

# **Bundesrechnungshof's spring report 2014 on federal financial management in 2013 – additional audit findings –**

## **Introduction**

*The German SAI reports on **additional audit findings** supplementary to its 2013 Annual Report (Parliamentary paper 18/111). This additional reporting covers findings on federal financial management which the Bundesrechnungshof generates only after conclusion of the traditional annual reporting process. These findings provide an up-to-date basis for the decision of the Legislature about granting discharge to the Federal Government in respect of FY 2012.*

### **1 Subject addressed by the additional reporting**

The German SAI audits the entire financial management of the Federal Government including federal off-budget funds and industrial or trading funds (Art. 88.1 German Federal Budget Code). Where the result of its audit may be significant for granting discharge to the Federal Government in respect of the budget and capital accounts, it reports annually to the two Houses of Parliament (Art. 97.1 German Federal Budget Code, FBC).

The *Bundestag* (the directly elected House of the German Legislature) forwards our report to its Budget Committee, which in turn refers it to its sub-committee, the Public Accounts Committee (PAC). The PAC deliberates on the individual audit findings and adopts resolutions on them. In the course of the parliamentary discharge procedure, the audit findings reported by us may prompt parliamentary resolutions calling for action to be taken (Art. 114.2 FBC) or a disapproval of specific matters under scrutiny (Art. 114.5 FBC).

We forwarded our 2013 annual report with our findings on the 2012 annual accounts to the two Houses of Parliament on 9 December 2013.<sup>1</sup> The President of the Bundesrechnungshof presented the report to the public at a press conference held on 10 December 2013. That annual report is available on our website.<sup>2</sup> Detailed information on our audit mandate, the criteria, scope and focus of our work is provided in our 2013 annual report.<sup>3</sup>

## **2 Timeliness of reporting to Parliament**

Finalising the annual report requires considerable lead time, which is necessary especially to be able to take into account the comments provided by the audited bodies. Audit findings suitable for inclusion in the annual report but developed later than in spring cannot be incorporated in the annual report that is communicated to the Legislature at the end of the year.

To avoid this time lag, we developed an additional reporting procedure, in agreement with the PAC, to supplement our annual report. We communicate any additional audit findings relevant for the annual report and developed after the finalisation of the annual report to the PAC for deliberation in the spring of the following FY. This procedure ensures that the Parliament's decision about granting discharge to the Federal Government in respect of the previous FY, which is scheduled for June each year, can be taken on the basis of more recent information.

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<sup>1</sup> Bundestag Paper 18/111; Bundesrat Paper 799/13.

<sup>2</sup> <http://www.bundesrechnungshof.de>

<sup>3</sup> Cf. Introduction to Bundestag paper 18/111; Bundesrat paper 799/13.

### **3 Additional audit findings**

The current audit conclusions deal with key audit findings across various government departments which we generated jointly with our regional audit offices. Keeping the specific objective of this supplementary reporting in mind, we have taken special regard to topicality when selecting the individual reporting items. The order of presentation does not warrant conclusions as to the frequency of errors and objections made by the various audited bodies.

In the same way as for the annual report, the additional audit findings have been forwarded for comment to the audited bodies in the form of draft reports. This contradictory procedure has the purpose of once more validating the findings of fact which, as a rule, have been discussed with the audited bodies beforehand during the audit exercise. Differences of opinion about the facts and figures presented are mentioned in the supplementary report. Where the bodies concerned have expressed divergent opinions, these are also reported.

In the same way as the annual report, additional reporting distinguishes between “cross-boundary and horizontal audit findings” (of the type set forth in Part II of the Annual Report) and “audit findings on departmental budgets” (of the type set forth in Part III).

