

**PART – I URBAN LOCAL BODIES**

**CHAPTER – I**

**OVERVIEW ON FINANCES OF THE URBAN LOCAL BODIES INCLUDING THE ACCOUNTING PROCEDURES**

**1.1 Introduction**

Article 243 (W) of the Constitution of India envisages that the State Government may, by law, endow the municipalities with such powers and authority as may be necessary to enable them to function as institutions of self Government and such law may contain provisions for devolution of powers and responsibilities upon municipalities.

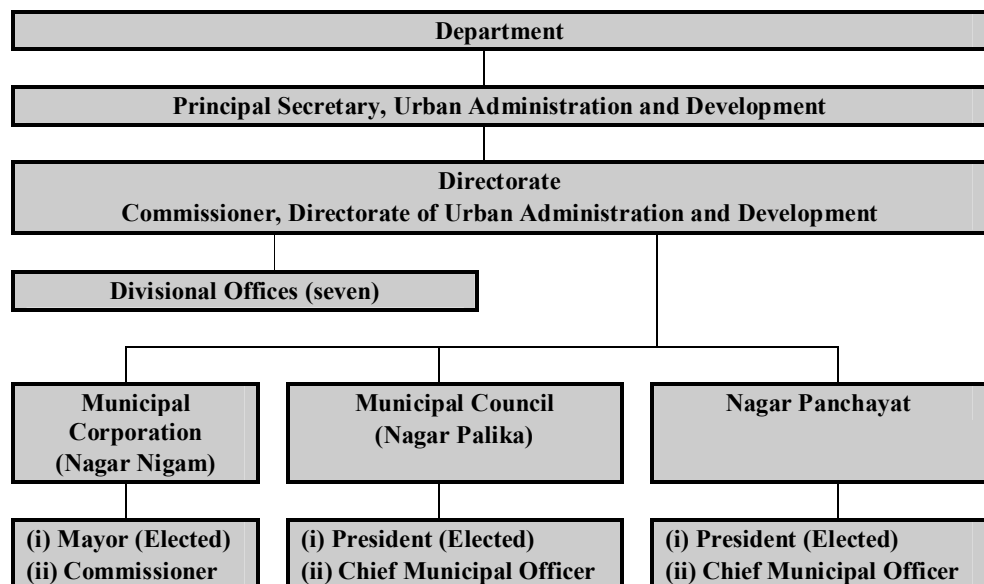
After the 74<sup>th</sup> Constitution Amendment, the Urban Local Bodies (ULBs) were made full fledged and vibrant institutions of Local Self Government by vesting them with clearly defined functions and responsibilities. Accordingly, the State Government reorganized (1993) these institutions into three tier system of ULBs namely Municipal Corporations for a larger urban area, Municipal Councils for smaller urban area and Nagar Panchayats for a transitional area.

At present, there are 14 Municipal Corporations, 96 Municipal Councils and 250 Nagar Panchayats. The last elections for the ULBs were held during 2005-06. All 360 ULBs as shown above cover 1.52 crore urban population of the state i.e. 25 percent of the total population of the state.

**1.2 Administrative arrangements**

All the ULBs are distinct legal authority to discharge the functions devolved under the provisions of Acts and Rules subject to monitoring powers vested in state authorities provided there in. The organisational structure of the Department is given below.

**Organisational Chart of ULBs**



### **1.3 Accounting arrangements**

**1.3.1** Consequent upon adoption of the budget and accounts format prescribed by the Task Force constituted by Comptroller & Auditor General of India (CAG) which inter alia suggested adoption of accrual based accounting by ULBs, the UADD published Madhya Pradesh Municipal Accounts Manual (MPMAM) in July 2007. However, as per orders of the UADD (July 2007) the accrual system of accounting was to be implemented with effect from April 2008 in 14 Municipal Corporations only. The above system is yet to be implemented in the remaining ULBs.

**1.3.2** As per the decisions taken in the National Seminar organized (September 2003) by the Ministry of Urban Development, GOI, a Steering Committee was to be formed in all the States to see the implementation of budget and accounting formats as suggested by the CAG's Task Force. Even after regular correspondence, the committee was not formed so far till March 2010.

**1.3.3** Government of India (GOI) forwarded (September 2004) extracts of section 93 to 96 of Model Municipal Law (MML) along with CAG's suggestions thereon for adoption by State Government. Commissioner (UADD) stated in the meeting (November 2008) that some progress in this regard has been made and assured to appraise audit accordingly. Reminders were issued to Principal Secretary (FD) in September 2009 and January 2010, but reply has not been received so far.

