonging to a local authority (general meeting), no general principles of using cars, which would preclude the establishment of corruptive relationships, had been usually agreed on for the management. Leasing a car from oneself or from a company related to oneself means that the official has violated the restrictions provided for in the Anti-corruption Act. The NAO found that in at least one agency an official had leased a car from a related company.

■ The Ministry of Finance who should keep an eye on the financial capacity of local authorities and analyse the relevant contract made by local authorities and their companies, has not taken any interest in car lease contracts. The communication of information to the Ministry of Finance has also not been ensured by the compulsory reports of local authorities and therefore the accounting of car lease causes confusion.

Response by the auditees. All the auditees and the Ministry of Finance replied to the NAO based on the report. In general, they agreed with all the recommendations. The full texts of the responses are available on the website of the NAO at www.riigikontroll.ee.

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