## Summaries

### Federal Ministry of the Interior

#### 1 Decommissioning of air-raid shelters lack a structured approach

*The Federal Interior Ministry is arranging for decommissioning, dismantling or selling all 1,300 public air-raid shelters. In order to carry out the pertinent transactions efficiently in terms of nature, scope and timing, it must obtain a complete overview of the condition, legal status and costs for the maintenance and dismantling of all public air-raid shelters.*

The Federal Government maintains public shelters in order to protect the population in a state of defence or tension. Up to the 1990's, the Federal Government spent €1.1 billion on the construction of public air-raid shelters. Additional expenditure of €100 million was incurred for the furnishing and technical installations and another €100 million for maintenance. In 2007, the Ministry decided to decommission the public air-raid shelters. This includes measures such as dismantling or selling the shelters and decommissioning wells and technical installations. The Ministry justified its decision by arguing that, given the damage and very short warning time to be expected in case of a military attack, the public shelters cannot afford protection. Up to now, the Ministry has not yet informed Parliament about the consequences and costs of its decision.

According to estimates made in 2008, the Federal Government will have to spend up to €60 million for dismantling the shelters. The Ministry has not obtained an overview of the conditions and legal status of the public shelters. It has not developed an overall decommissioning strategy. For instance, no regulations have been developed as to which costs the Federal Government will have to bear when shelters or wells are dismantled. In practice, this has already resulted in large differences of the dismantling costs of similar structures.

We criticised the failure to inform Parliament. We have asked the Ministry to obtain a complete overview of the condition and legal status of the shelters. On this basis, it should plan the decommissioning operations in terms of type, scope and timing and should estimate the costs.

The Ministry announced that it would inform Parliament about the decommissioning during the 2014 budget deliberations. It rejected compiling a full inventory for basing plans on a sound legal footing and for cost estimates of the proposed project.

With a view to the assessment of the changed security situation, the budget funds spent on building the shelters and the considerable costs of their decommissioning, we consider Parliament needs to be involved. Furthermore, the Ministry will have to show how the shelters can be commissioned in an expedient and cost-effective way.

## **Federal Ministry of Finance**

### **2 Regulation on teaching staff's working hours at the department of financial management science of the Federal University of Applied Administrative Sciences reduces the staff time available for teaching**

*The regulation on teaching staff's working hours at the department of financial management science of the Federal University of Applied Administrative Sciences is inefficient. Since time spent on numerous other activities is deducted from obligatory teaching hours, the number of teaching hours is significantly lower than the standard number of hours prescribed by an agreement between the Conference of Education Ministers of the German states. We therefore demand that the Federal Finance Ministry introduce more restrictive rules for crediting non-teaching work for purposes of determining the hours worked by staff. This would make more staff resources available for teaching.*

The Federal Revenue Administration's Training and Knowledge Centre trains candidates for the higher intermediate customs service at the financial management science department of the Federal University of Applied Administrative Sciences. The Federal Finance Ministry issued a directive determining the working hours of full-time teaching staff. This directive also prescribes obligatory teaching hours, which are defined as the number of hours which the staff must, as a rule, spend on preparing, holding and following up on lectures.

The directive stipulates that obligatory teaching hours are reduced, if the teaching staff do other work. Such other work may include e.g. internal meetings or the supervision of exams. The list of types of work eligible for being credited to the total obligatory teaching hours includes 25 items. This reduced the actual teaching hours to the extent that overtime and the hiring of additional teaching staff was necessary to deliver training at the department of financial management sciences.

We objected to the fact that the Ministry's directive listed more types of work creditable against the obligatory teaching hours than provided for in an agreement of the Conference of Education Ministers. We recommended revising the list.

In response, the Ministry revised the working hours regulation and reduced the number of types of work creditable against the obligatory teaching hours. In our opinion, this is not yet sufficient. Under the revised scheme, the number of actual teaching hours available in the department of financial management sciences is still smaller than provided for in the agreement of the Conference of Education Ministers. We therefore demanded that the Ministry proceed with its efforts to reduce the number of types of work creditable against the obligatory teaching hours.

