

## Chapter-III

### Urban Development Department

#### Accountability framework and financial reporting in Urban Local Bodies

#### 3.1 Introduction

The 74<sup>th</sup> Constitutional amendment enacted in 1992 envisaged creation of local self-governments for the urban population. The amendment sought to empower Urban Local Bodies (ULBs) to function efficiently and effectively as autonomous entities to deliver services for economic development and social justice with regard to 18 subjects listed in the Twelfth Schedule of the Constitution. The category-wise ULBs in the State are shown in **Table 3.1**.

**Table 3.1: Category-wise ULBs in Karnataka State**

Urban Local Bodies	Number of ULBs
City Corporations (CCs)	11
City Municipal Councils (CMCs)	58
Town Municipal Councils (TMCs)	116
Town Panchayats (TPs)	91
Notified Area Committees (NACs)	4

Source: Information furnished by the Department

CCs are governed by the Karnataka Municipal Corporations Act, 1976, (KMC Act) and other ULBs are governed by the Karnataka Municipalities Act, 1964 (KM Act). Each Corporation/Municipal area has been divided into a number of wards, which are determined and notified by the State Government considering the population, geographical features, economic status, *etc.*, of the respective area.

#### 3.2 Organisational structure

The Urban Development Department (UDD), headed by the Additional Chief Secretary to the Government, is the nodal department. The Directorate of Municipal Administration (DMA), established in December 1984, is the nodal agency which is responsible for the administrative, development and financial activities of ULBs except Bruhat Bengaluru Mahanagara Palike (BBMP), which functions directly under UDD.

All ULBs have a body comprising Corporators/Councillors elected by the people under their jurisdiction. The Mayor/President who is elected by the Corporators/Councillors presides over the meetings of the Council and is responsible for governance of the body. While ULBs other than BBMP have four Standing Committees, BBMP has 12 Standing Committees. The Commissioner/Chief Officer is the executive head of ULBs. The organisational structure with respect to functioning of ULBs in the State is given in **Appendix 3.1**.

### 3.3 Devolution of Functions

The 74<sup>th</sup> Constitutional amendment envisaged devolution of 18 functions listed in the Twelfth Schedule of the Constitution to ULBs. As per the information furnished (November 2017) by the Director of Municipal Administration, the State Government had transferred 17 functions, and Fire Services function had not been transferred to ULBs.

### 3.4 Accountability framework

#### 3.4.1 Powers of the State Government

As per the Acts governing ULBs, the State Government has the following powers for monitoring the proper functioning of ULBs:

- to frame rules to carry out the purposes of KMC and KM Acts;
- to dissolve those ULBs which fail to perform or default in the performance of any of the duties imposed on them;
- to cancel a resolution or decision taken by ULBs if the State Government is of the opinion that it has not been legally passed or is in excess of the powers conferred by provisions of the Acts; and
- to regulate classification, method of recruitment, conditions of service, pay and allowance, discipline and conduct of the staff and officers of ULBs.

#### 3.4.2 Vigilance mechanism

The Lokayukta appointed by the State Government has the power to investigate and report on allegations or grievances relating to the work and conduct of officers and employees of ULBs.

#### 3.4.3 Audit mandate

**3.4.3.1** The Principal Director, Karnataka State Audit and Accounts Department (KSAD), is the primary Auditor of ULBs in terms of KMC and KM Acts. The status of audit by KSAD during the period 2013-14 to 2017-18 in respect of ULBs is shown in **Table 3.2**.

