

## 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 and the municipalities had been accorded constitutional status for governance. 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)	57
Town Municipal Councils (TMCs)	114
Town Panchayats (TPs)	89
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 Government, is the nodal department. The Directorate of Municipal Administration (DMA), established in December 1984, is the nodal agency to control and monitor 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 of March 2017, the State Government had transferred 17 functions to ULBs. 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

The Principal Director, Karnataka State Audit and Accounts Department (KSAD), is the primary Auditor of ULBs in terms of KMC and KM Acts. 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 with effect from 2011-12 onwards, by amending the statutes (October 2011).

The status of audit by KSAD during the period 2012-13 to 2016-17 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 September 2017**

Year	CC		CMC		TMC/TP/NAC	
	Total	Audited	Total	Audited	Total	Audited
2012-13	7	5	44	42	168	167
2013-14	7	6	44	41	168	167
2014-15	7	4	44	37	168	163
2015-16	10	6	56	43	208	176
2016-17	11	1	56	10	208	52

Source: Information furnished by KSAD

### 3.4.4 Response to Inspection Reports

As of March 2017, 302 Inspection reports (IRs) consisting of 5,127 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 2015-16**

Units	5 to 10 years (2007-08 to 2011-12)		3 to 5 years (2012-13 to 2013-14)		2014-15		2015-16		Total	
	IRs	Paras	IRs	Paras	IRs	Paras	IRs	Paras	IRs	Paras
ULBs other than BBMP	58	549	44	914	33	848	65	1,545	200	3,856
BBMP	6	208	24	240	48	567	24	256	102	1,271
<b>Total</b>	<b>64</b>	<b>757</b>	<b>68</b>	<b>1,154</b>	<b>81</b>	<b>1,415</b>	<b>89</b>	<b>1,801</b>	<b>302</b>	<b>5,127</b>

Source: Inspection Reports

Out of 302 IRs outstanding, 132 IRs (44 *per cent*) containing 1,911 paragraphs (37 *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. A proposal was forwarded (July 2017) by DMA to the Government for establishment of an Internal Audit Wing as part of the upgradation of the Directorate to the Commissionerate.

### 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 provides for establishment of the Karnataka Property Tax Board by the State Government.

The Property Tax Board was not yet established in the State (November 2017).

## 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, 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>19</sup> released by the State Government to ULBs during the period 2012-13 to 2016-17 are shown in **Table 3.4**.

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

ULBs	2012-13		2013-14		2014-15		2015-16		2016-17	
	Budget	Grants released	Budget	Grants released	Budget	Grants released	Budget	Grants released	Budget	Grants released
CCs	3,544	2,669	4,348	3,632	4,956	4,372	4,435	4,307	4,233	4,099
CMCs/TMCs	1,513	1,126	1,629	1,139	1,589	1,365	1,644	1,555	1,488	1,368
TPs/NACs	290	214	344	248	312	273	233	214	259	219
<b>Total</b>	<b>5,347</b>	<b>4,009</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>

Source: State Budget Estimates and Finance Accounts

It can be observed from the table that the allocated quantum of funds were not released to ULBs during any of the years from 2012-13 to 2016-17. While actual releases to ULBs showed an increasing trend during the years 2012-13 to 2015-16, the releases decreased by six *per cent* during 2016-17 compared to 2015-16. The releases to CCs and CMCs/TMCs were reduced by 5 and 12 *per cent* respectively during 2016-17 and increased by 2 *per cent* to TPs/NACs.

### 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* (₹8,875.07 crore) of Non-Loan Net Own Revenue Receipts (NLNORR) was to be released to ULBs during 2016-17. As against this, the State Government had only released 6.41 *per cent* (₹5,685.58 crore) of NLNORR (₹88,750.66 crore), resulting in short release of ₹3,189.49 crore to ULBs during 2016-17.

### 3.5.1.4 Delayed release of Fourteenth Finance Commission grants

GoI released total basic grants of ₹778.29 crore, in two equal instalments, and ₹229.70 crore as performance grants to ULBs during the year 2016-17.

FFC guidelines stipulated that the funds should be transferred to the accounts of ULBs within 15 days from the date of receipt of grant from GoI, failing which, the State Government would be liable to release the instalment with interest at the Reserve Bank of India (RBI) rate for the delayed period. GoI released the instalments during June 2016 and December 2016.