### **1.3.4 Database on finances of ULBs**

The data is to be collected, compiled and maintained in standard formats prescribed by CAG. UADD agreed (June 2004) in principle to adopt the formats of database. In compliance it was stated (September 2009) that the database on finances is being maintained in standard formats in Nagar Nigam and action will be taken to maintain the database in other ULBs also.

### **1.4 Audit arrangements**

**1.4.1** The State Govt. has appointed Director/Commissioner of Local Fund (DLFA) as a primary auditor of accounts of Urban Local Bodies. As per recommendations of the Eleventh Finance Commission (EFC), audit by DLFA has been brought under the Technical Guidance and Supervision (TGS) of CAG by the State Government in November 2001. Accordingly, the office of the Senior Deputy Accountant General, (Local Body Accounts and Audit) is conducting audit of ULBs under TGS module. 88 ULBs including three Municipal Corporations were test checked by audit during 2008-09.

### **1.4.2 Approval of audit plans of Commissioner Local Fund Audit**

The CLFA was required to prepare the audit plan in consultation with the Principal Accountant General (PAG) as a part of the TGS arrangement. However, inspite of request to the Government (February - November 2008), the audit plans of CLFA have not got approved from the PAG. The CLFA has furnished the list of units proposed to be audited during 2009-10 without getting it approved from PAG.

### 1.4.3 Internal Audit System

According to para 7.2 of the recommendations submitted (July 1996) by the First SFC and decision of the Finance Department (FD), an Internal Audit System was to be set up to ensure the accountability of ULBs. Such provision for creation of internal audit department was also mentioned in para 2.2.1 of MPMAM. However Directorate UADD (September 2009) stated that apart from the arrangement of pre-audit in 50 ULBs units, there was no system of internal audit in other ULBs.

### 1.5 Source of revenue

There were mainly two sources of revenue for local bodies (i) Government grants and (ii) own revenues. Own revenue resources of ULBs comprise of tax and non-tax revenues realised by them. Government grants comprise of funds released by the State Government and Government of India (GOI) on the recommendation of SFC, Central Finance Commission and State and GOI share for implementation of various schemes. The ULBs also obtain loans for implementation of various schemes relating to urban development.

### 1.6 Receipts and expenditure

**1.6.1** Funds (share of tax revenue of the state, schemes funds & grants etc.) allocated to ULBs by the State Government through budget including State share of the GOI schemes & grants recommended by Twelfth Finance Commission (TFC) were as under:-

(` in crore)

Sl. No.	Bifurcations of grant						Actual Expenditure			Excess (+)/ Saving (-)
	Year	Share of Tax	Scheme funds	Grant	Pay & Allowance of Directorate	Total	Revenue	Capital	Total	
1.	2005-06	899.38	142.32	222.45	2.72	1266.87	1158.12	19.45	1177.57	(-) 89.30
2.	2006-07	1047.30	304.45	531.93	8.22	1891.90	1614.57	28.81	1643.38	(-) 248.52
3.	2007-08	1300.39	395.02	635.04	2.93	2333.38	1695.40	305.55	2000.95	(-) 332.43
4.	2008-09	1531.07	502.07	563.14	22.34	2618.62	2112.90	205.43	2318.33	(-) 300.29

The above figures indicate that the budget provisions increased by 38 per cent in ULB sector during the year 2008-09 as compared to the year 2006-07 but the ULBs could not spend the amount, resulting in saving during 2006-07 to 2008-09. Details of receipts of ULBs from their own sources and loans & expenditure was not available with Directorate, UADD. The Commissioner, (UADD) stated (September 2009) that the same would be collected and furnished to audit. However the position of State and Central grant, own revenue realized and classification of expenditure into capital and revenue heads of the test checked ULBs (Bhopal, Gwalior, Mandasaur, Neemuch and Ratlam) has been mentioned in the **Appendix-I**.

### 1.6.2 Submission of Utilisation Certificates (UCs)

Directorate UADD circular (December 2004) stipulated that grants should not be released before obtaining UCs of previous years. Audit scrutiny (September 2009) of records relating to the release of SFC grants by the Directorate UADD Bhopal revealed that grants were released without obtaining UCs (September 2009) for the year 2008-09. On being pointed out, the Commissioner UADD stated (September 2009) that orders have been issued for submission of UCs regularly.