**Table 3.2: Statement showing the details of audit of ULBs by KSAD as of December 2018**

Year	CC		CMC		TMC/TP/NAC	
	Total	Audited	Total	Audited	Total	Audited
2013-14	7	7	44	43	168	167
2014-15	7	4	44	39	168	166
2015-16	10	6	56	48	208	189
2016-17	11	1	56	37	208	163
2017-18	11	1	56	17	210	78

Source: Information furnished by KSAD

**3.4.3.2** The State Government entrusted (May 2010) the audit of accounts of all ULBs except NACs to the Comptroller and Auditor General of India (CAG) under Section 14 (2) of CAG's Duties, Powers and Conditions of

Service (DPC) Act, 1971, with effect from 2008-09 and under Technical Guidance and Supervision (TGS) with effect from 2011-12 onwards, by amending the statutes (October 2011). At the end of March 2018, 135 ULBs were audited under TGS module for the year 2017-18.

#### 3.4.4 Response to Inspection Reports

As of March 2018, 445 Inspection reports (IRs) consisting of 8,261 paragraphs were outstanding in various ULBs as detailed in **Table 3.3**.

**Table 3.3: Statement showing the details of outstanding IRs and paragraphs up to the audit period 2016-17**

Unit	5 to 10 years (2008-09 to 2012-13)		3 to 5 years (2013-14 to 2014-15)		2015-16		2016-17		Total	
	IRs	Paras	IRs	Paras	IRs	Paras	IRs	Paras	IRs	Paras
ULBs other than BBMP	110	1,321	77	1,773	53	1,502	56	1,720	296	6,316
BBMP	19	341	59	674	45	645	26	285	149	1,945
<b>Total</b>	<b>129</b>	<b>1,662</b>	<b>136</b>	<b>2,447</b>	<b>98</b>	<b>2,147</b>	<b>82</b>	<b>2,005</b>	<b>445</b>	<b>8,261</b>

Source: Inspection Reports

Out of 445 IRs outstanding, 265 IRs (60 *per cent*) containing 4,109 paragraphs (50 *per cent*) were pending for more than three years, indicating inadequate action on the part of ULBs. The details about IRs and paragraphs outstanding are in **Appendix 3.2**.

#### 3.4.5 Internal Audit

The State Government did not have an Internal Audit Wing to oversee the functions of ULBs. The DMA stated that the Government approved (August 2018) the upgradation of the Directorate of Municipal Administration and has sanctioned additional posts, which would be utilised for establishing the internal audit wing.

#### 3.4.6 Property Tax Board

The Thirteenth Finance Commission recommended that State Governments must put in place a state level Property Tax Board, which would assist all municipalities and municipal corporations in the State to put in place an independent and transparent procedure for assessing property tax. Further, Sections 102A to 102Y under Chapter IX-A of KMC Act provide for establishment of the Karnataka Property Tax Board by the State Government.

The Property Tax Board was not yet established in the State (November 2018).

### 3.5 Financial profile and reporting framework

#### 3.5.1 Financial profile

##### 3.5.1.1 Resources of Urban Local Bodies

The finances of ULBs include receipts from own sources, grants and assistance from Government of India (GoI)/State Government and loans from financial institutions or nationalised banks as the State Government may approve. ULBs do not have a large independent tax domain. The property tax on land and buildings is the mainstay of ULB's own revenue. While the authority to collect certain taxes is vested with ULBs, the authority pertaining to the rates and revision thereof, procedure of collection, method of assessment, exemptions, concessions, *etc.*, is vested with the State Government. The own non-tax revenue of ULBs comprises fee for sanction of plans/mutations, water charges, *etc.*

##### 3.5.1.2 Release of grants to Urban Local Bodies

The details of grants<sup>7</sup> released by the State Government to ULBs during the period 2013-14 to 2017-18 are shown in **Table 3.4**.

