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August 8, 2019

Cody Pearce  
Statewide Accounting Bureau  
Department of Administration  
P.O. Box 200102  
Helena, MT 59620

BY ELECTRONIC DELIVERY TO: [LGSPortalRegistration@mt.gov](mailto:LGSPortalRegistration@mt.gov)

Dear Ms. Pearce:

The Montana League of Cities and Towns (MLCT) is an incorporated, nonpartisan, nonprofit association of all 127 Montana municipalities. We submit these comments on behalf of our members on the Montana Department of Administration's proposed amendment to ARM 2.4.401, 2.4.402, 2.4.403, 2.4.404, 2.4.405, 2.4.406, 2.4.409, 2.4.410, and 2.4.411 pertaining to accounting and financial reporting standards, report filing fees, filing penalties, waivers and extensions of penalties, audit and audit reporting standards, the roster of independent auditors, resolution and corrections of audit findings, financial reviews, and incorporation by reference of various standards, accounting policies, and federal laws and regulations and the repeal of ARM 2.4.408 pertaining to audit contracts, as published in MAR Notice No. 2-4-581 on June 21, 2019.

We encourage you to consider the following concerns expressed by our members, and make changes to the proposed regulations to better reflect the needs and local authority of municipalities:

ARM 2.4.401 – Accounting and Financial Reporting Standards.

- (1) The proposed changes to this ARM include the addition of the term "special purpose districts." This term is not defined in any existing or proposed administrative rule or state statute. The Statement of Reasonable Necessity indicates that the rule is being amended to clarify that all local governments other than school districts and associated cooperatives are subject to the ARM. This terminology is confusing, as "special purpose district" is a term that can and is used to refer to such governmental sub entities as an assessment district established within a city or town. Section 2-7-501, MCA uses and defines the term "local government entity" and includes a long list of example districts that are included within that term. We request that you use the term "local governmental entities" instead of "special purpose districts" in ARM 2.4.401 for consistency with the statute and clarification of the applicability of the requirements.

- (2) The proposed changes to this ARM also include adoption by reference of the new Small Government Financial Reporting Framework (SGFRF), with a reference to ARM 2.4.411. We support the Department's work to provide a streamlined, reduced accounting framework as an alternative to the increasingly stringent, complex, time-consuming, and cost prohibitive Generally Accepted Accounting Principles (GAAP) developed by the Governmental Accounting Standards Board (GASB). We welcome any alternative to this framework that will help local governments save them money, reduce issues of training and retention, and help streamline the process. However, we have concerns about the structure being proposed by the Department for the use of this new framework.
- (i) We would like to confirm that the GASB compliance requirement set forth in the proposed amendments to ARM 2.4.401(1) is not applicable to those local government entities that qualify for and choose to use the SGFRF reference in (2). If yes, then we request that (1) be modified to begin with "Except as provided in (2), all counties, cities, ..."
- (ii) The Department proposes to limit the use of the SGFRF to local government entities with a population of 2,500 or less. The Department makes no mention of this arbitrary decision in either the proposed rules or its statements of reasonable necessity. When asked about this proposed population limit, the Department has referenced one of the exceptions to the municipal classification system set forth in Section 7-1-4112(3), MCA that allows towns with a population of a third-class city to remain a town until it reaches a population of 2,500. This reasoning is misplaced. The classification system is an antiquated system that was not based on any specific need or substantive issue, and hasn't been modified since it was adopted in 1895. Secondly, it only applies to municipalities, whereas the vast majority of local governmental entities subject to the local government accounting standards are not municipalities.

The Department's statement of reasonable necessity specifically points out that the SGFRF will relieve small communities of "the most costly and burdensome aspects of financial reporting that lack relevance to the users of those local governments. One such example is actuarially determined post-employment benefit information, which is not only highly technical and expensive to produce, but also does not factor into the day-to-day, cash-basis or budgetary-basis decisions of the governing officials of small, rural governments." Of the 13 municipalities the Department will leave out of the SGFRF option, 3 of them have had findings on this specific reporting point but will be left out of the Department's proposed fix.

