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## **Review of Local Government Audit Reports**

Fiscal Year Ending June 30, 2009

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**OFFICE OF LEGISLATIVE AUDITS**  
DEPARTMENT OF LEGISLATIVE SERVICES  
MARYLAND GENERAL ASSEMBLY

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**Karl S. Aro**  
Executive Director

**DEPARTMENT OF LEGISLATIVE SERVICES**  
**OFFICE OF LEGISLATIVE AUDITS**  
**MARYLAND GENERAL ASSEMBLY**

**Bruce A. Myers, CPA**  
Legislative Auditor

September 15, 2010

Senator Verna L. Jones, Co-Chair, Joint Audit Committee  
Delegate Steven J. DeBoy, Sr., Co-Chair, Joint Audit Committee  
Members of Joint Audit Committee  
Annapolis, Maryland

The Honorable Peter V. R. Franchot  
Comptroller of Maryland

Mr. Karl S. Aro, Executive Director  
Department of Legislative Services

Ladies and Gentlemen:

In accordance with Article 19, Section 40(a) of the Annotated Code of Maryland, we have performed desk reviews of the audit reports filed by each county, incorporated city or town, and taxing district in Maryland for the fiscal year ended June 30, 2009. The desk reviews consisted of assessments of compliance with accounting and auditing standards, evaluations of compliance with certain State laws, and analyses of selected financial data to identify potential financial problems.

Most of the local governments and their independent auditors substantially complied with accounting and auditing standards for the fiscal year ended June 30, 2009. Nevertheless, we identified instances of noncompliance with certain requirements of our audit guidelines, generally accepted accounting principles, and/or generally accepted auditing standards. Letters were sent to 46 local governments and to their independent auditors to notify them of the deficiencies disclosed by our reviews so that corrective actions could be taken to help ensure future compliance.

The financial statements disclosed 11 local governments with uninsured or uncollateralized bank deposits, which is an area of noncompliance with State law. In addition, our desk reviews identified 9 local governments with potential financial problems, including deficit fund balances and unfavorable financial trends. Where appropriate, letters were sent to these local governments, and to their legislative representatives, to communicate their noncompliance or potential financial problems, and to request that the local governments advise us of the corrective actions that will be taken.

Respectfully submitted,

Bruce A. Myers, CPA  
Legislative Auditor

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## **Introduction and Scope**

Article 19, Section 40(a) of the Annotated Code of Maryland requires each county, incorporated city or town, and taxing district in Maryland to file annual (once every four years under specified conditions) audit reports. There were 192 local government audit reports due for fiscal year 2009 (24 counties, 152 cities and towns, and 16 taxing districts). The reports are to include financial statements with accompanying notes, and auditors' reports that express opinions as to whether the financial statements are fairly presented. The financial statements are required to be prepared in accordance with generally accepted accounting principles and audited in accordance with generally accepted auditing standards. We have prepared and distributed audit guidelines to provide additional information regarding the accounting, reporting, and auditing requirements.

Article 19, Section 40(a) of the Code requires the Office of Legislative Audits to perform a desk review of each local government's annual audit report for compliance with generally accepted accounting principles and auditing standards. Subsections (b) through (f) of Section 40 specify the reporting and review requirements applicable to special taxing districts created by the counties. The applicable county is responsible for reviewing each special taxing district's compliance with the applicable provisions of the law and for submitting the districts' reports to the Office of Legislative Audits. The Office is required to review the results of the counties' reviews and the districts' reports for compliance with the law.

We conducted a desk review of each of the fiscal year 2009 reports that had been received from the counties, incorporated cities and towns, and taxing districts, as well as seven fiscal year 2008 reports (Town of Capitol Heights, Town of Deer Park, Town of Forest Heights, City of Hyattsville, Town of Lonaconing, Town of Westernport, and the Washington Suburban Transit Commission) and one fiscal year 2007 report (Town of Forest Heights) received subsequent to our previous review. The desk reviews were performed to accomplish the following tasks:

- Identify areas of noncompliance with our audit guidelines and accounting and auditing standards, using a checklist for governmental audits published by the American Institute of Certified Public Accountants.
- Identify any instances of noncompliance with certain provisions of State law (for example, collateral for bank deposits).

