

Audit Report

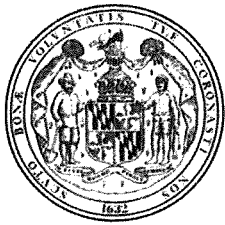
Review of Local Government Audit Reports

Fiscal Year Ending June 30, 2011



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 24, 2012

Senator James C. Rosapepe, Co-Chair, Joint Audit Committee
Delegate Guy J. Guzzone, 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, 2011. 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, 2011. 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 73 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 16 local governments with cash deposits that were not adequately collateralized, or otherwise insured, which is an area of noncompliance with State law. In addition, our desk reviews identified three local governments with potential financial problems as indicated by deficit fund balances. Additionally, for one of these local governments, the auditor's report included an explanatory paragraph describing an uncertainty about its ability to continue as a going concern. 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,

A handwritten signature in black ink, appearing to read "Thomas J. Barnickel III", with a stylized flourish at the end.

Thomas J. Barnickel III, CPA
Acting 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 (or once every four years under specified conditions) audit reports. There were 187 local government audit reports due for fiscal year 2011 (24 counties, 146 cities and towns, and 17 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 2011 reports that had been received from the counties, incorporated cities and towns, and taxing districts, as well as five fiscal year 2010 reports (Town of Deer Park, Town of Fairmount Heights, Town of Forest Heights, City of Hyattsville, and the Washington Suburban Transit Commission). 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 or unfavorable trends and ratios, based on analyses of financial data over the most recent five-year period (July 1, 2006 through June 30, 2011).

- We also reviewed each of the fiscal year 2011 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

Five local governments had not filed audit reports for fiscal year 2011 as of August 31, 2012. Forty-four local governments submitted audit reports after the required filing date.

Five local governments had not filed audit reports for fiscal year 2011. Furthermore, 44 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 23 of these 44 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, 2011 had not been received, as of August 31, 2012, for the following five local governments:

1. Baltimore City
2. Town of Deer Park
3. Town of Fairmount Heights
4. Town of Forest Heights
5. City of Hyattsville

We will review these fiscal year 2011 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 2012 local government audit reports.

The towns of Barclay, Burkittsville, and Port Tobacco requested and were granted a waiver from filing an audit report in fiscal year 2011 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 entities will next be required to file an audit report for fiscal year 2014. The towns of Brookview, Church Creek, Eldorado, Galestown, Goldsboro, Henderson, Hillsboro, Mardela Springs, Marydel, Queen Anne, and Templeville had previously requested and were granted waivers from filing audit reports. These entities will next be required to file audit reports for either fiscal year 2012 or fiscal year 2013.

The audit report for one local government contained an adverse opinion on one opinion unit and a qualified opinion on another opinion unit, and two other local government reports contained qualified opinions 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 two other local government reports contained qualified opinions 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 component unit. The Town's audit report also contained a qualified opinion (a 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 Governmental 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 Town's audit reports for each fiscal year since 2009 also contained an adverse opinion and a qualified opinion due to these situations.

The audit report for the Town of North East contained a qualified opinion on the fiduciary fund financial statements because the auditor was unable to obtain sufficient evidence supporting the carrying value of the assets held in the fiduciary fund or the changes in net assets of the fiduciary fund. The Town's audit report for fiscal year 2010 also contained a qualified opinion due to this situation.

The audit report for the Town of Westernport also contained a qualified opinion on the governmental activities, business-type activities, and the proprietary funds opinion units because the Town had not accounted for its unfunded pension liability and pension expense, along with the required disclosures, in accordance with Governmental Accounting Standards Board Statements No. 25, 27, and 50 for the Town's defined benefit pension plan. Thus, the Town's financial statements were not presented in accordance with generally accepted accounting principles as required by State law. This area of noncompliance has been noted in regard to the local government's financial statements each year since 2009.

Auditors' reports for 14 local governmental units were not presented in accordance with certain generally accepted auditing standards.

Auditors' reports for 14 local governmental units were not presented in accordance with generally accepted auditing standards. The auditor's report for two of these local governmental units included a deficiency that was also cited during our preceding year's review. The following is a summary of these deficiencies:

Area of Noncompliance	Number of Audit Reports
Auditor did not express an opinion(s) on all opinion units or on all financial statements.	8
Auditor's report did not include all basic elements of an audit report (for example, auditor did not include appropriate reference to the work of another auditor).	4
Auditor's report did not report on all required information (for example, supplemental information accompanying the basic financial statements).	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 36 local governments did not meet certain requirements of generally accepted accounting principles.