We specifically request that the Department increased the proposed population limit for use of the SGFRF to local government entities with a population of 5,000 or less. Under the current proposal, SGFRF will be available to 98 municipalities; doubling that limit to 5,000 would allow an additional 13 municipalities to use the framework. These communities are still small by any measure; they have small budgets and face the same staffing and resource difficulties with understanding and complying with the existing standards. The additional municipalities are Columbia Falls, Conrad, Cut Bank, Deer Lodge, Dillon, Glasgow, Glendive,

Hamilton, Hardin, Libby, Polson, Shelby, and Wolf Point (in the next census, Columbia Falls and Polson will likely fall off this list). There is no reasonable argument that these entities are too large to be able to take advantage of a proposal that will help save them money, reduce issues of training and retention, and help streamline the process for small communities.

- (iii) The rule as proposed will require our members to submit an application in order to be “approved” by the Department to use the alternative SGFRF. Neither proposed ARM 2.4.401 or 2.4.411 provide any information about the requirements, standards, criteria, or timeline for this application or approval process. The only criteria identified anywhere is in the SGFRF one-page summary that is proposed to be adopted by reference in 2.4.411:

“(1) A county, city, town, or special purpose district... may submit to the department an application for approval to report in accordance with the small government financial reporting framework ... *if the local government entity meets the following eligibility criteria:*  
(a) *if applicable, the population of a county, city, or town does not exceed 2,500, as reported in the most recent decennial survey issued by the United States Census Bureau*  
(b) *if applicable, a special purpose district is not a school district or a special education cooperative.*” (Italics added.)

As such, the Department is proposing to create a new bureaucratic, time-consuming application, review, and approval process to simply confirm the population of a community as published in the publicly available decennial census. This added requirement is unnecessary and we request that it be deleted from the final rule proposal. If a local government entity meets the population criteria, it should simply be allowed to choose whether to use the SGFRF. If the Department wants to track that information, it can modify its reporting templates to include a question or notation indicating whether the optional SGFRF is being used.

- (iv) Why is the Department not adopting the SGFRF standards into the rules directly? The proposed standards are not overly complex or lengthy. The statement of reasonable necessity indicates that this structure “facilitates beneficial coordination with other local government resources provided to assist the annual financial statement preparation process. Those resources include the annual financial report form and the uniform chart of accounts authorized at 2-7-503, MCA.” How does having a separate document, incorporated by reference, create coordination? We appreciate the simple, short SGFRF document, but in order to ensure clarity and transparency, we request that the Department adopt the standards directly into the rules and not by reference.
- (v) The Department has verbally indicated to our members that if a municipality chooses to use the SGFRF framework, it will need to enter into a separate contract with the auditor, approved by the Department, to use that framework. There is nothing in the proposed ARM rules or the referenced SGFRF document that

provides any information or specific proposal about this requirement. In addition, the Department has verbally indicated that the auditor for a local government entity will now be required to do the GASB statements for the entity. If true, this is yet another layer of unnecessary, costly, time-consuming bureaucratic requirements that will further exacerbate the growing crisis that local governmental entities have with finding and retaining qualified accountants and auditors to perform the requirements being set by the Department. This will result in increasing late reporting, missed deadlines, and growing penalties with no benefit to our local taxpayers. We request that the Department address whether it plans to move forward with these proposals and if so, incorporate those requirements into the ARMs and explain the reasonable necessity for the requirements.

#### 2.4.403 Penalties for Failing to File Reports Within Prescribed Time

Please confirm that the Department proposes to delete ARM 2.4.403(1) because it interprets Section 2-7-517(4), MCA to provide the Department with the same authority to grant extensions or waive fines, fees, and other penalties for late reporting.

#### 2.4.404 Penalty for Failing to Pay Filing Fee Within 60 Days of Due Date

We appreciate the Department's proposals to streamline these administrative rules. As a potential further clarification that may help in that regard, please consider combining ARMs 2.4.403 and 2.4.404 into one section.

