2.36 Municipal Inspections

Introduction

The Department of Municipal and Provincial Affairs is responsible for matters relating to local government, municipal financing, urban and rural planning, water quality, and monitoring municipal activities. The Department administers the provisions of the *Municipalities Act* and *Regulations,* which provide the framework to govern municipalities and local service districts.

At 31 March 2004, there were 286 municipalities in the Province. The breakdown of their locations across the four regions in the Province is included in Figure 1.

Figure 1

Municipalities per Region
31 March 2004

Region	Number of Municipalities
Eastern	113
Central	90
Westem	63
Labrador	20
Total	**286**

Source: Department of Municipal and Provincial Affairs

The *Act* includes provisions for the monitoring of municipal activities, including the requirement to submit annual balanced budgets and audited financial statements, and requiring prior approval of long-term borrowing by the Minister. The Department included over $1 million in its 2003-04 budget to provide various support and inspection services to ensure sound financial management and administrative practices, program design and implementation, and municipal training.

Scope and Objectives

We completed our review of municipal inspections in November 2004. Our objective was to determine if the Department has adequate systems and procedures in place to ensure that financial information prepared by the municipalities is submitted and monitored, and municipal inspections are performed in accordance with the legislation.

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Conclusion

The Department of Municipal and Provincial Affairs does not always receive budgets and financial statements of municipalities within the deadlines established under the *Municipalities Act*. Furthermore, the Department was not performing the annual municipal inspections in accordance with the *Act*. Although the Department implemented a new computerized Municipal Information Management System (MIMS) in 2002, not all information required for monitoring municipalities has been input into the system. Details are as follows:

Budgets - 2004 Calendar Year

- Of the 286 municipalities, 247 (86%) adopted their 2004 budgets after the 1 December 2003 deadline. Adoption of the 2004 budgets ranged from 1 day to 133 days after the deadline.

- Of the 286 municipalities, 141 (49%) submitted their 2004 budgets to the Minister after the 31 December 2003 deadline. Submission of the 2004 budgets ranged from 2 days to 176 days after the deadline. As at 27 October 2004, information on 2004 budgets for 3 of the 286 municipalities had not been entered into MIMS.

- Of the 283 (286 - 3) budgets received by the Department, staff have not keyed detailed budget information into MIMS relating to 9 of these budgets. All 9 of these budgets were received by the Department after the due date and all are for municipalities under the Eastern Regional Office.

Financial Statements - 2003 Calendar Year

- Audit reports for 144 (50%) of 286 municipalities were not received by the Department by the 30 June 2004 deadline. Of these 144, 116 reports were received from 1 day to 116 days after the deadline while the remaining 28 are still not recorded in MIMS.

- Of the 258 (286 - 28) audited financial statements received by the Department, staff have not keyed detailed financial statement information into MIMS relating to 46 of these statements. Of the 46 financial statements, 18 were received by the Department prior to the due date. Of the 46 financial statements, 45 are for municipalities under the Eastern Regional Office and 1 is under the Western Regional Office.

- Our review of 48 audited financial statements indicated that 24 had expenditures in excess of budgeted figures, ranging from $1,791 to $322,937, and totalling over $1.5 million. There was no approval provided by the Minister for the municipalities to exceed the total budgeted expenditure; therefore, these 24 municipalities contravened the *Act*.

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- Inspection information on the 113 municipalities in the Eastern Region was not available. Of the 173 municipalities in Central, Western and Labrador where inspection information was available, 133 did not have the required annual inspection performed for 2003. Similarly, only 40 had inspections performed in 2002. As a result, the Department has not complied with the requirements of the *Municipal Affairs Act*. We note that the annual inspection requirement was removed from the *Act* in June 2004.

- Although we were unable to determine the extent of inspections of the 113 municipalities in the Eastern Region, from discussions with officials, it is clear that the requirement for annual inspections was not met in any of the last three years.

Even though financial management concerns were raised by the auditors of the municipalities, the Department took little action to address the concerns identified. Information provided by the auditors of the 48 municipalities we reviewed indicated financial management concerns during 2001 to 2003 such as accounts were not kept in satisfactory condition, tax roll assessments were not reconciled for the year, disbursement records were totally inadequate and not acceptable, the general ledger was not maintained during the year, and irregularities occurred relating to cash receipts.

