

## **CHAPTER VIII**

### **FINANCIAL ADMINISTRATION**

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Municipalities are responsible for providing a variety of governmental services. To facilitate provision of these services, state law grants the governing authorities (board of aldermen, city council, etc.) of each municipality with specific powers, such as the right to raise revenue, expend money, and hold property. The exercise of these powers demands strict financial administration and accountability.

Financial administration is the management of assets and liabilities. The goal of financial administration is to ensure that assets, such as cash, are accounted for and managed according to law, so they will be sufficient to meet the needs of the municipality in a cost-effective manner. This goal is best accomplished by setting up a system that protects assets from loss or waste and provides financial information to the governing authorities in a timely fashion.

The governing authorities of each municipality should give careful consideration to the design of its system of financial administration. The system must comply with state law and the State Auditor's regulations. However, each municipality has authority to tailor the system to meet its own needs. The system may be designed to produce any information the governing authorities require. In establishing a system of financial administration, a municipality may employ as many people as necessary and may use manual or computer methods. Consultation with other municipalities and Certified Public Accountants (CPAs) can be helpful in the design of the system.

The first step in setting up a financial administration system is the employment of competent personnel. By law, the municipal clerk has most of the financial administration duties. If the clerk is elected, he should be given qualified support personnel; if the clerk is appointed, he should, above all, be qualified in financial administration. The clerk must have knowledge of accounting and municipal legal requirements. Municipalities may provide necessary education for its employees, such as participation in the Mississippi State University Extension Service's Certification Training Program for Municipal Clerks and Tax Collectors which is administered by the Center for Governmental Training & Technology.

A good accounting system produces the information necessary for proper management of the municipality. The system should be continuously reviewed to ensure that all needed information will be produced. For example, large cash balances may only be invested if it is known that they actually exist. The most important thing to remember is that the information must be distributed in a timely fashion to everyone who needs the information.

The following sections of this chapter deal with specific areas of responsibility in a system of financial administration. These important obligations should be understood to achieve proper financial administration.

## STATE LAWS AND REGULATIONS

To a large degree the financial administration of a municipality is dictated by state law and regulations issued by the State Auditor. It is very important to understand what must be done and how it is to be done. Failure to follow legal procedure could result in a loss of municipal resources and personal liability on the part of the municipal officials.

Title 21 of the *Code* (Volume 6) contains most of the laws concerning municipal financial procedures. A review of Chapter 33 (Taxation and Finance), Chapter 35 (Municipal Budget) and Chapter 39 (Contracts and Claims) in Volume 6 is recommended. In addition, municipal officials should read the *Municipal Audit and Accounting Guide (MAAG)*. This guide contains regulations prescribed by the State Auditor and should be on file in the city clerk's office.

### BUDGETING

Budgeting is the cornerstone of financial administration and is the responsibility of the governing authorities. It is the once-a-year process of evaluating the needs of the municipality and its resources. The budget process is the time when priorities are established and the hard decisions of what will and will not be done are made.

The budget process is one of the times when information from the financial administration system is most important. The best way to predict the future is to look at the past.

#### Budget Laws

Chapter 35 of Title 21 of the *Code* outlines the general budgeting process. This chapter sets the budget year, publication and public hearing requirements, and the form of the budget. It also requires the State Auditor to prescribe the forms and procedures, sets the procedure for emergency expenditures and loans, allows for budget revisions, and requires annual audits. The State Auditor's forms and procedures are included in the *MAAG*.

*Code*, § 27-39-201 *et. seq.* requires that a public hearing be held on the budget and specifies the form of the public notice for the hearing. This public hearing and notice is in addition to the public hearing and notice requirements of *Code*, § 21-35-5.

*Code*, § 21-35-17 imposes personal liability upon responsible municipal officials if the budget is exceeded. *Code*, § 21-35-33 imposes criminal responsibility upon municipal officials who do not comply with budget laws.