#### 2.4.405 Audit and Audit Reporting Standards

- (1) As explained in our comment (2)(i) on the proposed amendments to ARM 2.4.401, proposed ARM 2.4.405(1) should begin with "Except as provided in (2), audits or audit reporting..."
- (2) Although it is mentioned nowhere in the proposed rules or the accompanying SGFRF document, the Department has verbally indicated to our members and stated in its newsletter that "governments having grant or bond agreements that require reporting in accordance with Generally Accepted Accounting Principles SHOULD NOT apply for the regulatory Basis Reporting Framework, as they would then be in noncompliance with those requirements."
  - (i) We hope that the Department is willing to work with and actively reach out to other state agencies that use template GAAP compliance language in their contracts and their federal agency partners, if necessary, to help them understand the changes and assist in creating alternative language that allows local government entities, where possible, to use SGFRF and still be eligible for state and federal grants, loans, and other funding. This is a critical piece to the success of SGFRF as a relief for smaller local governments, nearly all of whom have some type of infrastructure funding agreement with a Montana state agency for state or federal grants or loans.
  - (ii) Our members would like clarification about whether the SGFRF will be available to communities that qualify for the small government framework but also receive a federal grant, loan, or other funding award. Is this simply a matter of whether the

contract reflects the appropriate accounting standards in the contract with the federal agency? If SGFRF will not be available to any local government entity that receives a federal award, how long will that prohibition last? Is there a possibility that there are particular federal award auditing and reporting standards that can be used, so that SGFRF can continue to be used but supplemented with the necessary reporting and auditing information pertaining to items relevant to the federal award?

2.4.409 Actions by Local Government Entity Governing Bodies to Resolve or Correct Audit Findings and Penalty for Failure to Do So

- (1) SB 302 (Section 1, Chapter 268, Laws 2019) amends Section 2-7-515(1), MCA to require a local government to submit a “corrective action plan that details what action or actions they plan to take on any findings or recommendations contained in the audit report.” Existing ARM 2.4.409(1) uses similar language. The proposed amendments to ARM 2.4.409 uses only the terminology “submit its planned corrective measures.” Please confirm that the Department interprets these different terms to refer to the same requirement.
- (2) Proposed ARM 2.4.409(1) provides for publication on the Department’s website if the local government entity misses the 30-day statutory deadline. In existing and proposed ARM 2.4.403 related to financial and audit reports, such publication does not occur until 180 days after the original statutory deadline is missed. We request that the Department consider a similar, consistent later deadline before the publication of delinquent audit responses in ARM 2.4.409.
- (3) Proposed ARM 2.4.409(2) refers to corrective measures adopted by the local government entity that are either being accepted or accepted with modifications. However, the statute preserves the authority of the local governmental entity to reject noted deficiencies or proposed recommendations for improvement. (Section 2-7-515(2), MCA.) This section should be reordered or restructured to reflect that rejecting a recommended measure, or taking no corrective measure, may also be an acceptable response to a noted deficiency in an audit or financial review report.
- (4) Under SB 302, there are now penalties and potential legal liability for failing to resolve significant audit findings or implement corrective measures. (Section 4, Chapter 268, Laws 2019.) Unlike the failure to meet a deadline, this failure is a discretionary determination that will involve a weighing of the evidence and findings being made by the Department. Therefore, it is critical that the process the Department engages in when making a final determination is transparent, understandable, and provides due process. In that respect, we request the Department amend the proposed rules with detail regarding the internal process that the Department will follow in making “a determination of the acceptableness of the local government entity’s planned corrective measures.” Will the decision be made by a particular staff person? What internal review of that decision will the Department make? Will there be a process for appealing a decision by an individual employee, that employee’s supervisor, or the Department director?
- (5) SB 302 amended Section 2-7-515, MCA to add the qualifying term “significant” to the Department’s ability to withhold financial assistance, and provides a process for administrative and judicial review of a failure to resolve “significant” findings. In this

respect, providing a clear definition of the term “significant” is critical for local governmental entities, the public, and the Department.