- Identify local governments with potential financial problems relating to deficit fund balances, underfunded pension plans, or unfavorable trends and ratios, based on analyses of financial data over the most recent five-year period (July 1, 2004 through June 30, 2009).

We also reviewed each of the fiscal year 2009 special taxing district reports received and the related results of the counties' reviews of these reports. The purpose of our review was to ensure that the counties had reviewed the reports submitted for compliance with the provisions of the law and to identify instances in which required reports were not submitted.

## Results of Desk Reviews

### Audit Reports

**Nine local governments had not filed audit reports for fiscal year 2009, as of June 23, 2010. Twenty-eight local governments submitted audit reports after the required filing date.**

Nine local governments had not filed audit reports for fiscal year 2009. Furthermore, 28 local governments submitted audit reports after the required filing date. The failure of a local government to file an audit report, or a delay in filing, results in the lack of timely accountability to its citizens. The submission of audit reports after the required filing date was also noted for 19 of these 28 local governments during our preceding year's review. Article 19, Section 40(a) of the Annotated Code of Maryland generally requires audit reports to be filed by November 1 after the close of the fiscal year, or by January 1 after the close of the fiscal year for those local governments with a population of more than 400,000.

Audit reports for the fiscal year ended June 30, 2009 had not been received, as of June 23, 2010, for the following nine local governments:

1. Town of Capitol Heights
2. Town of Eagle Harbor
3. Town of Fairmount Heights
4. Town of Forest Heights
5. City of Hyattsville
6. Town of Lonaconing
7. Town of Sharptown
8. Town of Westernport
9. Mount Savage Special Taxing Area

We will review these fiscal year 2009 audit reports and take any follow-up action necessary when the reports are received. The results of these reviews will be included in the report on our review of fiscal year 2010 local government audit reports.



The towns of Brookview, Church Creek, Eldorado, Galestown, Goldsboro, Henderson, Hillsboro Mardela Springs, and Queen Anne requested and were granted a waiver from filing an audit report in fiscal year 2009 because the towns met the conditions for filing an audit report every fourth year as provided for under Article 19, Section 40(a) of the Code. These towns will next be required to file an audit report for fiscal year 2012. The Town of Barclay, the Village of Port Tobacco, and the Ellerslie Special Taxing Area had previously requested and were granted waivers from filing audit reports. These entities will next be required to file an audit report for either fiscal year 2010 or fiscal year 2011.

**The audit report for one local government contained an adverse opinion on one opinion unit and a qualified opinion on another opinion unit, and one other local government's report contained a qualified opinion on certain opinion units.**

The audit report for one local government contained an adverse opinion on one opinion unit and a qualified opinion on another opinion unit, and one other local government's report contained a qualified opinion on certain opinion units. The following is a summary of these opinions:

The audit report for the Town of Sykesville contained an adverse opinion (a statement that the financial statements are not presented fairly in conformity with generally accepted accounting principles) on the discretely presented component unit opinion unit because of the omission of financial data for the Town's legally separate component unit. The Town's audit report also contained a qualified opinion (statement that, except for the effects of the matter to which the qualification relates, the financial statements are presented fairly in conformity with generally accepted accounting principles) on the governmental activities opinion unit because the Town had not measured the effect of Government Accounting Standards Board Statement No. 49 entitled "*Accounting and Financial Reporting for Pollution Remediation Obligations.*". Thus, the Town's financial statements were not presented in accordance with generally accepted accounting principles as required by State law.

The audit report for the City of Westminster contained a qualified opinion on the business-type activities and Water Fund opinion units because City management had not measured the effect of the Government Accounting Standards Board Statement No. 42 entitled "*Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries.*" Thus, the City's financial statements were not presented in accordance with generally accepted accounting principles as required by State law.