#### Budget Preparation Process and Calendar

The budget is best developed within a formal "building block" process. To manage the various steps in budget preparation, it is advisable to use a budget calendar. A budget calendar sets deadlines for each step of this process. The following budget calendar is suggested, but it may be adjusted to meet the needs of the municipality. The stages of this process are outlined in the following table:

<i>Month</i>	<i>Steps in the Budget Process</i>
May	<p>Starting the Budget Process</p> <ol style="list-style-type: none"> <li>1. Policy making – What will be done, how it is done, and deadlines</li> <li>2. Assigning personnel – Who will do what</li> <li>3. Requesting information – Past practices and outcomes, legal changes, budget officer's forecast, new initiatives, and obligations</li> </ol>
June	<p>Initiate Procedure for Departmental and Outside Agency Requests</p> <ol style="list-style-type: none"> <li>1. Distribute departmental budget worksheets and policies – Forms from MAAG</li> <li>2. Contact dependant groups for budget request – Library, airport, legal donees, etc.</li> <li>3. List of obligations – Debt payments, shared cost, etc.</li> </ol>
July	<p>Receive and Consider Request</p> <ol style="list-style-type: none"> <li>1. Compare to past request</li> <li>2. Ask of justification</li> <li>3. Determine available funding</li> </ol>
August	<p>Prepare the Recommended Annual Budget</p> <ol style="list-style-type: none"> <li>1. Use forms from the MAAG</li> <li>2. Issue public notice of budget and tax levy public hearing</li> <li>3. Hold public hearing</li> <li>4. Adjust budget as finally agreed upon</li> </ol>
September	<p>Adopt and Implement Final Budget</p> <ol style="list-style-type: none"> <li>1. Adopt budget and tax levy by September 15</li> <li>2. Issue public notice of final budget</li> <li>3. Inform departments and others affected by budget</li> <li>4. Make budget available to departments</li> <li>5. File with municipal clerk</li> </ol>

### Monthly Budget Report

*Code*, § 21-35-13 requires a budget report be made to the governing authorities at each month's regular board meeting. This report presents the status of the budget, including the revenues and

expenditures to date and current charges. With each report, an evaluation should be made to ensure that budget estimates are on track and sufficient funds are available to pay current bills.

### Budget Amendments

*Code*, § 21-35-25 allows the governing authorities to revise the budget. Routine revisions may be made as often as are necessary. However, at the point where a department's total budget has been revised up or down by 10 percent or more, public notice must be given of the change.

There are revision limitations. During the first three months of office, while operating under the prior governing authority's budget, the new governing authorities are limited to one revision if a deficit is evident. This revision must be made no later than the August regular meeting. Also, the budget must be revised by the July regular meeting if a deficit occurs or a revenue item is not realized.

### Emergency Expenditures

*Code*, § 21-35-19 and § 21-35-21 allow the governing authorities, with a unanimous vote, to authorize emergency expenditures in the event of emergencies specified in the law – fire, flood, storm, health, etc. The law allows an emergency loan to be made and the budget to be revised for the emergency.

*Code*, § 31-15-17 through § 31-15-31 should be reviewed for local organization of emergency management authority and special powers which take effect when the governor declares a state of emergency.

## REVENUE SOURCES

Providing public services costs money. State laws grant municipalities authority to impose certain taxes and charges for its services. *Code*, § 21-17-5 (municipal home rule) makes clear that a municipality may not impose a tax or issue debt without specific authority.

Revenue sources may be local, state, or federal. Some revenues may be restricted. This means they must be spent for specified purposes, such as the *Code*, § 83-1-37 requirement that insurance rebate money from the state be spent to improve fire protection.

### Local Source Revenue

Typical local sources of revenues are privilege taxes, fees for services, utility system rates, franchise fees, permit fees, and ad valorem taxes. However, there may be local revenues unique to a particular municipality due to special laws, such as local share taxes on casinos.

Ad valorem tax is one of the most important local revenues. It is used to make up the difference between other revenues and the amount of total revenue necessary to fund the budget. With certain exceptions, such as for new property, debt service, and mandatory new programs, this tax is limited

by *Code*, § 27-39-321 to a growth of 10 percent over prior year dollar collections, unless allowed by a special election. *Code*, § 27-39-205 requires a public notice and hearing for tax increases, and *Code*, § 21-33-47 requires certification to certain other governmental agencies and public notice of the final tax levy.

*Code*, § 21-33-53 requires municipalities to assess and collect ad valorem taxes in the same way as counties. They must use the county assessment rolls and collect the tax at the same time and subject to the same penalties as the county. Municipalities may contract with the county to collect this tax. The county may retain a share of the collection as provided by *Code*, § 25-7-21. With an interlocal cooperative agreement (*Code*, § 17-13-9), the county may conduct the sale of land for delinquent taxes.