Findings and Recommendations

The Regional Office Division of the Department of Municipal and Provincial Affairs is the first line of contact with the Department for municipalities, local service districts and the general public. The services provided to the municipalities by the Regional Offices include municipal inspection services, coordination and monitoring of capital works, assessment of infrastructure problems, and consultation and advice on legislative policy and financial matters related to municipal operations. The Municipal Finance Division of the Department is responsible for providing assistance to municipalities in the form of grants, subsidies and refinancing.

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Municipal Information Management System

In our 1999 Annual Report to the House of Assembly, we recommended that, in addition to ensuring that municipalities are in compliance with the *Municipalities Act*, the Department should track financial information required to adequately monitor municipal operations and to provide for timely analysis for decision making.

In 2001, xwave developed the Municipal Information Management System (MIMS), a web based real time system, to provide a central data system to collect information such as financial statements, budgets, population, tax rates and Departmental inspection results. The system was developed to eliminate data entry duplication and provide consistent information on municipalities. In 2002, the system became operational and the Municipal Profile and Finance modules of the system replaced the Regional Office Operating System that was used to track budgets, audited financial statements and inspections.

To adequately monitor the operations of municipalities in the Province, the Department has a need for appropriate, reliable and timely information. This information is essential to create a complete and accurate financial picture. From our review of documentation related to the development, training and application of MIMS, we found that MIMS does not provide the information required by the Department to monitor the operations of municipalities. In particular:

- Although regional office staff, who enter most of the financial data and are significant end users of the system, were involved in testing the system before it was implemented, they were not involved in systems development. In addition, there was no documentation or training provided to these staff to ensure that information was consistently entered into the new system. As a result, we found there was inconsistent use of negative and positive signs to indicate surpluses or deficits. Therefore, amounts could not be totalled in reports.

- The report generator included in MIMS is not user-friendly in that its functionality is limited to direct extractions, including a sort feature, and required users to have detailed knowledge of the various tables and system design. Departmental staff indicated that in order to produce useful reports, in many instances they had to either go to their IT division or use other software. Therefore, for example, there is no readily available comparison of budget and actual financial information (in a report format) for the analysts to use when discussing budgets and other financial matters with municipalities.

- Much of the data entered into MIMS cannot be easily printed, and therefore results in a duplication of effort. For example, although there are details on the MIMS screen which are required for attachment to budgets and financial statements, there is no print command on this screen to print this information. Instead, regional office staff indicated that they use a manual form to document their review of budgets and financial statements.

- There is no management review of the data entered into the system to verify that it is complete and correct. Also, MIMS is not used on a consistent basis among regions to track documents received, or to monitor actual municipal results. For example, the audited financial statement review screen information is currently being entered only by the Western Regional Office. This greatly reduces the usefulness of MIMS.

Budgets

The *Municipalities Act* requires that a town council, not later than 1 December, prepare and adopt a budget containing estimates of the revenue and expenditure of the council for the next financial year. The budget is required to be sent to the Minister by 31 December in the calendar year of its adoption.

In its response to our 1999 report on Municipal Debt, the Department indicated it would be tracking the status of the budget and financial statement submissions by municipalities, and would be placing greater priority on encouraging municipalities to submit the necessary financial documents on a timely basis. MIMS includes fields to track the dates financial information is adopted and received. We reviewed the information in MIMS as of 27 October 2004 and found that budget information was being adopted by the councils and was received by the Department after the deadlines. In particular:

2004 Budgets

- Of the 286 municipalities, 247 (86%) adopted their 2004 budgets after the 1 December 2003 deadline. Adoption of the 2004 budgets ranged from 1 day to 133 days after the deadline.

- Of the 286 municipalities, 141 (49%) submitted their 2004 budgets to the Minister after the 31 December 2003 deadline. Submission of the 2004 budgets ranged from 2 days to 176 days after the deadline. As at 27 October 2004, information on 2004 budgets for 3 of the 286 municipalities had not been entered into MIMS.

