



CHAPTER-V

Financial Reporting in Urban Local Bodies

CHAPTER V
URBAN DEVELOPMENT DEPARTMENT
FINANCIAL REPORTING IN URBAN LOCAL BODIES
5.1 Framework

5.1.1 Financial reporting in the public sector is a key element of accountability. According to the Karnataka Municipalities Accounting and Budgeting Rules, 2006 (KMABR), the Urban Local Bodies (ULBs) shall prepare the financial statements consisting of Receipts and Payments Account, Balance Sheet and Income and Expenditure Account along with Notes on Accounts in the form and manner prescribed and submit them to the auditor appointed by the State Government, within two months from the end of the financial year.

5.1.2 Municipal reforms

The initiative of municipal reforms was started during 2006 through the 'Nirmala Nagara' programme whose components, among others, included accounting reforms, computerisation of municipal functions, setting up public grievance redressal system, etc. Only 57 ULBs, including eight⁵⁹ City Municipal Councils (CMCs) which merged with Bruhat Bengaluru Mahanagara Palike (BBMP) were covered under this programme. These reforms are now adopted by the remaining ULBs of the State under Karnataka Municipal Reforms Project (KMRP).

The Municipal Reforms Cell (MRC) working under Directorate of Municipal Administration (DMA) is responsible for computerisation and maintaining accounts on Fund Based Accounting System (FBAS) in ULBs (except BBMP). To bring in better governance and more efficient service delivery through the use of technology and process re-engineering, the State Government initiated (2005) the process of computerisation of municipal functions in all the ULBs of the State in a phased manner.

5.1.3 Accounting reforms

On the recommendations of Eleventh Finance Commission, Government of India (GoI) entrusted the responsibility of prescribing appropriate accounting formats for the ULBs to the Comptroller and Auditor General of India (CAG).

The Ministry of Urban Development, GoI developed the National Municipal Accounts Manual (NMAM) as recommended by the CAG's Task Force. The State Government brought out the KMABR based on the NMAM with effect from 1 April 2006. KMABR was introduced in a phased manner in all the ULBs except BBMP. As of 31 March 2014, all the ULBs were preparing the fund-based accounts in double entry system. BBMP was maintaining FBAS based on the Bangalore Mahanagara Palike (Accounts) Regulations, 2001.

⁵⁹ Bommanahalli, Bommasandra, Bytarayanapura, Dasarahalli, Kengeri, Krishnarajpuram, Rajarajeshwarinagar and Yelahanka

5.1.4 Preparation and certification of accounts of ULBs

According to KMABR, the financial statements of ULBs should be audited by the Chartered Accountants (CAs) appointed by the DMA. The Commissioner/Chief Officer of ULBs concerned should submit the Annual Financial Statements for each year within two months from the end of financial year to the financial auditor and the auditor should complete the audit within four months (July) from the date of closure of financial year. The CA, after completion of audit, should submit a report along with the audited accounts to the Municipal Council and the State Government. The Audited Accounts should be adopted by the Council within five months from the end of financial year. **Table 5.1** below indicates the position of accounts prepared by ULBs and certified by the CAs during 2009-14 (December 2014).

Table 5.1: Position of preparation and certification of accounts as on December 2014

Year	Total number of ULBs required to prepare accounts	Number of ULBs which prepared the accounts	Number of ULBs accounts certified	Number of ULBs accounts yet to be certified
2009-10	213	213	213	0
2010-11	213	213	213	0
2011-12	213	213	212	01
2012-13	213	213	202	11
2013-14	213	213	75	138
Total	1,065	1,065	915	150

Source: As furnished by DMA

It could be observed that, 150 Accounts prepared for the years 2011-14 were yet to be certified.

