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

Fiscal Year Ending June 30, 2018

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

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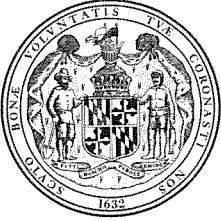
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DEPARTMENT OF LEGISLATIVE SERVICES  
OFFICE OF LEGISLATIVE AUDITS  
MARYLAND GENERAL ASSEMBLY

Victoria L. Gruber  
Executive Director

Gregory A. Hook, CPA  
Legislative Auditor

September 23, 2019

Senator Craig J. Zucker, Senate Chair, Joint Audit and Evaluation Committee  
Delegate Shelly L. Hettleman, House Chair, Joint Audit and Evaluation Committee  
Members of Joint Audit and Evaluation Committee  
Annapolis, Maryland

The Honorable Peter V. R. Franchot  
Comptroller of Maryland

Ms. Victoria L. Gruber, Executive Director  
Department of Legislative Services

Ladies and Gentlemen:

In accordance with the Local Government Article, Section 16-307 of the Annotated Code of Maryland, we have performed desk reviews of the audit reports for the fiscal year ended June 30, 2018 filed by each county, incorporated city or town, and taxing district in Maryland (referred to as local governments). We also reviewed overdue audit reports for prior fiscal years that were received over the past year. The desk reviews consisted of assessments of compliance with certain 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 financial statements filed by the local governments for the fiscal year ended June 30, 2018, along with the related independent auditors' reports, complied with the accounting and auditing standards that we assessed. 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 40 local governments and, as applicable, 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.

A number of audit reports were not filed timely in accordance with the requirements of State law. As of July 26, 2019, eight local governments had not submitted audit reports for the fiscal year ended June 30, 2018; three of these also had not filed audit reports for certain prior years.

If a local government does not comply with the audit report filing requirements, State law provides that the Comptroller of Maryland, on notice from the Executive Director of the Department of Legislative Services, may order the discontinuance of all moneys, grants, or State aid to which the local governments are entitled. Provisions were included in Chapter 565, 2019 Laws of Maryland (the State's Budget Bill) to withhold certain transportation aid for one of the aforementioned local governments until the government has submitted their delinquent audit reports. We notified the Executive Director of the Department of Legislative Services of those local governments with more than one audit report outstanding.

The fiscal year 2018 financial statements disclosed 18 local governments with cash deposits that were not adequately collateralized, or otherwise insured, which is an area of noncompliance with State law. The financial statements also disclosed that one local government had investments in equities, which is also a violation of State law. Finally, our desk reviews identified one local government with a potential financial problem, as indicated by unfavorable financial trends.

As 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 that reads "Gregory A. Hook". The signature is written in a cursive, flowing style.

Gregory A. Hook, CPA  
Legislative Auditor

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## **Introduction and Scope, Objectives, and Methodology**

The Local Government Article, Section 16-306 of the Annotated Code of Maryland requires each county, incorporated city or town, and taxing district in Maryland (referred to in this report as local governments) to file annual (or once every four years under specified conditions) audit reports. There were 195 local government audit reports due for our fiscal year 2018 review (24 counties, 157 cities and towns, and 14 taxing areas that are created under State law). 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. Finally, we annually prepare and distribute audit guidelines to provide additional information regarding the accounting, reporting, and auditing requirements.

The Local Government Article, Section 16-307 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. As part of the desk review process, we also addressed other attributes as described below. Section 16-308 of the Article specifies 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 2018 reports that had been received from the counties, incorporated cities and towns, and taxing districts. We also reviewed one fiscal year 2013 and 2014 report (Town of Marydel); two fiscal year 2015 reports (Town of Deer Park and Town of Marydel); two fiscal year 2016 reports (City of Hyattsville and Town of Marydel); and five fiscal year 2017 reports (City of Hyattsville, Town of Marydel, City of Seat Pleasant, Bel Air Special Taxing Area, and Washington Suburban Transit Commission) that were received over the last year. The desk reviews consisted of reviewing each audit report in order to accomplish the following tasks:

- Identify areas of noncompliance with our audit guidelines and certain accounting and auditing standards pertaining to the presentation of the financial statements and auditors' reports.

- Identify any instances of noncompliance with certain provisions of State law (for example, collateral for bank deposits, timely filing of audit reports).
- 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, 2013 through June 30, 2018).

We also reviewed each of the fiscal year 2018 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.