### 1.7 Position of outstanding loans

The position of outstanding loans of all ULBs was not available with the Directorate UADD. Scrutiny (September 2009) of records in MC Bhopal, Ratlam, Mandsoore, Neemuch and Gwalior revealed that principal amount of ` 47.20 crore was due for repayment (September - November 2008) against the outstanding loans. The position of outstanding loans and interest in test checked districts were as under:-

(` in lakh)

Sl. No.	Name of ULB	Balance as on 1.4.08	Fresh loan during 08-09	Repayment during 08-09		Outstanding Principal as on 31 March 2009.
				Principal	As Interest	
1.	Bhopal	3509.90	--	1355.74	372.22	2154.16
2.	Ratlam	1120.00	--	--	--	1120.00
3.	Mandsoure	--	--	--	--	--
4.	Neemuch	--	--	--	--	--
5.	Gwalior	545.66	900	--	34.93	1445.66
		<b>5175.56</b>	<b>900</b>	<b>1355.74</b>	<b>407.15</b>	<b>4719.82</b>

### 1.8 Position of outstanding audit paragraphs

The position of outstanding audit paragraphs of ULBs included in the Inspection Reports (IRs) of the CLFA and AGs Inspection Reports are as under:-

#### (A) Outstanding audit paragraphs of CLFA

(As on 31 March 2009)

Sl. No.	Financial Year	ULB			
		Total No. of outstanding audit paragraphs	Addition	No. of paragraphs settled	No. of paragraphs Outstanding
1.	2006-07	178265	8227	13066	173426
2.	2007-08	173426	6471	8890	171007
3.	2008-09	171007	7183	9142	169048

#### (B) Outstanding audit paragraphs of AGs Inspection Reports.

(As on 31 March 2009)

Sl. No.	Financial Year	ULB			
		Total No. of outstanding audit paragraphs	Addition	No. of paragraphs settled	No. of paragraphs Outstanding
1.	2006-07	2508	601	0	3109
2.	2007-08	3109	514	0	3623
3.	2008-09	3623	778	61	4340

These outstanding paragraphs require active pursuance by CLFA for early settlement.

### 1.9 Bank-reconciliation statement not prepared

Rules 97-98 of Madhya Pradesh Nagar Palika Lekha Niyam 1971, provides that the reconciliation of any difference between the balances of cash book and

bank accounts is required to be conducted every month. However, it was noticed that the difference of cash balance of ` 2.65 crore between Cashbook and Bank statement at the close of the year (2001 to 2009) was not reconciled by 9 ULBs<sup>1</sup>. Due to non-reconciliation of cash balance, possibility of temporary misappropriation or fictitious booking of expenditure could not be ruled out. The authenticity of cash balance of ULBs in the cashbook also remained doubtful in the absence of reconciliation with bank statement.

The position of the difference is given in **Appendix- II**.

#### **1.10 Non-recovery of advances from individuals**

Temporary advances were paid to Staff/officials for making petty payments. Madhya Pradesh Finance Department orders (2001) provides that the temporary advances should be adjusted or recovered at the earliest but in no case later than 3 months of payment of advance or last month (March) of financial year. In case of non-adjustment/recovery penal interest @ of interest payable by Banks on fixed deposits shall also be recovered. Audit of 13 Nagar Nigam/ Nagar Palika/ Nagar Panchayat revealed that a sum of ` 22.08 lakh paid to officials/ staff for various purposes were outstanding against them for the last one to 5 years as shown in **Appendix -III**. Lack of effective action to recover/ adjust the old outstanding advances may lead to loss with the passage of time.

#### **1.11 Diversion of funds**

Central Government / State Government released funds in the form of grants-in-aid for development of urban areas which were to be spent exclusively on the projects for which these were sanctioned. Diversion of funds from one scheme to another was not permissible without prior approval of the Central/ State Government.

Scrutiny of records revealed irregular diversion of funds amounting to ` 24.98 lakh by 4 ULBs during 2001-07 for the purposes not covered under the schemes or for routine municipal activities as shown in **Appendix -IV**.

#### **1.12 Non recovery of taxes**

Urban Local Bodies (ULBs) earn revenue from their own resources through taxes, rent, fees, issue of licenses etc. In (18) test checked Nagar Nigam/Nagar Palika/Nagar Panchayat. As of March, 2009 a sum of ` 7.71 crore as shown in **Appendix –V** was outstanding against the taxpayers, although the ULBs had powers under section 165 of Madhya Pradesh Municipalities Act, 1961 to approach a Magistrate to seek orders for recovery by distress and sale of any movable property of attachment and sale of immovable property belonging to defaulters, they failed to invoke these power to recover the outstanding taxes.