5.1.5 Preparation and certification of accounts of BBMP

In terms of Provision 9 (2) of part II of Schedule IX to the KMC Act, the Commissioner, BBMP is required to make ready the Annual Accounts for the year 2013-14 and produce the same along with relevant records to the Chief Auditor for scrutiny not later than the first day of October 2014. However, BBMP has not prepared the Annual Financial Statements for the year 2013-14 for want of information from unit offices. The Controller, State Accounts Department (SAD) is the Statutory Auditor for BBMP. BBMP had submitted the Annual Accounts for the years 2008-13 to the SAD for scrutiny, which are yet to be certified (February 2015).

BBMP in its reply, stated (January 2015) that a request was made to Controller, SAD in November 2014 to certify the accounts early.

5.2 Comments on Accounts

5.2.1 Statement of expenditure for deposits with external agencies

As per Rule 73 of KMABR, the amount paid to Public Works Department/other external agencies should be treated as advance and a statement showing the outlay incurred during each month with up-to-date

figures should be obtained and adjusted against the advances paid. Five⁶⁰ test-checked ULBs had released ₹3.53 crore during 2012-13 as advances to external agencies but did not take any action to obtain statement of expenditure along with unspent amount, if any, and adjust it against the advances.

5.2.2 Fixed Assets

None of the tests-checked ULBs had maintained the records showing full particulars including quantitative details and location of fixed assets and conducted the physical verification of fixed assets during the five years ended 31 March 2013. In the absence of this, the correctness of valuation of fixed assets and impact on depreciation exhibited in the Annual Financial Statements of test-checked ULBs could not be assessed.

5.2.3 Advances to Employees for exigencies

In six⁶¹ test-checked ULBs, an amount of ₹4.02 crore given to employees as advance for incurring specific and urgent expenditure was outstanding for recovery/adjustment over five years as on 31 March 2013. However, no action was taken by the ULBs to obtain the details of expenditure and recover the amount.

5.2.4 Investments

Audit observed that four⁶² ULBs had invested ₹18.14 crore in term/fixed deposits and Government securities as on 31 March 2013 without Government sanction/approval.

5.3 Borrowings

As per Section 154 (1) of the KMC Act, City Corporations (CCs) may, after passing a resolution at a special general meeting of the Council, with previous sanction of the State Government, borrow funds for asset creation and repayment of loan.

In terms of section 86 of KM Act, the CMCs, Town Municipal Councils (TMCs) and Town Panchayats (TPs) may borrow money required for constructing any work of a permanent nature which it is required or empowered to undertake under the provisions of this Act, or for acquisition of land, from the Government, any bank, corporation or person, after passing a resolution at a special General Meeting of the Council, with previous sanction of the State Government. The amount so borrowed is subject to such conditions as may be prescribed by the Government as to security, the rate of

⁶⁰ CCs, Mysuru (₹2.80 crore) and Kalaburagi (₹0.05 crore); CMC, Shahabad (₹0.25 crore); TMCs, Hunsur (₹0.41 crore) and Wadi (₹0.02 crore)

⁶¹ CC, Mysuru (₹3.07 crore); CMC, Shahabad (₹0.36 crore); TMCs, Hunsur (₹0.19 crore); Nanjangud (₹0.18 crore); Wadi (₹0.13 crore) and Aland (₹0.09 crore)

⁶² CCs, Kalaburagi (₹3.4 crore); Mysuru (₹7.26 crore); TMCs, Hunsur (₹3.16 crore) and Wadi (₹4.32 crore)

interest and the repayment of principal and interest. The details of borrowings in test-checked ULBs are given in **Table 5.2**.