Utility system rate collections are another important revenue. *Code*, § 21-27-23 allows municipalities to operate specified utility systems and charge for their services. It does not allow rates to be set to produce money to be transferred to the general fund of the municipality.

### State and Federal Source Revenues

State and federal source revenues are received from the state or federal government. These sources of revenue include such things as sales tax, homestead exemption reimbursements, insurance rebate funds, and federal grants.

Sales taxes are usually the most important state source revenue. *Code*, § 27-65-75 provides for a share of state sales taxes collected within each municipality to be paid to that municipality.

### Loans

Loans may only be made with specific legal authority. There are many specific provisions for loans depending on the purpose of the loan. Care should be taken to document legal authority and to follow that authority's procedure if a loan is made. The most commonly used authority for bonded debt is *Code*, § 21-33-301. The authority for lease purchases is *Code*, § 31-7-13 (e); for notes as an alternative to bonds, *Code*, § 17-21-51; and for revenue shortfalls, *Code*, § 27-39-333.

### Transfers

Money may be transferred from one fund to another only with specific legal authority or if the fund transferring the money has all of the expenditure authority of the fund to which the money is being transferred. For example, the general fund may transfer money to the library fund under *Code*, § 39-3-7 or the general fund may transfer money to the utility system under *Code*, § 21-27-59.

Surplus funds occur when the purpose of a fund is completed, and money is left over which cannot be used as intended. For example, when a bonded debt is paid off and a balance remains in a debt service fund. In this case, *Code*, § 27-105-367 explains the procedure to transfer this money to another fund. Care should be taken to prevent surplus funds from developing, because this transfer process can take up to a year to complete.

Transfers from utility systems to the general fund should not be made unless (1) rates are set in good faith for operations only and (2) there is an unexpected windfall profit in the revenue account as provided by *Code*, § 21-27-57 or funds develop through unexpected efficiency and all debt is paid off as provided by *Code*, § 21-27-61.

## EXPENDITURES

The governing authorities of a municipality provide governmental services by hiring people, purchasing property and supplies, and contracting for services. However services are provided, they will cost money. As with most other things in municipal government, the process of spending money is defined by law.

### Appropriations

*Code*, § 21-17-7 and § 21-13-3 allow the governing authority to appropriate funds. This is the process of making money in the budget available to municipal departments or outside dependent organizations such as domestic violence shelters.

The authorizing order of the governing authority should explain how funds are to be paid. For example, funds appropriated to a municipal department are expended as salary and bill payments through the claims process, subject to appropriation limits. Funds appropriated to a dependent organization are paid on the date and in the amount specified in the order.

### Contracted Obligations

*Code*, § 25-1-43 requires specific authority from the municipal authorities to enter into a contract. Contracts should be entered upon the minutes, approved by the governing authority, and signed by the designated officer. Purchasing agents should be designated, and their routine purchase authority defined.

### Claims Process

Claims are the request for payment for services and supplies received by the municipality. *Code*, § 21-39-5 requires claims to be received, dated, and filed by the city clerk in the order in which they are received, and establishes claims as a public record. *Code*, § 21-39-7 goes a step further and requires a formal claims docket for municipalities with populations of more than 2,000.

*Code*, § 21-39-9 requires the governing authority to review all unpaid claims and determine if there is an obligation. An obligation exist if the related materials and supplies were properly contracted and received. The governing authority should adopt procedures so that it will have the information it needs to determine if an obligation exists and the claim should be paid. Procedures should include some method to ensure that materials and supplies were received. One such method is to have the responsible official verify receipt of the goods by signing the claim or providing a receiving report.

### Claims Exceptions

Some items need not be presented as a claim for the governing authority to authorize payment. Generally, these are items where there is no preexisting obligation, such as an appropriation to a dependent organization, a donation to an authorized beneficiary, or payment of a scheduled bonded debt. The Attorney General's Opinion to Ronald S. Cochran of March 8, 1996, provides insight into exceptions to the claims system. *Code*, § 21-39-7 allows salaries to be paid after being earned, but prior to claim approval, if the governing authority authorized such payments and the wages have been established by order of the governing authority or as a separate budget item.