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<sup>1</sup> (1) Nagar Palika Varaseoni (2) Nagar Palika Gadarwara (3) Nagar Palika Maudla (4) Nagar Palika Ganj Basoda (5) Nagar Palika Gohad (6) Nagar Panchayat Rahatgarh (7) Nagar Panchayat Gautampura (8) Nagar Panchayat Rajgarh (9) Nagar Panchayat Jaura

Failure to invoke its powers resulted in non-recovery of outstanding taxes and resource crunch leading to hindrance in development works.

### **1.13 Non depositing of amount in Provident Fund Accounts**

Rule 102 (4) of M.P. Nagar Palika Lekha Niyam 1971 provides that the deduction of P.F. subscription will be credited in P.F. Account. Government of Madhya Pradesh, Department of Local Bodies further directed (February 1998) all the Commissioners / Chief Municipal Officers that Provident Fund (PF) subscriptions is required to be credited to the fund account of the employees scrupulously. However it was noticed that one Nagar Panchayat Rahatgarh (District-Sagar) did not deposit provident fund subscription of ` 10.61 lakh in the fund account of the employees during 10/1996-2005 which resulted not only loss of interest on provident fund account but also put additional burden on the ULB.

### **1.14 Non-creation of Reserve Fund of ULB's**

Sub rule 3 (3) of Madhya Pradesh Nagar Palika Budget Rules, 1962 provides that every Nagar Palika is required to create a reserve fund account (Sanchit Nidhi) by depositing five per cent of net income every year, so that it may be used in special circumstances in the interest of the ULB.

Scrutiny of records of Ten Nagar Panchayat/Nagar Palika/Nagar Nigam revealed that due to financial crisis a sum of ` 1.55 crore was not deposited in the reserve fund account from their net income during 2001-08 as shown in **Appendix-VI**.

### **1.15 Non recovery of rent and premium of shops**

Shops were constructed at various places by the ULBs to increase the revenue by way of premium and monthly rent of these shops.

Test check of records of 13 Nagar Palika, Nagar Panchayat revealed that the premium of shops amounting to ` 0.68 crore and rent of shops amounting to ` 0.52 crore was not recovered by these ULBs for the last two to six years. Detail are shown in **Appendix - VII**.

This has resulted in loss of revenue of ` 1.20 crore.

### **1.16 Conclusion**

Budget and accounts in the format, prescribed by the CAG, were not maintained in all the three tiers of ULBs. Database in the formats prescribed by the CAG on finances of ULBs is yet to be compiled. The provisions of MML along with suggestion of CAG on section 93 to 96 of MML have not yet been incorporated in the concerned Acts. The information regarding receipts and expenditure of all ULBs was not being maintained by the Directorate UADD. Approval of PAG on audit plan was not obtained by the CLFA. The Steering Committee and State Legislature Committee were not yet formed.

**1.17 Audit findings on release and utilisation of Twelfth Finance Commission's grants of Urban Local Bodies**

**1.17.1 Delay in transfer of grant to ULBs and non payment of interest on delayed transfer**

According to para 6.1 and 6.4 of GOI guidelines of TFC grants, States have to mandatorily transfer the grants released by the Centre to the ULBs within 15 days from the date of its credit into the State Government's account. In case of delayed transfer of grants to ULBs beyond the specified period of 15 days, the State Government was required to pay interest to ULBs at the rate equal to the RBI rate on such delayed transfer.

Scrutiny of records of the FD revealed (September 2009) that the GOI released the first and second instalment of ` 72.20 crore (first instalment of ` 36.10 and second instalment of ` 36.10 crore) for the year 2008-09 on 24 October 2008 and 12 February 2009 respectively and credited into State Government's accounts on the same date. Bank accounts of ULBs were test checked in audit. The test check in eleven ULBs (September - December 2009) revealed that there was a delay of 06 to 17 days (beyond specified period of 15 days) in transfer of grants of ` 5.44 crore to their respective bank accounts. As per GOI guidelines and also as per past practice, the FD was required to pay interest @ 5% on the delayed transfer of grants to ULBs during the year 2008-09.

But no reply has been furnished so far by the FD and UADD (February 2010).

**1.17.2 Unspent balance of previous grant**

State TFC working plan/ guidelines envisaged that the TFC grants received may be utilised (i) on Solid Waste Management (SWM) 50 percent, (ii) on water supply and sanitation 48 percent and (iii) on building a data base on finances 2 percent.