At the conclusion of our review, letters were sent to applicable local governments and their independent auditors to notify them of the deficiencies disclosed during the review so that corrective actions can be taken to help ensure future compliance. Additionally, as appropriate, letters were also sent to local governments, and to their legislative representatives, to communicate noncompliance with State law or potential financial problems. For these issues, the local governments were asked to advise us of corrective actions that will be taken.



## Results of Desk Reviews

### Audit Reports

#### **Finding 1**

**A number of local governments had not filed the required audit reports or had filed after the required filing date.**

As of July 26, 2019, eight local governments were delinquent in filing audit reports as required by the Local Government Article of the Annotated Code of Maryland.

Local Government	Fiscal Years Outstanding
Allegany County	2018
Town of Deer Park	2016, 2017, 2018
City of Hyattsville	2018
Town of Lonaconing	2017, 2018
City of Mount Rainier	2017, 2018
City of Seat Pleasant	2018
Bel Air Special Taxing Area	2018
Upper Potomac River Commission	2018

Furthermore, 18 local governments submitted audit reports after the required filing date. The submission of audit reports after the required filing date was also noted for 8 of these 18 local governments during at least our preceding year's review. 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 Local Government Article, Section 16-306 of the Annotated Code of Maryland generally requires audit reports to be filed on or before October 31 after the close of the fiscal year or on or before December 31 after the close of the fiscal year for those local governments with a population of more than 400,000.

Budget language adopted during the 2019 Session of the Maryland General Assembly (Chapter 565, 2019 Laws of Maryland) resulted in the withholding of certain transportation aid from the Town of Deer Park pending receipt of their delinquent audit reports. Furthermore, failure to file a required report with the Department of Legislative Services for three successive years provides the Executive Director with reasonable cause to suppose that the municipality is no longer actively operating under its charter, which could cause this town to have its charter repealed. The failure of this local government to submit audit reports has been reported to the Executive Director. The failure of the City of Mount Rainier

to file the required reports for the fiscal years ending June 30, 2017 and 2018 has also been reported to the Executive Director.

Subsequent to July 26, 2019, Allegany County, the City of Seat Pleasant, and the Upper Potomac River Commission submitted their audit reports for fiscal year 2018. Also subsequent to July 26, 2019, the Town of Lonaconing submitted its audit report for fiscal year 2017, although its fiscal year 2018 audit report is still outstanding.

We will review all delinquent 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 2019 local government audit reports.

The towns of Barton, Brookview, Church Creek, Eagle Harbor, Eldorado, Galestown, Goldsboro, Henderson, Hillsboro, Mardela Springs, Queen Anne, Templeville, and the Ellerslie and Mount Savage Special Taxing Areas previously requested and were granted waivers from filing audit reports. These local governments met the conditions for filing an audit report every fourth year as provided for under the Local Government Article, Section 16-305 of the Code and, depending on the waiver period, will be required to file its next audit report for either fiscal year 2019, 2020, or 2021.

## **Finding 2**

**The auditor's report for one local government contained an adverse opinion on one opinion unit.**

The auditor's 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. Specifically, financial data related to a development corporation that is a component unit of the Town had not been audited and was not included in the Town's financial statement, thus resulting in the adverse opinion regarding the discretely presented component units.

As a result, the Town's financial statements were not presented in accordance with generally accepted accounting principles as required by State law. The Town's audit report for each fiscal year since 2009 also contained an adverse opinion due to this situation.

The auditor for the Town of Sykesville submitted a letter providing an explanation regarding the opinion that was not unqualified, as required, but the resolution of the applicable condition is uncertain.

**Finding 3**

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

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

Area of Noncompliance	Number of Audit Reports
Auditor's report did not include all basic elements (for example, auditor did not include an emphasis-of-matter paragraph related to a change in accounting principle).	4
Auditor's report did not clearly express an opinion on all basic financial statements.	2

The Local Government Article, Section 16-306 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

### **Finding 4**

**Financial statements submitted by 14 local governments did not meet certain requirements of generally accepted accounting principles.**

Financial statements submitted by 14 local governments did not meet certain requirements of generally accepted accounting principles. The financial statements of 1 of these 14 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:

<b>Deficiency</b>	<b>Number of Instances</b>
Misclassification or improper presentation (for example, presentation of net position was improper).	7
All required financial statements were not presented or presentation of statement(s) was inappropriate.	3
Governmental fund balances were not properly classified.	3
Items reported as assets, deferred outflows of resources, liabilities, or deferred inflows of resources were not properly displayed.	1