**Auditors' reports for nine local governmental units were not presented in accordance with certain generally accepted auditing standards.**

Auditors' reports for nine local governmental units were not presented in accordance with generally accepted auditing standards. The following is a summary of these deficiencies:

Area of Noncompliance	Number of Audit Reports
Auditor's report did not properly report on all required information (for example, supplemental information accompanying the basic financial statements).	4
Auditor did not express an opinion(s) on all opinion units or on all financial statements.	3
Auditor's report did not include all basic elements of an audit report (for example, auditor did not sign the audit report).	2

Article 19, Section 40(a) of the Annotated Code of Maryland requires that audits be performed in accordance with generally accepted auditing standards. These standards require, in part, that the auditor express an opinion(s) as to whether the basic financial statements present fairly, in all material respects, the respective financial position, the respective changes in financial position, and cash flows, where applicable, of the local government in conformity with accounting principles generally accepted in the United States of America.

## **Financial Statements**

**Financial statements submitted by 18 local governments did not meet certain requirements of generally accepted accounting principles.**

Financial statements submitted by 18 local governments did not meet certain requirements of generally accepted accounting principles. The financial statements of one of these local governments included two such deficiencies, and the financial statements of two of these local governments included a deficiency that was also cited during our preceding year's review. The following is a summary of the deficiencies and the corresponding number of instances:

Deficiency	Number of Instances
Misclassification or improper presentation (for example, presentation of Statement of Cash Flows was improper).	13
All required financial statements were not presented or presentation of statement(s) was inappropriate.	6

**Financial statements and accompanying notes for six local governments did not include certain disclosures required by generally accepted accounting principles.**

Certain required information was not included in the financial statements, or in the accompanying notes, for six audit reports. Adequate disclosure is necessary to facilitate the understanding of, and to provide for fair presentation of, the financial information. The following is a summary of these areas of insufficient disclosure and the corresponding number of instances:

Area of Insufficient Disclosure	Number of Instances
Long-term debt	4
Cash deposits with financial institutions	2

## **Noncompliance with State Law**

**Financial statements of 11 local governments contained disclosures that cash deposits were not fully collateralized, or otherwise insured, as required by State law.**

Financial statements of 11 local governments contained disclosures that cash deposits were not fully collateralized, or otherwise insured, as required by State law (Exhibit A). Article 95, Section 22 of the Annotated Code of Maryland requires that deposits with financial institutions by local governmental units be fully collateralized. Full collateralization minimizes the risk of loss of deposits in the event the financial institution defaults.

## Potential Financial Problems

For the fiscal year ended June 30, 2009, the following potential financial problems were noted based on the information presented in the local governments' audited financial statements and accompanying notes.

### **Unreserved general fund deficit balances were noted for six local governments as of June 30, 2009.**

Unreserved general fund deficit balances were noted for six local governments as of June 30, 2009 (Exhibit B). The general fund is used to account for most of the current operating expenditures of a local governmental unit. A general fund deficit balance represents the costs of current or past services that will need to be financed in future periods. Consequently, a general fund deficit may indicate a potential financial problem. Four of these local governments also had a general fund deficit as of June 30, 2008, including one that has had such a deficit since June 30, 2006.

### **Significant unfavorable trends and ratios were noted for three local governments as of June 30, 2009.**

Significant unfavorable trends and ratios were noted for three local governments as of June 30, 2009 (Exhibit C). The unfavorable trends and ratios occurred because, over the five-year period reviewed, the local governments had general fund expenditures that exceeded general fund revenues, significant decreases in general fund balances, and significant decreases in the ratio of general fund balances to general fund expenditures. Significant unfavorable trends and ratios were also noted for two of these local governments in the preceding year's review.

## Special Taxing Districts

The preceding contents of this report are applicable to local governments filing audit reports in accordance with the provisions of Article 19, Section 40(a) of the Code. Subsections (b) through (f) of this Section require that certain types of special taxing districts file annual audit or financial reports with the county in which the districts are located within 90 days of the close of the fiscal year, in accordance with the rules and regulations established by the applicable county. The applicable county is responsible for reviewing each district's compliance with the applicable provisions of the law and for submitting copies of these reports to the Office of Legislative Audits.

**The required reports have not been filed for eight special taxing districts as of June 23, 2010.**

As of June 23, 2010, we had not received the required reports for the fiscal year ended June 30, 2009 for eight special taxing districts, seven of which are located in Anne Arundel County and one is located in Baltimore City. Anne Arundel County and Baltimore City advised us that they were in the process of pursuing compliance with applicable filing requirements for these districts and that appropriate follow-up action would be taken (for example, withholding funds).