Scrutiny of records of twenty two ULBs revealed that out of total TFC grant of ` 13.41 crore received by the ULBs during 2005-08, an amount of ` 5.86 crore remained unspent (September to December 2009) as shown in **Appendix-VIII**. On pointing out in audit, the Heads of auditee units explained various reasons viz. non approval of Parishad for incurring the expenditure, late allotment of grant, non acquisition of land for landfill stations and non demarcation of land for unspent grants.

**1.17.3 False Certificate of Utilisation**

As per para 6.3 of GOI guidelines of TFC grants, the State Finance Secretary was required to provide a certificate to GOI every year regarding percentage of grants spent by the ULBs on SWM.

Test check of records of Municipalities and Councils revealed that ` 9.71 crore on account of SWM was received in 23 ULBs during 2005-09. Out of it only ` 2.66 crore could be utilised during the period and ` 7.05<sup>2</sup> crore remained unutilised as detailed in **Appendix - IX**. Whereas the FD submitted the UCs of entire amount of ` 144.40 crore received on account of SWM (being 50 percent of total TFC grant) during 2005-09 in the state.

Thus UCs submitted to GOI by FD did not reflect the actual position of utilisation of TFC grants. Reply of FD was awaited (February 2010).

#### **1.17.4 No progress in Solid Waste Management (SWM)**

As per para 3.1 (XIV) of GOI guidelines of TFC grants, at least 50 percent of the grant-in-aid provided to each state for the ULBs should be earmarked for SWM. The Municipalities should concentrate on collection, segregation & transportation of solid waste.

Test check of records of nine ULBs belonging to six districts revealed that no work on SWM except an expenditure during 2005-09 of ` 0.0228 crore on preparation of DPRs was started despite release of grant of ` 1.97 crore as detailed in **Appendix- X**.

#### **1.17.5 Non achievement of Solid Waste Management (SWM) parameters**

According to the schedule II annexed to (Rule 6 (i) and (iii), 7 (i)) of GOI Municipal Solid Wastes (Management and Handling Rules 2000) parameters were fixed alongwith its compliance criteria for collection, segregation, storage, transportation, processing and disposal of municipal solid wastes.

Test check of records of six MCs<sup>3</sup> revealed that an expenditure of ` 19.78 crore<sup>4</sup> was incurred from 2005-06 to 2008-09 only for collection and transportation of Municipal Solid Waste (MSW) under SWM but other activities like: segregation, storage, processing and disposal of MSW were not taken-up through Public Private Partnership (PPP) as required vide para 3.1 XIV of GOI guidelines of TFC grants. The reasons for not taking up the activities specified in the notification were Non-approval by the Parishad, Land under development, work under progress etc. This resulted in non-fulfillment of all the parameters & non-implementation of PPP in SWM.

#### **1.17.6 Database on finances of ULBs**

The second State Finance Commission (SFC) (Beyond the Fiscal Package) recommended (December 2003) the need for building up database in respect of municipal finances. This recommendation was accepted by the State Government (March 2005). The database needs to be collected, compiled and maintained in the standard formats as prescribed by the C&AG which was

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<sup>2</sup> Unutilised amount ` 7.05 crore (pertaining to SWM) is included in unspent amount of ` 9.13 crore explained in para 2.1.4.1.

<sup>3</sup> Nagar Nigam Bhopal, Dewas, Jabalpur, Sagar, Satna and Ujjain

<sup>4</sup> ` 19.78 crore (Bhopal: ` 9.15, Dewas: ` 0.31, Jabalpur: ` 6.09, Sagar: ` 0.31, Satna ` 1.07 and Ujjain ` 2.85 crore)



agreed (June 2004) by UADD. But the final action for development of database was awaited (December 2009). As per UCs reported (July 2009) to GOI by FD, the TFC grants amounting to ` 5.78 crore (being 2 percent of total TFC grant ` 288.80 crore) for maintenance of accounts and creation of database received from 2005-06 to 2008-09 have been utilised on the specified purpose, but the database of finances in the formats prescribed by C&AG was not found created in any of the test checked Municipal Corporation/ Council in five districts<sup>5</sup>. It was also observed that in 15 Municipal bodies out of ` 19.07 lakh received for building of data base a sum of ` 16.85 lakh (84 percent) remained unspent as of March 2009.

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<sup>5</sup> Jabalpur, Jhabua, Sagar, Satna and Ujjain.