Table 5.2: Details of Borrowing in the selected ULBs

(₹ in crore)

Year	CC, Mysuru	CC, Kalaburagi	CMC, Shahabad	TMC, Aland	TMC, Hunsur	TMC, Nanjangud	TMC, Wadi
2009-10	96.64	1.58*	Nil	Nil	0.43 ^{&}	0.63 ^{&}	Nil
2010-11	111.01	1.53*	Nil	Nil	0.43 ^{&}	0.54 ^{&}	Nil
2011-12	146.89	1.48*	Nil	Nil	0.43 ^{&}	0.44 ^{&}	Nil
2012-13	146.89	1.46*	Nil	Nil	0.43 [@]	0.35 ^{&}	Nil
2013-14	NF	1.46 [#]	Nil	Nil	NF	NF	NF

Source: Financial statements of ULBs

NF: Not furnished

* Audited and secured; # Secured and unaudited; & Unsecured and audited; @ Unsecured and unaudited

On a review of financial statements of above ULBs with reference to records maintained by them during the years 2009-14, the following observations are made:

5.3.1 Borrowings in Kalaburagi City Corporation

CC, Kalaburagi borrowed (October 2008) long term loan of ₹1.50 crore on security of term deposit made in Indian Bank and utilised it for the wages of contract labourers. However, it was not approved by the Council in General Body meeting. Thus, ₹1.50 crore borrowed and utilised was irregular.

Karnataka Urban Water Supply & Drainage Board (KUWS&DB) on behalf of CC, Kalaburagi raised a loan of ₹35.01 crore from Housing and Urban Development Corporation Limited (HUDCO) and ₹4.21 crore from Life Insurance Corporation of India (LIC) during 2001-04 for execution of Improvement to Infrastructure works (underground drain) of Kalaburagi City. Against this loan, the KUWS&DB repaid the loan principal of ₹36.35 crore up to 31 March 2014 out of State Finance Commission grants. However, this loan account had not been taken to the books of accounts of CC, Kalaburagi as envisaged in rule 73 of KMABR for accounting of delegated loans.

5.3.2 Sinking fund in Mysuru City Corporation

In terms of Section 160 of the KMC Act, the corporation shall maintain sinking funds for the repayment of moneys borrowed on debentures issued by the corporation. The money paid into sinking funds should be invested in Government securities. The CC, Mysuru created sinking fund to the extent of ₹0.24 crore and exhibited the same in its Financial Statement of Accounts. However, the purpose and period of sinking fund created and details of investment made in Government securities out of sinking fund was not on record.

5.4 Thirteenth Finance Commission grants

The Thirteenth Finance Commission (TFC) was constituted to recommend the measures needed to augment the consolidated funds of the States to supplement the resources of the Panchayat Raj Institutions (PRIs) and ULBs. The Commission recommended grant-in-aid to the local bodies as a percentage of the previous year's divisible pool of taxes, over and above the share of the States.

The GoI released general basic grants of ₹304.68 crore and performance grants of ₹208.05 crore for the year 2013-14 to ULBs in two instalments.

5.4.1 Delayed release of funds

The TFC guidelines stipulated that the funds should be transferred to the accounts of ULBs within five days from the date of receipt of grant from GoI, failing which the State Government would be liable to release the instalment with interest at the Reserve Bank of India (RBI) rate for the delayed period. The GoI released the instalments during February 2014, March 2014 and July 2014. Audit observed that there were delays ranging from 10 to 27 days in transfer of funds to ULBs. The interest of ₹1.92 crore for the delay in transferring of funds was not released to ULBs by State Government.

5.4.2 Poor utilisation of TFC grants by the test-checked ULBs

Out of ₹101.16 crore received by the test-checked ULBs during the period 2010-14, only ₹34.81 crore (ranging from 11 to 41 per cent) as detailed in **Table 5.3**, was utilised.

Table 5.3: Details of TFC grants in test-checked ULBs

Name of the ULB	Grants released					Amount utilised	Balance	Percentage of utilisation
	2010-11	2011-12	2012-13	2013-14	Total			
TMC, Aland	0.51	0.97	1.32	1.18	3.98	0.43	3.55	11
CC, Kalaburagi	2.93	5.56	14.17	8.05	30.71	10.15	20.56	33
TMC, Hunsur	0.63	1.20	1.77	1.91	5.51	1.73	3.78	31
TMC, Nanjangud	0.56	1.06	1.68	1.37	4.67	1.76	2.91	38
CC, Mysuru	5.13	9.76	21.07	12.01	47.97	17.84	30.13	37
CMC, Shahabad	0.56	1.07	1.44	0.91	3.98	1.65	2.33	41
TMC, Wadi	0.59	1.05	1.35	1.35	4.34	1.25	3.09	29
Total	10.91	20.67	42.80	26.78	101.16	34.81	66.35	34