### Claims Disallowed

Claims not found to be legal obligations should be disallowed, or payment of these claims may be viewed as a donation. Section 66 of the *Mississippi Constitution* and *Code*, § 21-17-5 prohibit donations without specific authority. A payment in advance constitutes a donation and may not be authorized. Claims may be held for further consideration, pending presentation of additional information. For example, a claim based on a statement rather than an invoice should have verification that it has not already been paid.

*Code*, § 21-35-17 imposes liability upon the governing authority for approving claims in excess of the budget. The city clerk's budget report should verify that funds are in the budget to cover the claim. Responsible officials should explain obligations in excess of their budget. The board may amend the budget as previously discussed.

*Code*, § 21-39-11 allows claimants to appeal to circuit court if they wish to challenge the governing authority's decision. *Code*, § 31-7-57 explains that vendors who acted in good faith and did not participate in a purchase law error are entitled to payment. These vendors may also appeal to circuit court.

### Claim Payments

*Code*, § 21-39-13 and § 21-35-17 provide that when claims are approved, the city clerk must determine that the funds are available in the budget and sufficient cash is in the municipal depository to pay the claims. Upon this determination, the mayor or majority of the governing authority must sign the check, and the city clerk must attest the check. Payment is then promptly made to the claimant.

*Code*, § 31-7-305 requires that claimants be paid within 45 days after services have been provided and claims filed. It is the municipality's obligation to add 1½% interest per month to any claims, not in dispute, paid later than 45 days.

There is no responsibility for the governing authority to determine that cash is available for it to approve a claim. It is presumed that since funding is in the budget, cash will be available within the fiscal year. In the event that cash is not currently available, *Code*, § 21-33-325 provides for tax

anticipation loans of up to 50 percent of ad valorem taxes. However, the loan must be paid back by March 15 of the fiscal year.

## CASH MANAGEMENT

Proper cash management is necessary for financial planning, security, and legal compliance. Municipal authorities should understand when and where cash is collected, how it is handled, and where it is held. Policies should be developed to ensure that cash is secure and available when needed.

### Cash Flow

The time cash is received rarely matches the time it is needed. The budget and taxing process makes cash available during the fiscal year, but does not ensure that it will be available when municipal services are required. For example, cash collections may be low until January when most ad valorem tax collections are made.

Cash shortfalls cost the municipality in late charges due to vendors and cost the public in delayed services. Unmanaged surpluses cost the municipality through lost investment interest. The flow of cash should be analyzed so shortfalls and surpluses of cash can be anticipated and managed. Expected cash shortages may be offset by budgeting a beginning working cash balance or making a tax anticipation loan. Cash surpluses may be invested and interest may be earned on the investment.

### Cash Security

Obviously, cash security is a major concern. State laws require some security measures; however, every situation is different and demands constant evaluation. Every step of the flow of cash should be examined to assure that there is accountability and security. This evaluation should be done by a qualified CPA during the annual audit.

Employees whose duties involve handling cash should be screened very carefully. They must be trustworthy and competent to perform their duties correctly. State law requires that every employee who handles cash be bonded. This bond protects the municipality from loss due to the employee. Municipalities should also consider purchasing theft insurance and errors and omissions insurance.

### Cash Investments

*Code*, § 21-33-323 allows municipalities to invest their surplus funds; however, this is a very restrictive authority. They may only invest in direct obligations of the United States, or the State of Mississippi, or certain local Mississippi governments. They may also invest in certificates of deposit from the municipal depositories or State of Mississippi depositories located within the municipality. There is no authority to invest in mutual funds or brokerage firm accounts.

## MUNICIPAL DEPOSITORIES

*Code*, § 27-105-353 and § 27-105-363 require municipalities to commission one or more depositories to serve the municipality for two year terms. The municipality must give notice to qualified financial institutions in December and receive bids in January. The selected depositories must pledge certain securities to secure deposits and should outline their services and fees.

## ACCOUNTING

*Code*, § 21-35-11 requires the city clerk to maintain accounting records as prescribed by the State Auditor. The State Auditor prescribed the accounting system in the *MAAG*. As required by *Code*, § 21-35-11, the system is designed to be on a cash basis to show the status of the budget.

Generally, this cash basis system requires journals to record all receipts and checks written. These are classified as revenues and expenditures as set out in the budget. Each month, this journal is totaled into a ledger. This system may be manual or computer-based. It may also contain such additional information as the municipality may require. These are public records and must be available to the public for inspection during normal office hours.