## **Federal Ministry of Labour and Social Affairs**

### **3 Excess administrative burden of ascertaining other income of orphans to be set off against the orphans' pension claims**

*Once orphans have reached the age of majority, the pension insurance bodies are obliged to annually ascertain other income of adult orphans that draw orphans' pensions, since such other income may reduce the pension claim. However, the costs incurred for ascertaining income exceed the total amount of the pension reductions.*

Orphans have a claim to an orphan's pension up to age 27, if they attend school or vocational training. If they have other income of their own, this may reduce the pension claim. The relevant statutory provisions are complex and require comprehensive legal knowledge. They also result in a vast administrative burden on the pension insurance bodies themselves, the orphans, their employers and health insurance funds. For the pension insurance bodies alone, ascertaining the other income of the claimants causes expenditure of at least €12.5 million annually. The pension insurance bodies estimate the total deductions from pension claims at €8 million, while our audits suggest an even lower figure. We recommended that the provision requiring the deduction of claimants' other income from the pension claim should be repealed. In line with a change made in the case of child benefit, the pension insurance bodies could then limit their determination of claims to the question as to whether the adult orphans are undergoing training and whether the training actually demands the input of most of their time and capacity to work.

The Federal Ministry of Labour and Social Affairs has already drafted a legislative amendment and stated that it would arrange for its enactment, along with the amendment of other provisions, still during the life of the present Parliament.

In our opinion, it is necessary to disconnect the draft amendment from other legislative projects not yet agreed and to submit the amendment concerning orphans' pension claims to the Legislature without delay.

## **Federal Ministry of Transport and Digital Infrastructure**

### **4 Federal Railway Assets Fund pays an inadmissible and excessive lump sum to compensate for personnel costs**

*By virtue of a flat rate agreement, Deutsche Bahn AG received a total amount of €278 million in compensation for personnel costs. Contrary to applicable legal provisions, it did not have to supply evidence justifying that the conditions for such compensation were met.*

The relevant legislation gives rise to compensation claims, if, owing to rationalisation measures, Deutsche Bahn AG (the national railway company) can no longer employ staff taken over by or assigned to it. For this purpose, Deutsche Bahn AG has to prove its claims in detail. In the past, it had not succeeded in doing so. The Federal Transport Ministry and the Federal Finance Ministry concluded an agreement with Deutsche Bahn AG providing for a lump-sum payment to compensate for any arising claims. As a consequence, considerable amounts of compensation were paid for groups of employees not legally eligible for such compensation.

The Federal Transport Ministry and the Federal Finance Ministry regard the regulations as being of little use. They argued that, owing to the lack of insight into strategic company data, it was impossible to verify the claims on the basis of detailed circumstances.

We found that the prescribed detailed determination of the compensation claims is reasonable and therefore mandatory. Deutsche Bahn AG has to give detailed proof that the prerequisites for compensation have been met. Moreover, we recommend amending of legislation to completely abolish such compensation claims.

## **Federal Ministry of Transport and Digital Infrastructure**

### **5 Federal Government should no longer use cancer-causing materials for road construction**

*Roads partly contain cancerogenous binders whose ingredients include tar or pitch. These materials are reused when repairing roads. This is inexpedient both in terms of ecology and economy. Rather than that, it would be possible to incinerate the cancer-causing materials nearly without any residues (thermic process).*

Reuse does not only keep the substances considered as hazardous wastes in circulation. Their total quantity built into roads is already about 1,000 million tons. The contaminated quantity increases by more than 30 per cent with every instance of reuse whenever the old pavement gets mixed with uncontaminated layers.

In addition, some states built their cancerogenous waste into federal roads. This will result in future burdens on the federal budget, since the federal government is responsible for the later reprocessing or disposal. At this time, such burdens already total about €1.1 million. The Federal Transport Ministry has so far not taken adequate remedial action. For instance, the Ministry failed to demand the timely and complete submission of data about the quantities of hazardous waste used in road upgrading and maintenance.

At present, there is the risk that the quantity of contaminated wastes will increase continuously, imposing ever higher burdens on future federal budgets. We therefore consider it appropriate that the Federal Transport Ministry intends to stop reusing cancerogenous wastes. We demanded that the Ministry exercise its technical oversight over the states' road construction administrations with the necessary vigour in order to counteract or compensate for shifts of financial burdens from the states to the Federal Government.