- Thirty municipalities were requested by the Department to provide revised budgets for 2004; however, our review indicated that only 10 of these revised budgets were subsequently entered into MIMS.

- Of the 283 (286 - 3) budgets received by the Department, staff have not keyed detailed budget information into MIMS relating to 9 of these budgets. All 9 of these budgets were received by the Department after the due date and all are for municipalities under the Eastern Regional Office.

2003 Budgets

- Of the 286 municipalities, 252 (88%) adopted their 2003 budgets after the 1 December 2002 deadline. Adoption of the 2003 budgets ranged from 1 day to 367 days after the deadline.

- Of the 286 municipalities, 166 (58%) submitted their 2003 budgets to the Minister after the 31 December 2002 deadline. Submission of the 2003 budgets ranged from 2 days to 312 days after the deadline. As at 27 October 2004, information on 2003 budgets for 3 of the 286 municipalities had not been entered into MIMS.

- Thirty-eight municipalities were requested by the Department to provide revised budgets for 2003; however, our review indicated that only 8 of these revised budgets were subsequently entered into MIMS.

2002 Budgets

- Of the 288 municipalities, 262 (91%) adopted their 2002 budgets after the 1 December 2001 deadline. Adoption of the 2002 budgets ranged from 2 days to 381 days after the deadline.

- Of the 288 municipalities, 206 (72%) submitted their 2002 budgets to the Minister after the 31 December 2001 deadline. Submission of the 2002 budgets ranged from 2 days to 361 days after the deadline. As at 27 October 2004, information on 2002 budgets for 3 of the 288 municipalities had not been entered into MIMS.

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Audited Financial Statements

The *Municipalities Act* provides deadlines for completion of audits and submission to the Minister of audit reports on the financial statements of municipalities. The timely submission of audit reports is important as the Department uses the audited financial statements to assess the financial position of the municipality, and is better able to assess their needs. Analysis of the financial statement data and the related report can provide insight into municipal operations both financial and administrative and if there are any problems, the Department can determine if assistance or further investigation is necessary.

Section 92 (1) of the *Municipalities Act* states that the auditor shall complete and submit the report on his or her audit to the council before June 1 of the year immediately following the financial year that he or she is auditing and, not more than 30 days later, the auditor shall submit a copy of that report to the Minister. In addition, Section 89 of the *Act* states that the Minister may waive the requirement of an audit for a council where he or she is satisfied that an inspection by the officials of his or her department is sufficient to ensure adequate financial control and accountability with respect to that council. However, Departmental officials indicate that no municipalities have been granted a waiver of their audit for the past two years.

We reviewed the information in MIMS as of 27 October 2004 and found that audited financial statements were received by the Department after the deadline. In particular:

<u>2003 Audited Financial Statements</u>

- Audit reports for 144 (50%) of 286 municipalities were not received by the Department by the 30 June 2004 deadline. Of these 144, 116 reports were received from 1 day to 116 days after the deadline while the remaining 28 are still not recorded in MIMS.

- Of the 258 (286 - 28) audited financial statements received by the Department, staff have not keyed detailed financial statement information into MIMS relating to 46 of these statements. Of the 46 financial statements, 18 were received by the Department prior to the due date. Of the 46 financial statements, 45 are for municipalities under the Eastern Regional Office and 1 is under the Western Regional Office.

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2002 Audited Financial Statements

- Audit reports for 135 (47%) of 288 municipalities were not received by the Department by the 30 June 2003 deadline. Of these 135, 125 reports were received from 1 day to 481 days after the deadline while the remaining 10 are still not recorded in MIMS.

2001 Audited Financial Statements

- 9 of 289 municipalities had their audit requirement waived.

- Audit reports for 148 (53%) of 280 municipalities requiring audits were not received by the Department by the 30 June 2002 deadline. Of these 148, 146 reports were received after the deadline (2 were not received until 2004) while the remaining 2 are still not recorded in MIMS.