**Table 3.4: Statement showing release of grants**

(₹ in crore)

ULBs	2013-14		2014-15		2015-16		2016-17		2017-18	
	Budget	Grants released	Budget	Grants released	Budget	Grants released	Budget	Grants released	Budget	Grants released
CCs	4,348	3,632	4,956	4,372	4,435	4,307	4,233	4,099	5,000	4,457
CMCs/TMCs	1,629	1,139	1,589	1,365	1,644	1,555	1,488	1,368	1,754	1,660
TPs/NACs	344	248	312	273	233	214	259	219	383	373
<b>Total</b>	<b>6,321</b>	<b>5,019</b>	<b>6,857</b>	<b>6,010</b>	<b>6,312</b>	<b>6,076</b>	<b>5,980</b>	<b>5,686</b>	<b>7,137</b>	<b>6,490</b>

Source: State Budget Estimates and Finance Accounts

It can be observed from the table that the allocated quantum of funds was not released to ULBs during any of the years from 2013-14 to 2017-18. The actual releases to ULBs showed an increasing trend during the years 2013-14 to 2017-18 except during 2016-17 when the releases decreased by six *per cent* as compared to 2015-16.

##### 3.5.1.3 Short release of funds

As per recommendations (December 2008) of the Third State Finance Commission and decision of the State Government (October 2011), 10 *per cent* (₹9,360.69 crore) of Non-Loan Net Own Revenue Receipts (NLNORR) was to be released to ULBs during 2017-18. As against this, the State Government had only released 6.93 *per cent* (₹6,489.76 crore) of NLNORR (₹93,606.91 crore), resulting in short release of ₹2,870.93 crore to ULBs during 2017-18.

<sup>7</sup> Grants include State Finance Commission grants, Fourteenth Finance Commission grants, grants released for Centrally sponsored schemes and State schemes.

### 3.5.1.4 Release of Fourteenth Finance Commission grants

GoI released total basic grants of ₹899.25 crore, in two equal instalments to ULBs during the year 2017-18. However, the performance grants for the year 2017-18 were not released as of March 2018.

### 3.5.1.5 Status of collection of Property Tax

The State Government had introduced the Self-Assessment Scheme (SAS) for payment of property tax applicable to all Municipalities of the State with effect from 1 April 2002. The position of property tax demanded, collected and outstanding at the end of March 2018 in respect of all ULBs (except BBMP) and targets fixed and collections against targets in respect of BBMP are shown in **Tables 3.5** and **3.6** respectively.

**Table 3.5: Position of demand, collection and balance of Property Tax in ULBs**

(₹ in crore)

Year	Opening balance	Current year demand	Total demand	Collection	Balance	Percentage of collection to total demand
2013-14	218.19	368.44	586.63	364.95	221.68	62
2014-15	221.68	458.01	679.69	423.44	256.25	62
2015-16	256.25	569.67	825.92	481.27	344.65	58
2016-17	344.65	679.46	1,024.11	553.56	470.55	54
2017-18	470.55	774.15	1,244.70	674.09	570.61	54

Source: Details furnished by DMA

From the above table, it can be seen that arrears of property tax had increased from ₹221.68 crore in 2013-14 to ₹570.61 crore in 2017-18 and the collection decreased from 62 per cent during 2013-14 to 54 per cent during 2017-18.

**Table 3.6: Position of target and collection of property tax in BBMP**

(₹ in crore)

Year	Budget estimate	Actual collection	Percentage of collection
2013-14	3,200.00	908.06	28
2014-15	2,135.00	1,176.01	55
2015-16	1,900.00	1,244.98	66
2016-17	2,300.00	1,452.57	63
2017-18	2,600.00	1,551.90	60

Source: Budget and details furnished by BBMP

BBMP did not achieve the targets for collection of property tax during the period 2013-14 to 2017-18 and the collection decreased from 66 per cent during 2015-16 to 60 per cent during 2017-18.

### 3.5.1.6 Non/short remittance of cess

Section 108A of KMC Act provides for levy and collection of Property Tax along with the applicable cess such as health, library and beggary cess in respect of City Corporations including BBMP. Further, Section 4A of the Health Cess Act, 1962, Section 30 (4) of the Karnataka Public Libraries Act,

1965 and Section 31 of the Karnataka Prohibition of Beggary Act, 1975 state that the cess<sup>8</sup> collected by the local authorities as per the respective Cess Acts shall be remitted to the departments concerned and the local bodies are entitled to deduct 10 per cent of cess collected and retain as collection charges.