## **Federal Ministry of Transport and Digital Infrastructure**

### **6 Expensive planning of the construction of a bridge of Federal Motorway A 20 across the river Oste**

*The Federal Transport Ministry intends to have an unnecessarily high bridge near Bremervörde for the Federal Motorway A 20 to cross the river Oste. A bridge nearly 1 metre lower would be sufficient.*

The planned bridge is in the 6<sup>th</sup> building section of A 20 and nearly 280 metres long. The road works administration estimates the construction costs at €11.4 million, while we estimate that these costs will amount to at least €13.9 million. The planned air draught is 5.45 metres above the medium high-water level. The road works administration thinks that the height of the bridge is necessary to enable working boats to pass under it for purposes of river and dike maintenance and to preserve ecological passability under the bridge structure.

In our opinion, a height of 4.50 metres will be sufficient for permitting maintenance work to be performed with the usual heavy equipment, the more so since the water level drops by 1.30 metres at low tide. The requirements imposed by the applicable “Memorandum for the installation of wildlife crossings for ensuring the connectivity of habitats near roads” would be completely complied with. Finally, this would also be sufficient for river transport, since only sports and recreational vessels and not cargo vessels can navigate there.

We demanded that the Federal Transport Ministry correct the height of the bridge over the river Oste. We expect that this will generate savings of about €1 million. Moreover, the consumed area would be about 900 square metres less. The planning modification would mitigate the impact on the landscape and the ecologically sensitive river meadows of the Oste.

## **Federal Ministry for the Environment, Nature Conservation, Building and Nuclear Safety**

### **7 Pilot projects for environmentally friendly inland shipping largely unsuccessful**

*The Federal Environment Ministry gave grants towards two shipbuilding projects but did not achieve the essential goals sought. One major reason for this is that the Ministry failed to identify project risks or assessed these risks inaccurately. Thus, it did not use valuable options for steering the projects.*

In spite of considerable warning by experts, the Ministry gave grants towards the use of a combined exhaust gas technology not yet developed to maturity. This technology then functioned only inadequately and failed several times. The Ministry was not able to conduct the scheduled measurements to verify if the grant-funded technology was workable in practice because it had not created the necessary prerequisites. Although the purpose of the grant-funding was to make inland shipping more environmentally friendly, one of the ships navigated almost exclusively at sea and along coasts in the Mediterranean. Instead of preventing this, the Ministry even financially supported the necessary retrofitting of the vessel.

The Ministry announced its intention to arrange for better project steering. We consider this suitable first steps. In addition we expect the Ministry to consistently align its projects with the goal of the grant-funding and to take corrective action whenever something is about to go wrong. If it becomes apparent that the objective of the grant-funding cannot be accomplished, the Ministry must terminate its financial support or reduce its grants to the amount needed to meet at least those sub-targets likely to be achievable.

## **Federal Ministry of Defence**

### **8 Unnecessary expenditure for private-sector service providers**

*Through the years 2011-2013, the Armed Forces spent more than €2 million on purchasing an unnecessary service. It commissioned a private-sector service provider to procure equipment and materiel for the two Armed Forces universities. The service provider was able to carry out the procurements without any significant effort. We repeatedly recommended that the Armed Forces make themselves the procurements.*

The two Armed Forces universities have procurement units of their own which partially cover their needs of equipment and materials. Simultaneously, the Armed Forces have for more than 30 years commissioned a private-sector service provider who also procures items for the universities. Through the years 2011-2013, the Armed Forces paid remunerations totalling €2.1 million to the service provider.

Assisted by our Munich regional audit office, we audited procurements made by the contractor on behalf of one university. We found that, apart from standard items, e.g. tablet computers and digital cameras, the contractor also procured technical equipment for laboratories. As a rule, the university described the items to be purchased in such detail that the contractor was able to directly place orders on this basis. For instance, the Armed Forces paid a remuneration of €2,400 for the following procurement. The university forwarded to the service provider the negotiated five-page tender of a supplier for a robot system with all desired component and technical specifications. On this basis, the service provider bought the robot system from the supplier.

Already in 1988, 2001 and 2003, we had pointed out to the Federal Defence Ministry that the permanent use of a private-sector service provider for making the procurements on behalf on the universities was unnecessary.

The Ministry stated that, apart from the examples we gave, the contractor had provided much more demanding services and that the universities had installed extremely complex facilities and laboratories with the assistance of the contractor's technical competence. The Ministry promised that the Armed Forces would in future process "less complex" procurements on their own.