There were substantial delays ranging from 26 to 34 days in transfer of first instalment of basic grants to ULBs. The consequent interest payable amounting to ₹1.70 crore was not released to ULBs by State Government. There were

<sup>19</sup> Grants include State Finance Commission grants, Fourteenth Finance Commission grants, grants released for Centrally sponsored schemes and State schemes.

delays of one to five days in release of other two instalments of funds, which needs to be curtailed. Government should ensure timely transfer of funds to avoid extra burden on the exchequer.

### 3.5.1.5 Release of performance grants to ineligible Urban Local Body

FFC recommended performance grant for duly constituted ULBs. To be eligible, ULB was required to submit audited annual accounts that would relate to a year not earlier than two years preceding the year in which it sought to claim the performance grant.

The performance grants of ₹229.70 crore released during 2016-17 was distributed to 191 ULBs in the State. Scrutiny of records revealed that ₹81.77 crore was irregularly released to BBMP towards performance grants though the accounts of BBMP for the year 2014-15 was not audited by KSAD.

### 3.5.1.6 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<sup>20</sup> demanded, collected and outstanding at the end of March 2017 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
2012-13	62.19	342.00	404.19	284.18	120.01	70
2013-14	75.84	387.48	463.32	371.56	91.76	80
2014-15	83.47	433.35	516.82	369.63	147.19	72
2015-16	98.20	504.05	602.25	508.54	93.71	84
2016-17	105.80	666.80	772.60	563.19	209.41	73

Source: Details furnished by DMA

From the above table, it can be seen that arrears of property tax had increased from ₹93.71 crore in 2015-16 to ₹209.41 crore in 2016-17. Further, the closing balances of previous years had not been adopted as opening balances during the subsequent years. The reasons thereof were not furnished by DMA.

<sup>20</sup> The figures for the years 2012-13 to 2015-16 furnished (October 2017) by DMA and BBMP varied with the information furnished during January 2017 for the same period, which needs reconciliation.

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

(₹ in crore)

Year	Budget estimate	Actual collection	Percentage of collection
2012-13	2,000.00	936.76	47
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

Source: Budget and details furnished by BBMP

BBMP did not achieve the targets for collection of property tax during the period 2012-13 to 2016-17 and the collection ranged from 28 to 66 *per cent* of the budget estimates.

### 3.5.1.7 Non/short remittance of cess by Bruhat Bengaluru Mahanagara Palike

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>21</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.

Test-check of records in the office of Chief Accounts Officer, BBMP showed that huge balances of cess collected during the period 2012-13 to 2016-17 were not remitted to the departments concerned as detailed in the **Table 3.7**:

**Table 3.7: Details of Collection, remittance and balance of cesses**

(₹ in crore)

Year	Health cess			Library cess			Beggary cess		
	Collected	Remitted	Balance	Collected	Remitted	Balance	Collected	Remitted	Balance
2012-13	140.51	0	140.51	56.20	25.15	31.05	28.10	9.00	19.10
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
<b>Total</b>	<b>857.73</b>	<b>0</b>	<b>857.73</b>	<b>343.08</b>	<b>159.73</b>	<b>183.35</b>	<b>171.53</b>	<b>61.67</b>	<b>109.86</b>

Source: Information furnished by BBMP

While BBMP had not remitted the entire health cess of ₹857.73 crore collected to the State Government, the balance of library cess (₹183.35 crore) and beggary cess (₹109.86 crore) were not remitted to the departments concerned.

<sup>21</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.

### 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 2017, 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.

#### 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 2016-17, audit of 46 out of 270 ULBs were completed (October 2017).

#### 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 2014-15 to 2016-17.

## 3.6 Conclusion

Out of 18 functions to be devolved to ULBs, the State Government had devolved 17 functions. As of March 2017, 132 IRs containing 1,911 paragraphs were pending for more than three years, indicating inadequate action on the part of ULBs. The State Government did not have an Internal Audit Wing to oversee

the functions of ULBs. KSAD had not audited the accounts of BBMP for the years 2014-15 to 2016-17. BBMP had not remitted health cess and had short remitted library and beggary cess. The State Government released only 6.41 *per cent* of NLNORR as against the stipulated 10 *per cent*. The State Government did not release interest amounting to ₹1.70 crore to ULBs for delayed transfer of FFC grants. BBMP, though ineligible, received ₹81.77 crore as performance grants during 2016-17.