Source: As furnished by ULBs

5.4.3 Non-maintenance of separate cash book and bank account

It was observed that test-checked ULBs (except BBMP) had not maintained separate bank account as envisaged in the guidelines and no separate cash book was maintained for TFC grants.

BBMP had not maintained cash book or any other records/grant register for recording the grant-wise receipt and component-wise expenditure of TFC grants during the year 2013-14. BBMP had submitted the Utilisation Certificate (UC) to the State Government in March 2014 for the entire amount of General Basic Grant of ₹34.69 crore received during the year 2013-14. In the absence of basic records, cash book and grant register, the correctness of grant receipts and component-wise expenditure mentioned in the UC submitted to the State Government could not be assessed.

These issues would not only impact the process of obtaining UCs but there was also the risk of misappropriation of funds.

BBMP in its reply, stated (January 2015) that the cash book was maintained. On verification, Audit noticed that cash book maintained was incomplete as only payment details were recorded.

5.4.4 Diversion of grant

BBMP had diverted TFC grant of ₹44.20 crore for payment of salaries and advances to works not covered under TFC grants. This was done by irregularly transferring the funds from TFC grant to the General Fund bank account of BBMP.

BBMP, in its reply, stated (January 2015) that the diversion was made to meet the emergency requirement of finance and ₹25.00 crore out of ₹44.20 crore diverted was recouped.

It was also observed in CC, Mysuru that TFC grant amounting to ₹11.86 crore was utilised for payment of Jawaharlal Nehru National Urban Renewal Mission (JNNURM) project contribution (₹8.21 crore) and other works (₹3.65 crore) which were not included in the action plan approved for utilisation of TFC grant.

5.4.5 Non-preparation of action plan by BBMP

As per guidelines issued (18 August 2010) by the State Government for utilisation of TFC Grants, an Action Plan was required to be prepared and approved by Council/Government before utilisation of grants. However, no such Action Plan was prepared and got approved by the Council before utilisation of grants.

BBMP in its reply, stated (January 2015) that the action plan was incorporated in the regular budget of BBMP. However, the fact remains that BBMP had not prepared the action plan work-wise and component-wise for utilisation of fund.

5.5 Internal control

The State Government did not have Internal Audit Wing to oversee the functions of ULBs. Further, it was observed that ULBs were not adhering to financial rules as the statement of expenditure was not obtained and Annual

Accounts were not prepared and certified within the stipulated dates. Non-maintenance of cash books, bank books and mandatory registers indicated inadequate internal control system in ULBs. Further, there was no system of conducting physical verification of stores in the seven test-checked ULBs.

The Annual Accounts of BBMP were not prepared and certified within the stipulated dates. The ledger accounts prepared under FBAS were not properly balanced at the end of each financial year. The bank accounts were not reconciled periodically. Cash books, grant registers and records envisaged in fund based accounting manual for recording the transactions out of borrowings were not maintained. Internal audit system was not in existence in BBMP. These deficiencies in maintenance of books of accounts and absence of internal audit system indicated that the internal control was not effective in BBMP.

5.6 Conclusion

In spite of preparation of accounts by ULBs, there was shortfall in certification of accounts by CAs during the years 2011-14. Annual Accounts of BBMP for the years 2008-13 were not yet certified. Statement of expenditure was not obtained from external agencies to which ULBs had paid advances. The ULBs did not utilise the entire TFC grants during the period 2010-14. Internal control mechanism was inadequate as there was no Internal Audit Wing and there were instances of non-maintenance of cash books and bank books.