In our opinion, this is not sufficient. In all procurement cases we audited, the university informed the service provider in detail about requirements and technical specifications and even about the results of price negotiations with suppliers. Therefore, the service provider's own input was limited to placing orders on this basis and monitoring delivery. Neither the Ministry nor the university gave examples for more demanding services rendered by the contractor. This shows that the university does not need the technical competence of the service provider. Expenditure in the range of millions of euros on purchasing these services could therefore be saved.

The Ministry has for several years failed to ensure that the Armed Forces make procurements with their own personnel. In particular, the necessary resources for doing so are available in the universities' own procurement units and the Armed Forces' central procurement office. The Ministry should ensure that the Armed Forces do not permanently rely on a service provider for processing procurements on behalf of the Armed Forces' universities.

## **Federal Ministry of Defence**

### **9 Lacking cost transparency of the EUROFIGHTER**

*The Federal Defence Ministry lacks transparency about the total expenditure incurred so far and to be incurred in future for the EUROFIGHTER. Actual expenditure is likely to considerably exceed earlier estimates. This reduces the funds available for other defence systems. This lack of transparency makes it difficult to determine the volume of resources available for alternative defence projects.*

In 1997, the Armed Forces planned to procure 180 EUROFIGHTER aircraft at a cost of about €11.8 billion. This amount will be almost completely exhausted by the procurement of 140 EUROFIGHTERS. The Defence Ministry expects life cycle costs to total at least €30 billion.

The Armed Forces use the term “life cycle costs” for all expenditure that is incurred during the life cycle of a defence system and can be imputed to the operational system. Knowing the life cycle costs serves to help plan expected expenditure in the long-term.

Although the number of EUROFIGHTER aircraft to be procured is to be reduced from 180 to 140, we estimate that the life cycle costs will be about twice higher than those estimated at the beginning of the procurement process. The increase of operational expenditure is exceptionally large; this applies especially to the expenditure on material maintenance.

Moreover, additional needs for complementary developments and procurements are arising and only a small portion of these is already reflected in the budget and the medium-term financial plan.

We criticised that, in spite of changing conditions, the Federal Defence Ministry failed to update life cycle costs and did not keep track of all incurred and expected expenditure on the EUROFIGHTER. We demanded the Ministry to

ensure greater transparency of expenditure and to enhance its monitoring. To do so, the Ministry should re-estimate life cycle costs, to look into the causes for cost increases and to press for cost reductions. In our opinion, it is imperative that the Ministry's annual progress reports compare the expenditure actually incurred with the re-estimated life cycle costs.

## **General Fiscal Administration**

### **10 Electronic communication of notarial deeds to tax offices is long overdue**

*Up to the present, notaries are obliged to forward deeds about legal transactions concerning incorporated companies to tax offices as printed format rather than electronically. This impairs the necessary exchange of information. In our opinion, it is necessary and feasible to introduce electronic communication of these deeds without delay. The Federal Chamber of Notaries had submitted proposals to this effect already in 2007. However, these proposals have not yet been implemented. The Federal Finance Ministry should advocate the change in the relevant joint bodies of Federal Government and state government representatives.*

Already in 2007, the Federal Chamber of Notaries had suggested to the Federal Finance Ministry to forward deeds about incorporations and certain other legal transactions concerning incorporated companies to tax offices electronically and no longer as printed format. The Federal Finance Ministry then stated that, in principle, this proposal could be implemented in the IT system in place. This has not been done so far.

The current paper-based procedure that is still in use impairs the necessary information exchange. In 2011, we therefore recommended introducing electronic communication of such deeds. The Ministry told us that, before implementing the proposal, it wished to wait for the experience gathered with the technical implementation of another communication procedure. It went on to say that the objective was not only to forward the communications electronically but also to process them by computer. This preparatory phase is still under way.

Already since 2007, notaries have forwarded such deeds to the commercial register electronically. Arranging for their electronic forwarding to the tax offices would have been feasible years ago. Processing there would be significantly

facilitated, even if the deeds could not yet be processed completely by computer.

We therefore hold that the electronic communication of such deeds – independent of any other communication procedures – is both necessary and feasible and could be speedily introduced. The Federal Finance Ministry should be committed to switching to electronic communication in the relevant joint bodies of Federal Government and state government representatives.