### **Finding 5**

**Financial statements, accompanying notes, and required supplementary information did not include certain disclosures required by generally accepted accounting principles for 11 local governments.**

Certain required information was not included in the financial statements, or disclosed in the accompanying notes or the required supplementary information, for 11 audit reports. The financial statements of 1 of these 11 local governments included two such deficiencies. Furthermore, the financial statements of 1 of these local governments included a deficiency that was also cited during our preceding year's review. 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 the areas of insufficient disclosure and the corresponding number of instances:

Area of Insufficient Disclosure	Number of Instances
Deferred inflows/outflows	5
Cash and cash equivalents	3
Long-term debt	2
Schedule of pension funding progress	2

## Noncompliance with State Law

### **Finding 6**

**Financial statements of 19 local governments contained disclosures that cash deposits were not adequately collateralized, or otherwise insured, as required by State law.**

Twenty financial statements for 19 local governments (primarily from fiscal year 2018, but also from fiscal years 2017 and 2015) contained disclosures that cash deposits were not adequately collateralized, or otherwise insured, as required by State law (Exhibit A). The Local Government Article, Section 17-101 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.

### **Finding 7**

**One local government invested in equities, which is a violation of State law.**

The financial statements of the Town of Morningside disclosed that the Town had investments in equities, totaling \$266,851 as of June 30, 2018, which is a violation of State law. Local Government Article, Section 17-101 of the Annotated Code of Maryland restricts the types of investments for local governments to those specified in the State Finance and Procurement Article, Section 6-222 of the Code. Investments not authorized by State law increase the Town's risk of loss associated with investments.

## Potential Financial Problems

For the fiscal year ended June 30, 2018, the following potential financial problems were noted based on the information presented in the local governments' audited financial statements and accompanying notes.

### **Finding 8**

**Significant unfavorable trends and ratios were noted for one local government as of June 30, 2018.**

Significant unfavorable trends and ratios were noted for one local government as of June 30, 2018 (Exhibit B). The unfavorable trends and ratios occurred because, over the five-year period reviewed, the local government 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.

## Special Taxing Districts

The preceding contents of this report are applicable to local governments filing audit reports in accordance with the provisions of the Local Government Article, Section 16-306 of the Code. Section 16-308 of this Article requires that certain types of special taxing districts (created by a county) file annual audit or financial reports with the county in which the districts are located not later than 90 days after 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.

### **Finding 9**

**The required reports had not been filed for four special taxing districts as of July 26, 2019.**

As of July 26, 2019, we had not received the required reports for the fiscal year ended June 30, 2018 for four 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 the applicable filing requirement 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 Fiscal Year Since
<b><u>At June 30, 2018</u></b>		
<b>Counties</b>		
Anne Arundel County	895,000	2000
Howard County	431,429	2016
Kent County	124,168	
St. Mary's County	37,908	2017
Somerset County	873,105	
Wicomico County	525,433	2014
<b>Cities and Towns</b>		
Town of Accident	94,071	
City of Annapolis	39,127	2017
Town of Boonsboro	1,425,786	2017
Town of Brentwood	784,809	2016
Town of Grantsville	293,410	
Town of Morningside	188,367	
Town of Port Deposit	42,237	
Village of Port Tobacco	83,692	
Town of Riverdale Park	1,301,237	
Town of Westernport	159,806	
<b>Special Taxing Areas</b>		
Village of Drummond Citizens Committee	174,504	
Washington Suburban Transit Commission	389,912	2017
<b><u>At June 30, 2017</u></b>		
<b>Special Taxing Areas</b>		
Washington Suburban Transit Commission	395,632	
<b><u>At June 30, 2015</u></b>		
<b>Cities and Towns</b>		
Town of Deer Park	1,438	

**Exhibit B**  
**Schedule of Unfavorable General Fund Trends and Ratios**  
**Fiscal Year Ended June 30, 2018**

<b><u>Entity</u></b>	<b><u>Unfavorable Trend or Ratio</u></b>
City of Crisfield	<p>Expenditures and other financing uses exceeded revenues and other financing sources for the fiscal years ending June 30, 2014, 2015, and 2018.</p> <p>Fund balance decreased from \$176,451 as of June 30, 2017 to \$89,359 as of June 30, 2018.</p> <p>Fund balance as a percentage of annual expenditures and other financing uses decreased from 6.1% as of June 30, 2017 to 2.7% as of June 30, 2018.</p>



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