In addition to our review of MIMS, we selected a sample of audited financial statements of 50 municipalities for the years ended 31 December 2003, 2002 and 2001 to determine if the financial statements were prepared and signed on a timely basis as per the *Act*, (i.e. by 1 June of the immediately following year) and to determine whether budgets were exceeded. Section 86 (2) of the *Act* stipulates that the financial statements must be signed by the mayor or chairperson and the treasurer by 1 June, and Section 81 of the *Act* states that a town council shall not, without prior approval of the Minister, incur … or become liable for expenditure … exceeding the total estimated expenditure in the annual or revised budget. Furthermore, auditors are required to submit their report to the Minister by 30 June.

Our review of the audited financial statements indicated that not all financial statements were signed and adopted as required, some municipalities exceeded their budgets without the approval of the Minister, and auditors did not always submit their report to the Minister by the 30 June deadline. In particular:

2003

- Of the 50 financial statements, 48 were provided while 2 were not submitted by the regional offices. Of the 48 audited financial statements we reviewed, 16 were dated after 1 June 2004 meaning that the audit was not completed in time for the municipality to adopt them in accordance with the *Act*, of which 9 were dated after 30 June 2004, thus also delaying submission to the Minister in contravention of the *Act*.

- Of the 48 audited financial statements we reviewed, 24 had expenditures in excess of budgeted figures, ranging from $1,791 to $322,937, and totalling over $1.5 million. There was no approval provided by the Minister for the municipalities to exceed the total budgeted expenditure. Therefore, these 24 municipalities contravened the *Act*.

- A review of the information provided by the auditors indicated financial management concerns at municipalities. These concerns included: accounts were not kept in satisfactory condition; tax roll assessments were not reconciled for the year; and disbursement records were totally inadequate and not acceptable.

- For 8 municipalities, the auditor indicated that adequate safeguards against fraud were not in place due to limited number of office staff.

2002

- All 50 audited financial statements were provided. Of the 50 audited financial statements we reviewed, 16 were dated after 1 June 2003 meaning that the audit was not completed in time for the municipality to adopt them in accordance with the *Act*, of which 8 were dated after 30 June 2003, thus also delaying submission to the Minister in contravention of the *Act*.

- Of the 50 audited financial statements we reviewed, 26 had expenditures in excess of budgeted figures, ranging from $179 to $1,935,463 and totalling over $3.6 million. There was no approval provided by the Minister for the municipalities to exceed the total budgeted expenditure. Therefore, these 26 municipalities contravened the *Act*.

- A review of the information provided by the auditors indicated financial management concerns at municipalities. These concerns included: the general ledger not being maintained during the year, taxes not being reconciled for the year, and irregularities relating to cash receipts.

- The auditor for one municipality indicated that "…during the year, it was discovered that funds had been misappropriated by the Acting Town Clerk in 2001 and 2002." It was further indicated that the auditor was unable to verify the cash balance.

- For 12 municipalities, the auditor indicated that adequate safeguards against fraud were not in place due to limited number of office staff.

2001

- Of the 50 financial statements, 48 were provided while 2 were not submitted by the regional offices. Of the 48 audited financial statements we reviewed, 18 were dated after 1 June 2002, meaning that the audit was not completed in time for the municipality to adopt them in accordance with the *Act*, of which 15 were dated after 30 June 2002, thus also delaying submission to the Minister in contravention of the *Act*.

- Of the 48 audited financial statements we reviewed, 36 had expenditures in excess of budgeted figures ranging from $4,840 to $324,974 and totaling over $2.2 million. There was no approval provided by the Minister for the municipalities to exceed the total budgeted expenditure. Therefore, these 36 municipalities contravened the *Act*.

- A review of the information provided by the auditor of one municipality indicated financial management concerns with irregularities relating to cash receipts.

- For 12 municipalities, the auditor indicated that adequate safeguards against fraud were not in place due to limited number of office staff.

Of the 146 audited financial statements that we reviewed in total, 87 (60%) were not signed by municipal officials in accordance with the *Act*. Departmental officials indicated that the auditors will often forward unsigned financial statements to the Department; however, the auditors should have signed copies of the financial statements in their files and only signed copies should be forwarded.

Municipal Inspections

The Regional Office Division is responsible for completing municipal inspections. The process for an inspection involves a visit to the municipality and completion of a checklist. Division staff will review a series of topics and documents relevant to municipal operations. The purpose is to assess a municipality's financial and administrative performance through the examination of records - budgets, financial statements, meetings, etc. This monitoring tool serves as a valuable

contact between municipalities and the Department. The inspections provide an opportunity to meet with town staff, review their work since the last visit, and assist them in any administrative activities.