The proposed amendments to ARM 2.4.409 provide no definition of “significant” whatsoever. Instead, proposed ARM 2.4.409(4) allows the Department to “request additional details, supporting information, or evidence of implementation of the corrective measures [for findings it deems to be significant]” and proposed ARM 2.4.409(5) explains the Department will “base the significance of findings on the risks to the entity of doubtful going concern, significantly distressed operations, or substantially unprotected public interest.”

This reference to significance and the reservation of unfettered discretion on the part of the Department as to what constitutes a “significant” finding does not provide sufficient definiteness or specificity to local government entities seeking to avoid such a determination on the part of the Department. Nor does the language provide any substantive limits on the Department’s exercise of discretion in making a final determination as to significance. Finally, as set forth above, there is no clear process for appealing a determination of significance; as written, the proposed rule allows only the Department to seek additional information or details regarding the significance of a finding. Under the proposed language, this entire process could happen with no knowledge or involvement of the local government entity.

We respectfully request that the Department reconsider and revise the proposed rules with respect to this critical process and terminology. At the very least, the Department’s discretion to determine significance should be limited with an adopted definition of “significant” as “findings that pose a risk to the entity of ongoing concern, significantly distressed operations, or a failure to protect a substantial public interest.”

- (6) Section 2-7-515, MCA applies specifically to audits and responses thereto. The statute provides no authority whatsoever for subjecting financial review reports to the same process set out for audits and audit findings. The statute does not authorize the Department to withhold financial assistance for a failure to resolve financial review report findings or implement corrective measures related thereto, nor does SB 302 provide an administrative or judicial review of such failures. We respectfully submit that the Department does not have the statutory authority to include financial review reports in the requirements being added by the proposed amendments to ARM 2.4.409.
- (7) Section 2-7-515, MCA, as amended by SB 302, provides a process for a conference between the parties if the Department rejects a local government entity’s proposed corrective measures. The proposed amendments to ARM 2.4.409 are silent on this requirement and where it fits into the process outlined in this ARM. We request that the Department add it into the proposed amendments, and then modify the proposed new subsection (4) to begin as follows: “If the department ~~does not receive~~ and the entity cannot agree to acceptable corrective measures...”
- (8) There appears to be a disconnect between the proposed language in new ARM 2.4.409(6) and (8). Subsection (6) refers to the previous withholding of financial assistance, but nowhere do the proposed amendments provide any discussion as to when or why it might be withheld upon an initial significant finding. Subsection (8),

however, provides details for when or why financial assistance might be withheld upon a repeat finding. We request that the Department provide a similar good cause process outlined in (8) for a withholding on a first finding as referenced in (6)

2.4.411 Incorporation by Reference of Various Standards, Accounting Policies, and Federal Laws and Regulations

Please see comments (2)(i), (ii), (iii) and (iv) with respect to the proposed amendments to ARM 2.4.401. All of those same comments apply to the proposed amendments to new ARM 2.4.411(2).

Conclusion

We appreciate the Department's attempt to streamline the ARMs and provide new methods for reporting and auditing intended to assist small local government entities. We are concerned that as proposed, the changes do not go far enough. We ask the Department to seek and adopt methods and rules that maximize the potential benefits to local taxpayers in the smallest communities that lack the resources to meet the increasingly difficult and complex reporting requirements and recruit, train, and retain qualified staff.

The Department is becoming less and less a resource for these communities; in 2018 it required its field staff to relocate to Helena and lost 2 of the only 3 Department employees who are experienced in local government accounting and auditing standards. This continuing decrease in resources and technical support from the Department has only aggravated the situation. These struggling local governments need your help and the maximum amount of discretion that the Department has the authority to provide. Thank you in advance for your consideration of our comments.

Sincerely,



Tim Burton  
Executive Director

Cc: Toni Henneman, Lead Staff, Local Government Interim Committee