

Department of Legislative Services
Maryland General Assembly
2009 Session

FISCAL AND POLICY NOTE

House Bill 19
Appropriations

(Delegates Frick and Haddaway)

Budget and Taxation

Municipal Corporations and Taxing Districts - Financial Audits

This bill enables a municipality or State-created taxing district with annual revenues of less than \$250,000 to be eligible for a waiver that allows them to be audited at least once every four years instead of annually. Currently, the waiver is only available to municipalities and taxing districts with annual revenues of less than \$50,000. In addition, the bill alters the auditing requirement for county-created special taxing districts with annual expenditures of less than \$250,000 by enabling them to conduct an audit once every four years instead of annually. Currently, this provision only applies to county-created special taxing districts with annual expenditures of less than \$50,000.

The bill takes effect July 1, 2009.

Fiscal Summary

State Effect: None.

Local Effect: Minimal reduction in expenditures for a limited number of municipalities, taxing districts, and special taxing districts. Revenues are not affected.

Small Business Effect: None.

Analysis

Current Law: Municipalities and State-created taxing districts are required to have an independent audit conducted by a certified public accountant each year. However, municipalities and taxing districts with annual revenues of less than \$50,000 in the prior

four fiscal years may petition the Office of Legislative Audits (OLA) for a waiver allowing an audit to be conducted once every four years instead of annually.

Each county is responsible for establishing audit requirements for county-created special taxing districts. At a minimum, State law requires county-created special taxing districts to have an audit conducted annually unless annual expenditures are less than \$50,000, in which case an audit may be conducted once every four years. The county may require special taxing districts with expenditures less than \$50,000 to have an audit conducted more often on a case-by-case basis.

All municipalities and taxing districts are required to submit an annual financial report, also known as the Uniform Financial Report, to the Department of Legislative Services on November 1 of each year. This includes municipalities and taxing districts that have received a waiver from the annual audit requirement.

Background: Annual audits promote government accountability to citizens and other interested parties and provide a means for management to assess a government's financial performance and fiscal condition.

OLA performs a desk review of audit reports filed by each county, municipality, and taxing district in Maryland. This desk review consists of assessments of compliance with accounting and auditing standards, evaluations of compliance with certain State laws (for example, collateral for bank deposits), and analyses of selected financial data to identify potential financial problems relating to deficit funds balances, underfunded pension plans, or unfavorable trends and ratios over the most recent five-year period. OLA also reviews some special taxing district reports to ensure that counties are reviewing the reports for compliance with the provisions of the law and to identify instances in which required reports are not being submitted. The OLA fiscal 2007 desk audit included 14 counties, 148 municipalities, and 18 taxing districts.

The 2007 OLA desk review of local government audits included the following findings:

- 26 local governments contained disclosures that cash deposits were not fully collateralized or otherwise insured;
- 3 local governments had unreserved general fund deficit balances;
- 2 local governments had unfavorable trends and ratios;
- 1 local government had a significantly underfunded pension plan; and
- 3 special taxing districts did not file annual reports.

Currently, 12 of 17 entities with annual revenues/expenditures under \$50,000 have received a waiver allowing an audit to be performed once every four years. As shown in **Exhibit 1**, there are approximately 20 municipalities and taxing districts with revenues

between \$50,000 and \$250,000 that may be eligible to request a waiver from filing an annual audit, as provided in the bill.

All counties have authority to establish special taxing districts for limited purposes, such as providing drainage improvements or providing street lighting. In addition, the governing bodies of counties that have adopted charter home rule or code home rule also have broad authority under the Express Powers Act to create special taxing districts to carry out most municipal services. Special taxing districts encompass a broad range of units including entities created by the General Assembly and those created by counties and municipalities. Some special taxing districts resemble municipalities and provide a broad range of public services. Other districts exist for a limited purpose, such as the financing of specific infrastructure improvements. Despite sharing some features similar to counties and municipalities, these entities lack home rule authority and must come to the legislative body that created them in order to change the scope of their powers.

The State Department of Assessments and Taxation has identified at least 462 areas in the State that could be considered special taxing districts. **Exhibit 2** outlines certain county-created special taxing districts.

Exhibit 1

<u>County</u>	<u>Municipalities and Special Taxing Districts with Annual Revenues between \$50,000 and \$250,000</u>
Allegany	Barton, Bel Air STA, Midland, Mt.Savage STA
Caroline	Goldsboro, Henderson, Hillsboro
Frederick	Burkittsville
Garrett	Deer Park, Friendsville, Loch Lynn Heights
Montgomery	Barnesville, Brookeville, Drummond Citizens Committee, Glen Echo, Laytonsville, Oakmont STA
Queen Anne's/Talbot	Queen Anne
Washington	Sharpsburg
Wicomico	Mardela Springs

Exhibit 2
County Created Special Tax Districts

<u>County</u>	<u>Description</u>
Anne Arundel	Includes 2 special tax districts, 64 special community benefit districts, 16 shore erosion control districts, 11 waterway improvement districts
Baltimore City	At least 6 special tax districts
Garrett	11 separate sanitary districts
Howard	Water and sewer district, fire district
Montgomery	Includes 3 development districts, recreation, fire tax district, mass transit facilities, urban districts, noise abatement districts
Prince George's	4 special tax districts that include residential properties
Total	

State Fiscal Effect: For each additional municipality or taxing district that receives a waiver from filing an annual audit report, the number of desk audits performed by OLA each year will decrease. OLA advises that desk audits for smaller municipalities only take a few hours to perform, so workload and costs are not materially affected by the bill.

Local Fiscal Effect: The cost of the annual audit for municipalities and taxing districts varies greatly and is dependant on the annual revenues, expenditures, and fiscal complexity of the entity. According to data submitted by municipalities and taxing districts to the Department of Legislative Services in the Uniform Financial Report, for fiscal 2006 through 2008, municipalities and taxing districts in Maryland spend, on average, approximately \$9,400 annually for independent accounting and auditing. A sample of 17 municipalities with revenues less than \$50,000 annually showed an annual audit cost of approximately \$1,700.

Municipalities and taxing districts that receive a waiver from filing an annual audit may realize a minimal decrease in annual audit expenditures. A sample of 20 municipalities and taxing districts that have revenues between \$50,000 and \$250,000 report an average audit expense of \$3,400 annually for the past three years. The actual amount of savings that can be realized will vary for each entity as small municipalities often rely on outside accountants for services in addition to performing the annual audit. These services may still be required to complete the required Uniform Financial Report. Furthermore, municipalities and taxing districts that have annual audit requirements in their charter would not be able to request a waiver.

The number of county-created special taxing districts that would be affected cannot be reasonably ascertained at this time. The bill does not prohibit a county from requiring special taxing districts to perform an audit annually.

Additional Information

Prior Introductions: None.

Cross File: SB 146 (Senators Frosh and Madaleno) - Budget and Taxation.

Information Source(s): Comptroller's Office, Maryland Municipal League, Office of Legislative Audits, Department of Legislative Services

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Analysis by: Erik P. Timme

Direct Inquiries to:
(410) 946-5510
(301) 970-5510