Scrutiny of the information furnished by DMA and BBMP showed that huge balances of cess collected during the period 2013-14 to 2017-18 were not remitted to the departments concerned as detailed in the **Table 3.7** and **Table 3.8** respectively:

**Table 3.7: Details of Collection, remittance and balance of cesses in ULBs (other than BBMP)**

(₹ in crore)

Year	Health Cess				Library Cess				Beggary Cess			
	OB	C	R	CB	OB	C	R	CB	OB	C	R	CB
2013-14	152.94	39.79	16.69	176.04	28.87	16.08	14.27	30.68	30.76	8.03	8.07	30.72
2014-15	176.04	47.42	20.65	202.81	30.68	19.11	13.99	35.80	30.72	9.68	6.58	33.82
2015-16	202.81	52.07	15.56	239.32	35.80	21.45	16.63	40.62	33.82	10.49	7.15	37.16
2016-17	239.32	59.47	26.97	271.82	40.62	24.59	19.58	45.63	37.16	18.95	44.96	11.15
2017-18	271.82	67.06	24.91	313.97	45.63	26.84	18.77	53.70	11.15	16.77	8.72	19.20

Source: Information furnished by DMA

C: Collected R: Remitted

It can be seen from the above table that the ULBs in the State have not remitted ₹313.97 crore of health cess, ₹53.70 crore of library cess and ₹19.20 crore of beggary cess to the departments concerned.

**Table 3.8: Details of collection, remittance and balance of cesses in BBMP**

(₹ in crore)

Year	Health cess			Library cess			Beggary cess		
	Collected	Remitted	Balance	Collected	Remitted	Balance	Collected	Remitted	Balance
2013-14	136.20	0	136.20	54.48	18.50	35.98	27.24	15.00	12.24
2014-15	176.40	0	176.40	70.56	8.00	62.56	35.28	5.00	30.28
2015-16	186.74	0	186.74	74.69	58.08	16.61	37.34	12.67	24.67
2016-17	217.88	0	217.88	87.15	50.00	37.15	43.57	20.00	23.57
2017-18	232.78	0	232.78	93.11	14.00	79.11	46.56	19.22	27.34
<b>Total</b>	<b>950.00</b>	<b>0</b>	<b>950.00</b>	<b>379.99</b>	<b>148.58</b>	<b>231.41</b>	<b>189.99</b>	<b>71.89</b>	<b>118.10</b>

Source: Information furnished by BBMP

While BBMP had not remitted the entire health cess of ₹950 crore collected to the State Government, the balance of library cess (₹231.41 crore) and beggary cess (₹118.10 crore) was not remitted to the departments concerned.

### 3.5.1.7 Non-remittance of education cess

Section 2 of the Karnataka (Enhancement of Certain Cesses) Act, 1976 through amendment to Chapter III of the Karnataka Compulsory Primary Education Act, 1961 (KCPEA, 1961), stipulated that for the purpose of providing the cost of promoting primary education in the State, education cess shall be levied at the rate of 10 paise in the rupee on (i) land revenue, (ii) state revenue mentioned in Schedule A and (iii) items of tax mentioned in Schedule B<sup>9</sup>. Section 17-A stated that local authority shall be entitled to deduct

<sup>8</sup> Health cess: 15 per cent on the property tax collected; Library cess: six per cent on the property tax collected and Beggary cess: three per cent on the property tax collected.

<sup>9</sup> Taxes on buildings and lands and taxes on vehicles and animals.

ten *per cent* of the amount recovered as the cost of collection and the balance shall be paid to the State Government. Further, Section 146(1) of the Karnataka Education Act, 1983<sup>10</sup> (KEA, 1983), repealed the KCPEA, 1961 and there was no stipulation for levy and collection of education cess in the KEA, 1983.