Financial statements submitted by 36 local governments did not meet certain requirements of generally accepted accounting principles. The financial statements of seven of these local governments included two or more such deficiencies, and the financial statements of one 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
Governmental fund balances were not properly classified.	23
All required financial statements were not presented or presentation of statement(s) was inappropriate.	11
Misclassification or improper presentation (for example, presentation of net assets was improper).	11

Financial statements and accompanying notes for eight 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 eight audit reports. Adequate disclosure is necessary to facilitate the understanding of, and to provide for fair presentation of, the financial information. The financial statements of one of these local governments included a deficiency that was also cited during our preceding year's review. 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	5
Significant accounting policies	3

Noncompliance with State Law

Financial statements of 16 local governments contained disclosures that cash deposits were not adequately collateralized, or otherwise insured, as required by State law.

Financial statements of 16 local governments contained disclosures that cash deposits were not adequately 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. In addition, this law requires that collateral be of the types specified in the State Finance and Procurement Article, Section 6-202 of the Code.

Potential Financial Problems

For the fiscal year ended June 30, 2011, 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 two local governments as of June 30, 2011 and for one local government as of June 30, 2010.

Unreserved general fund deficit balances were noted for two local governments as of June 30, 2011 and for one as of June 30, 2010 (Exhibit B). Additionally, for the one local government noted as having a deficit as of June 30, 2010 (Town of Fairmount Heights), the auditor's report included an explanatory paragraph which stated that the Town's delinquency in making certain payments raised substantial doubt about its ability to continue as a going concern. 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. Two of these local governments have had general fund deficits since June 30, 2008, and one has had such a deficit since June 30, 2006.

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 two special taxing districts as of August 31, 2012.

As of August 31, 2012, we had not received the required reports for the fiscal year ended June 30, 2011 for two special taxing districts which are located in Anne

Arundel County. Anne Arundel County 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	Similar Disclosures Included in Audit Reports for Each Year Since Fiscal Year
<u>At June 30, 2011</u>		
Counties		
Anne Arundel County	\$1,320,317	2000
Wicomico County	379,109	
Cities and Towns		
Town of Brookeville	33,873	
Town of Charlestown	577,230	
Town of East New Market	63,796	
Town of Emmitsburg	4,248,022	
Town of Grantsville	38,168	
City of Hagerstown	150,000	
City of Mount Rainier	11,562	2008
Town of Perryville	319,349	
Town of Pittsville	241,063	
Town of Rising Sun	12,507,587	
Town of Thurmont	6,884	2009
City of Westminster	5,739	
<u>Other Than at June 30, 2011</u>		
Cities and Towns		
Town of Leonardtown	*	
Cash Deposits That Were Secured <u>by Unacceptable Types of Collateral</u>		
Town of Hancock	**	

* This entity did not disclose the dollar amount of the uninsured/uncollateralized cash deposits in the financial statements

** Secured by collateral which was not one of the types authorized by the State Finance and Procurement Article, Section 6-202 of the Annotated Code of Maryland at June 30, 2011

Exhibit B
Schedule of General Fund Deficits
Fiscal Year Ended June 30, 2011

Entity	Unreserved Fund Balance (Deficit) at July 1, 2010	Revenues and Other Increases	Expenditures and Other Decreases	Unreserved Fund Balance (Deficit) at June 30, 2011
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Cities and Towns

City of Cumberland*	\$ (1,912,378)	\$ 18,067,933	\$ 17,761,672	\$ (1,606,117)
Town of Ridgely**	(153,072)	968,536	911,378	(95,914)

* This local government has had an unreserved General Fund deficit balance since June 30, 2008.

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

Entity	Unreserved Fund Balance (Deficit) at July 1, 2009	Revenues and Other Increases	Expenditures and Other Decreases	Unreserved Fund Balance (Deficit) at June 30, 2010
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Cities and Towns

Town of Fairmount Heights***	\$ (54,392)	\$ 638,821	\$ 637,777	\$ (53,348)
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*** This Town's financial statements for the year ended June 30, 2010 were not received in time to be included in our fiscal year 2010 review and, thus, were reviewed during the fiscal year 2011 review. The Town's fiscal year 2011 financial statements had not been filed as of August 31, 2012. This local government has had an unreserved General Fund deficit balance since June 30, 2008.

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