# Exhibit A

## Schedule of Audit Reports Containing Disclosures That Cash Deposits Were Not Fully Collateralized or Otherwise Insured

Entity	Uninsured/ Uncollateralized Amount at June 30, 2009	Similar Disclosures Included in Audit Reports for Each Year Since Fiscal Year
<b>Counties</b>		
Anne Arundel County	\$1,165,029	2000
Caroline County	21,069	2005
Dorchester County	3,634,572	2003
<b>Cities and Towns</b>		
Town of Chestertown	\$ 10,272	
Town of Cheverly	66,257	2006
City of Crisfield	179,945	
Town of Luke	2,769	
Town of Morningside	240,745	2007
City of Mount Rainier	27,416	2008
Town of North East	7,090	
Town of Thurmont*	498,338	

\* This Town's financial statements also disclosed that uninsured/uncollateralized cash existed throughout the fiscal year, although the financial statements did not disclose the dollar amount of the uninsured/uncollateralized cash deposits during the year.

**Exhibit B**  
**Schedule of General Fund Deficits**  
**Fiscal Year Ended June 30, 2009**

<b>Entity</b>	<b>Unreserved Fund Balance (Deficit) at July 1, 2008</b>	<b>Revenues and Other Increases</b>	<b>Expenditures and Other Decreases</b>	<b>Unreserved Fund Balance (Deficit) at June 30, 2009</b>
<b>Counties</b>				
Anne Arundel County	\$ 54,447,182	\$1,231,031,365	\$1,287,571,003	\$ (2,092,456)
<b>Cities and Towns</b>				
City of Cambridge	\$ (961,152)	\$ 13,386,386	\$ 13,448,788	\$ (1,023,554)
City of Cumberland	(714,645)	21,482,214	21,990,680	(1,223,111)
City of Fruitland	281,688	3,562,237	3,927,805	(83,880)
Town of Princess Anne	(73,860)	3,173,824	3,168,977	(69,013)
Town of Ridgely*	(241,723)	1,275,810	1,315,300	(281,213)

\* This local government has had an unreserved General Fund deficit balance since June 30, 2006.

# Exhibit C

## Schedule of Unfavorable General Fund Trends and Ratios

### Fiscal Year Ended June 30, 2009

<u>Entity</u>	<u>Unfavorable Trend or Ratio</u>
Caroline County	<p>Expenditures and other fund uses exceeded revenues and other fund sources for the fiscal years ending June 30, 2007, 2008, and 2009.</p> <p>Fund balance decreased from \$9,826,101 as of June 30, 2006 to \$2,142,930 as of June 30, 2009.</p> <p>Fund balance as a percentage of annual expenditures decreased from 24% as of June 30, 2006 to 5% as of June 30, 2009.</p>
City of District Heights*	<p>Expenditures and other fund uses exceeded revenues and other fund sources for the fiscal years ending June 30, 2005, 2006, 2008, and 2009.</p> <p>Fund balance decreased from \$779,121 as of June 30, 2005 to \$147,490 as of June 30, 2009.</p> <p>Fund balance as a percentage of annual expenditures decreased from 27% as of June 30, 2005 to 3% as of June 30, 2009.</p>
Town of Riverdale Park*	<p>Expenditures and other fund uses exceeded revenues and other fund sources for the fiscal years ending June 30, 2007 and 2008. Expenditures also exceeded revenues for the fiscal year ending June 30, 2009, although revenues and other financing sources exceeded expenditures and other financing uses due to long-term debt proceeds.</p> <p>Fund balance decreased from \$1,082,037 as of June 30, 2006 to \$257,948 as of June 30, 2009.</p> <p>Fund balance as a percentage of annual expenditures decreased from 32% as of June 30, 2006 to 6% as of June 30, 2009.</p>

\* Significant unfavorable trends and ratios were also noted for this local government for the fiscal year ended June 30, 2008.



AUDIT TEAM

**Robert A. Garman, CPA**  
Assistant Director

**Catherine M. Easter**  
Senior Auditor

**Jonathan M. Bauman**  
**Sandra C. Medeiros**  
Staff Auditors