## PROPERTY

Providing services requires the use of real and personal property. *Code*, § 21-17-1 provides authority for municipalities to acquire, hold and dispose of property. As with cash, property must be accounted for and secured. It should also be managed to assure legal use, proper maintenance, and continued need.

### Real Property

*Code*, § 21-17-1 provides that real property may be purchased for municipal purposes. However, *Code*, § 43-37-1 requires that an appraisal be made and the appraised value communicated to the owner. Certain real property may be lease-purchased under *Code*, § 31-8-1.

Real property disposal must be made by public sale after three weeks of advertising. There is a special procedure for a sale to a particular buyer: it must be in the municipal interest and foster community, economic, educational, etc. interest. Real property may also be donated to certain not-for-profit corporations.

### Personal Property

The *MAAG* requires that certain personal property be accounted for and tagged. Municipal policy should assign responsibility for property items, and an annual inventory must be held to verify custody. Missing items must be justified, or responsible officials could be held liable.

Personal property may be disposed of by the governing authority through negotiated sale, public sale, trade-in, or “junking.” Such disposal and its justification should be documented on the

minutes. Fair market value must be received, unless the property is being transferred to a state agency, another governing authority, or an organization to which the municipality has authority to appropriate money. In this case, the terms of the agreement must be documented on the minutes as well.

### Marking Motor Vehicles

*Code*, § 25-1-87 requires motor vehicles to have the name of the municipality marked in 3 inch letters on the sides and 1½ inch letters on the rear, or a 12 inch municipal decal on the sides. This must be a permanent marking and in a contrasting color. There is provision for certain unmarked vehicles, if authorized in the governing authority minutes and if notification is made to the State Auditor. Verification of legal marking is made by the State Auditor. Municipalities found with improperly marked vehicles may have their sales tax revenue suspended.

## INTERNAL CONTROL

Internal control occurs through the organization of financial affairs to create a system of checks and balances that safeguards assets and assures legal compliance. No one system works for every municipality. Each governing authority must constantly review its operations and personnel in a effort to minimize weaknesses.

An example of a weakness would be more than one employee using the same cash drawer for collection of water bills. In this case, if money is missing, there is no way to absolutely assign responsibility. This results in liability being assigned to the person in charge which is probably the municipal clerk. An evaluation of internal control should be made by a qualified CPA during the annual audit.

## ANNUAL AUDIT

*Code*, § 21-35-31 requires every municipality to contract an audit within 12 months of the fiscal year's end. This audit must be contracted with a CPA or an auditor approved by the State Auditor. The auditor must conduct the audit as prescribed by the State Auditor in the *MAAG*.

Municipalities with a population of fewer than 3,000 and declaring a financial hardship may contract for a compilation in lieu of an audit. This is a cheaper contract with a more limited report and less audit work.

Municipalities who have received federal funds, directly or indirectly, may be required to have special federal audit work such as a federal single audit. A CPA must do this type of audit and should be consulted to determine audit responsibilities. Municipalities may also contract with CPAs for any additional audit or other services, if required. The annual audit is a good time to have special studies of internal control, accounting systems, and overall efficiency.

Within 30 days of completion of the audit, public notice of audit availability must be given. Also, copies of the audit must be sent to the State Auditor. Copies should also be sent to federal or state agencies as required by grant or loan contracts.

#### STATE AUDITOR'S SERVICES

The State Auditor's office does not perform routine financial audits of municipalities. The State Auditor does assign personnel to check municipal motor vehicles for proper markings and to investigate activities in municipalities when property may have been illegally purchased or used. Investigations may be initiated by citizen complains (which are kept confidential) or the State Auditor's own initiative.

To provide up-front help, the State Auditor issues a monthly publication entitled *Technicalities* which is mailed to each municipality and which may be viewed or downloaded over the Internet at <http://www.osa.state.ms.us/>. This publication provides answers to commonly asked questions and provides information about recent legal changes. Municipal officials should read *Technicalities* and keep copies on file for future reference.

The State Auditor also maintains a hotline at 1-800-321-1275. This number may be used to contact his office. His department of technical assistance has staff members on call to help municipal officials understand their legal options. If there is any doubt about the legality of a contemplated financial action, technical assistance should be requested.