## **General Fiscal Administration**

### **11 Accurate taxation of foreign internet provider**

*Inspection by the German tax authorities of foreign enterprises which provide internet services in Germany is insufficient. A large number of unregistered traders raises concerns that losses of related tax revenues may amount to millions of euros. The Federal Finance Ministry is called upon to step up the tax inspection of internet services and to eliminate deficiencies in the taxation procedure.*

Internet services giving access e.g. to music and videos, e-books, live cams and software are provided also by traders with headquarters outside the European Union ('third-country traders'). Turnovers generated by providing such services are liable to value added tax (VAT) in the Member State in which the user of such services resides. Therefore, the traders must register for VAT in all Member States in which they generate turnovers (general taxation procedure). Since 2003, they have been permitted to declare all their turnovers in the EU in one Member State which remits the VAT collected to the other Member States in proportion to the respective turnovers (special taxation procedure).

We found that only few third-country traders are registered for VAT in Germany. Under the special taxation procedure, Germany obtains VAT revenues of only about €23 million annually. In practice, there are no checks for such VAT liabilities. Thus, it is very easy for third-country traders to provide internet services without paying VAT on them. The market for internet services is in the range of billions of euros and is growing steadily. In our opinion, the related VAT revenues of only about €23 million suggest that there is a large number of third-country traders who do not pay VAT on the internet services which they provide.

Therefore we have called for an improvement of tax inspection. Procedural deficiencies, e.g. non-serviceable data bases, inadequate exchange of

information with other Member States and the lack of information in English, will have to be eliminated.

The Ministry has questioned the fact that there is a large number of unregistered traders. Rather than that, it assumes that third-country traders who provide internet access to music, videos, e-books, live cams and software essentially meet their tax liabilities. However, the Ministry admitted that there are some procedural deficiencies and intends to consider e.g. bilingual information.

We believe that it is wrong to assume that service providers from outside the European Union essentially meet their tax liabilities despite the absence of tax inspections. We therefore uphold our demand that tax inspection and the taxation procedure be improved so as to increase Germany's VAT revenues from third-country traders.

## **General Fiscal Administration**

### **12 Special VAT arrangement for farmers – Federal Finance Ministry must inform Parliament better**

*The Federal Finance Ministry has for years failed to inform Parliament about the trend of the input VAT burden on farmers to whom a special arrangement applies (flat rate farmers). Legislature uses the burden of input VAT as an important criterion for fixing the special VAT rate for flat rate farmers. Due to the lack of information, the Legislature was unable to take an appropriate decision about whether the special VAT rate for these farmers was to be adjusted. Failing such adjustment, considerable losses of tax revenue may ensue.*

The farmers who benefit from this arrangement may use a special provision on VAT. They may charge VAT at an average rate on the goods and services they deliver. They are not obliged to remit to the tax office the VAT they have collected. Instead, the additional revenues they thus obtain are to compensate farmers for the burden of input VAT charged to them by other traders. Under EU law, this special arrangement is not permitted to lead to a tax subsidy. Therefore, no Member State may fix the average rate at a level enabling them to receive VAT in excess of their input VAT burden. The Federal Finance Ministry must calculate the input VAT burden of the German flat rate farmers to enable German Legislature to determine the appropriate average rate. Such a calculation has to be based on the economic data of the recent three years. In 1990, the Finance Committee of the German Parliament decided that the Ministry should inform the Committee annually about the input VAT burden of the flat rate farmers.

The average rate of 10.7 per cent has remained unchanged for years. We found that, since 1998, the Ministry had not informed the Finance Committee about the trend of the input VAT burden. The Ministry told us that the Finance Committee had not objected to this. Therefore, the Ministry had assumed that the Committee did no longer need such information.

We demanded that the Ministry report to the Finance Committee annually about the development of the input VAT burden. Such reporting is absolutely needed for the Legislature to take a reliable decision as to whether the average rate is to be adjusted. Such decision will have a considerable financial impact. A change of the average rate by only one percentage point is already equivalent to a VAT amount of €150 million annually, which the flat rate farmers may or may not collect from their customers and treat them as their own revenue.