However, test check of records in 13 ULBs showed that these ULBs had a balance of ₹50.98 lakh of education cess as of March 2017. The DMA replied (July 2018) that out of 13 ULBs, 10 ULBs had remitted the cess and 3<sup>11</sup> ULBs would remit the remaining cess of ₹7.30 lakh in stages.

### 3.5.1.8 Release of duty on transfer of immovable properties

As per Section 140 of Karnataka Municipal Act, 1976, the duty on transfer of immovable property shall be levied in the form of a surcharge at the rate of two *per cent* of the duty imposed by the Karnataka Stamp Act, 1957, on instruments of sale, gift, mortgage, exchange and lease in perpetuity of immovable property situated within the limits of a larger urban area. The entire amount collected in respect of the lands and other properties situated in the urban areas shall be passed on to ULBs in the State, in proportion to the population of the ULBs by the Inspector General of Registration and Commissioner of Stamps (IGR) after deducting 10 *per cent* towards collection charges.

The duty on transfer of immovable properties of ₹21.19 crore for the year 2014-15 and 2015-16 was released to ULBs only during December 2017 and the duty on transfer of immovable properties to ULBs for the year 2016-17 and 2017-18 was not transferred (October 2018). IGR stated (October 2018) that duty on transfer of immovable properties would be transferred after receipt of complete information from all the District Registrars and necessary reconciliation.

### 3.5.2 Reporting framework

Financial reporting in the public sector is a key element of accountability. On the recommendations of Eleventh Finance Commission, GoI had entrusted the responsibility of prescribing appropriate accounting formats for ULBs to CAG.

The Ministry of Urban Development, GoI had developed the National Municipal Accounts Manual (NMAM) as recommended by CAG's Task Force. The State Government brought out the Karnataka Municipalities Accounting and Budgeting Rules, 2006 (KMABR), based on NMAM with effect from 1 April 2006. KMABR was introduced in a phased manner in all ULBs except BBMP. As of 31 March 2018, all ULBs were preparing fund based accounts in double entry system. BBMP was maintaining Fund Based Accounting System (FBAS) based on the Bengaluru Mahanagara Palike (Accounts) Regulations, 2001.

<sup>10</sup> The Karnataka Education Act, 1983 came into effect from 1 June 1995.

<sup>11</sup> Town Panchayats, Arabhavi (₹0.19 lakh), Kabbur (₹1.60 lakh) and Mallapura (₹5.50 lakh).

### **3.5.2.1 Preparation and certification of accounts of Urban Local Bodies**

According to KMABR, 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.

The auditor should complete the audit within four months (July) from the date of closure of financial year (31<sup>st</sup> March) and 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 the financial year.

For the year 2017-18, audit of 18 out of 279 ULBs were completed (October 2018).

### **3.5.2.2 Preparation and certification of accounts of Bruhat Bengaluru Mahanagara Palike**

In terms of Provision 9(2) of part II of Schedule IX to KMC Act, the Commissioner, BBMP is required to prepare annual accounts every year and produce the accounts along with relevant records to the Chief Auditor for scrutiny not later than the first day of October every year.

However, the Principal Director, KSAD, who is the Statutory Auditor for BBMP, had not audited the accounts of BBMP for the years 2016-17 and 2017-18.

## **3.6 Conclusion**

The collection of property tax *vis-a-vis* demand was poor. ULBs including BBMP had not remitted, or short remitted Health cess, Library cess and Beggary Cess. The Inspector General of Registration and Commissioner of Stamps had not transferred the required duty on transfers for the year 2016-17 and 2017-18 to ULBs as of October 2018. The State Government released only 6.93 *per cent* of NLNORR as against the stipulated 10 *per cent*. The State Government did not have an Internal Audit Wing to oversee the functions of ULBs. The Property Tax Board was not yet established in the State (November 2018). KSAD had not audited the accounts of BBMP for the years 2016-17 and 2017-18. As of March 2018, 265 IRs containing 4,109 paragraphs were pending for more than three years, indicating inadequate action on the part of ULBs.