Prior to June 2004, Section 4 (2) of the *Municipal Affairs Act* required that the books and records of every municipality be inspected at least once in every year and that the Minister may order a special inspection whenever considered advisable. An amendment, effective June 2004, removed the requirement for annual inspections.

The Department provided information on the inspection statistics for each of the regions for the last three years. This information is outlined in Figure 2.

Figure 2

Total Municipal Inspections
As of November 2004

Region	Number of Municipalities	2002 Inspections	2003 Inspections	2004 Inspections
Eastern	113	Not available	Not available	Not available
Central	90	21	18	8
Western	63	19	22	14
Labrador	20	0	0	0

Source: Department of Municipal and Provincial Affairs

Our review of the Department's inspection activity indicated that the Department is not performing the required inspections and information on inspections is not readily available. In particular:

- The only information reported in MIMS for 2003 and 2004 related to the Central Region while in 2002 information was only provided on the Central Region and the Western Region. Furthermore, the information in MIMS did not agree with the statistics provided by the Department and outlined in Figure 2. For example:
    - For 2004, MIMS shows 12 municipal inspections were conducted relating to the Central Region (Department reported 8).

- For 2003, MIMS shows 21 municipal inspections were conducted, all relating to the Central Region (Department reported 18).

- For 2002, MIMS shows 25 municipal inspections were conducted, 23 of the municipalities were in the Central Region (Department reported 21) and 2 of the municipalities were in the Western Region (Department reported 19).

- As Figure 2 indicates, inspection information from the Eastern Region was not available. Although we were unable to determine the extent of inspections in this region, from discussions with officials, it is clear that the requirement for annual inspections was not met in any of the last three years.

- Of the 173 municipalities in Central, Western and Labrador, 133 did not have the required annual inspection performed for 2003. Similarly, only 40 had inspections performed in 2002. As a result, the Department has not complied with the requirements of the *Act*. However, we note that the annual inspection requirement was removed from the *Act* in June 2004.

Recommendations

The Department should:

- *ensure that data entered into its Municipal Information Management System (MIMS) is accurate and is input on a timely basis;*

- *take action to ensure that budgets and financial statements are submitted in compliance with the* Municipalities Act;

- *follow-up on all issues identified by the municipalities' auditors; and*

- *establish a frequency for municipal inspections given that the annual inspection requirement has been removed from the* Municipal Affairs Act.

Department's Response

The Municipal Information Management System became operational in 2002. As with any new database system, it has taken some time with the system in actual use to identify operational weaknesses. While it is acknowledged that some of these weaknesses have contributed to the integrity of some of the data, we are confident that recent upgrades to the system and additional training provided to the Department's Municipal Analysts, who are responsible for inputting the data, will ensure, on a go forward basis that the data contained in the system is accurate. These system upgrades and training initiatives will also ensure that data is input to the system on a more timely basis.

While it is acknowledged that a number of municipalities in recent years have not complied with the statutory time lines for the submission of budgets and financial statements, the situation is improving. Steps taken by the Department over the past couple of years to withhold Municipal Operating Grants and to make municipalities that do not comply with predetermined submission deadlines ineligible for Municipal Capital Works funding, have resulted in budgets and financial statements being received by the Department in a much more timely manner than in the past. The Department will continue with this policy with the goal of having all municipalities comply with the statutory submission requirements.

While it may not always be documented in written form, the Department does address with municipalities any significant accounting, administrative or other concerns raised by their auditors in the course of their annual audits. This is often done through telephone discussions between departmental officials and municipal administrative personnel or through meetings with the respective councils.

The major focus of the Department's inspection activities in recent years has been targeted to those municipalities that have received assistance under the Debt Relief Program. While this focus will continue, starting this year, the Department has also begun inspections of the 184 Local Service Districts in the province. These inspections which will continue next year will be in addition to inspections of municipalities other than those under the Debt Relief Program for which the Department determines that this form of departmental intervention is necessary.

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