



House of Representatives

General Assembly

File No. 462

February Session, 2024

Substitute House Bill No. 5472

House of Representatives, April 11, 2024

The Committee on Planning and Development reported through REP. KAVROS DEGRAW of the 17th Dist., Chairperson of the Committee on the part of the House, that the substitute bill ought to pass.

AN ACT CONCERNING MUNICIPAL FINANCE AND AUDITS.

Be it enacted by the Senate and House of Representatives in General Assembly convened:

1 Section 1. Section 7-576a of the general statutes is repealed and the
2 following is substituted in lieu thereof (*Effective July 1, 2024*):

3 [(a) Any] The Municipal Finance Advisory Commission may
4 designate any municipality referred to said commission pursuant to
5 subsection (d) of section 7-395 [to the Municipal Finance Advisory
6 Commission shall be designated] as a tier I municipality. The chief
7 elected official of any municipality that does not meet the conditions
8 identified under subsection (d) of section 7-395 may apply to the
9 Municipal Finance Advisory Commission for designation as a tier I
10 municipality, provided such official (1) expects that such municipality
11 will meet one or more such conditions in the following twenty-four
12 month period, and (2) submits a report to the Municipal Finance
13 Advisory Commission, in a form and manner prescribed by the
14 commission, that confirms that such condition or conditions will be met

15 in such period. Each decision to designate a municipality as a tier I
16 municipality pursuant to this section shall be based on an evaluation of
17 such municipality's financial condition and financial practices. In
18 addition to the requirements of section 7-394b, each municipality
19 designated as a tier I municipality shall prepare and present a five-year
20 financial plan to the Municipal Finance Advisory Commission for its
21 review and approval.

22 [(b) The secretary shall refer any municipality designated as a tier I
23 municipality to the Municipal Finance Advisory Commission, pursuant
24 to the provisions of section 7-395. In addition to the requirements of
25 section 7-394b, such municipality shall prepare and present a five-year
26 financial plan to the Municipal Finance Advisory Commission for its
27 review and approval.]

28 Sec. 2. Section 7-576f of the general statutes is repealed and the
29 following is substituted in lieu thereof (*Effective July 1, 2024*):

30 (a) (1) A municipality designated as a tier I municipality in
31 accordance with section 7-576a, as amended by this act, shall retain such
32 designation, notwithstanding any positive changes in the factors
33 leading to its current designation, until the Municipal Finance Advisory
34 Commission, by unanimous vote, terminates such designation based on
35 an evaluation of such municipality's financial condition and financial
36 practices.

37 [(a)] (2) A municipality designated as a [tier I municipality in
38 accordance with section 7-576a,] tier II municipality in accordance with
39 section 7-576b, tier III municipality in accordance with section 7-576c, or
40 tier IV municipality in accordance with section 7-576e, as amended by
41 this act, shall retain such designation, notwithstanding any positive
42 changes in the factors leading to its current designation, until, in the
43 fiscal years following such designation, [(1)] the Municipal
44 Accountability Review Board determines that (A) there have been no
45 audited operating deficits in the general fund of the municipality for
46 two consecutive fiscal years, [(2)] (B) the [municipality's] municipality
47 has a long-term bond rating from one or more bond rating agencies that

48 is investment grade or higher and such bond rating has either improved
49 or remained unchanged since its most current designation, [(3)] (C) the
50 municipality has presented and the [commission or] board has
51 approved a financial plan that projects a positive fund balance for the
52 three succeeding consecutive fiscal years covered by such financial plan,
53 [where] provided (i) each fiscal year of such plan is based upon
54 recurring revenue and expenses, (ii) a positive fund balance of at least
55 five per cent is projected in the third such fiscal year, [and (4)] and (iii)
56 such plan does not include funding received pursuant to section 7-576i,
57 as amended by this act, or 7-576j, (D) the municipality's audits for such
58 consecutive fiscal years have been completed and [contain no general
59 fund deficit] the general fund reports an audited fund balance of at least
60 five per cent, and (E) there is no evidence that the municipality has
61 engaged in unsound or irregular financial practices in relation to
62 commonly accepted standards in municipal finance. The board may
63 undertake the determination described in this subdivision at its
64 discretion or upon the request of a municipality.

65 (b) [Notwithstanding subsection (a) of this section, the Municipal
66 Finance Advisory Commission may, by unanimous vote, end the
67 designation of a municipality designated as a tier I municipality, based
68 on an evaluation of such municipality's financial condition.] (1) If the
69 Municipal Accountability Review Board determines that a municipality
70 has satisfied the criteria listed in subdivision (2) of subsection (a) of this
71 section, the secretary shall, at the secretary's discretion and in
72 consideration of the fiscal condition of the municipality and best
73 interests of the state, terminate such municipality's tier designation or
74 redesignate such municipality to a lower tier, provided no such
75 municipality shall be redesignated as a tier I municipality. Not later than
76 sixty days after the board makes such determination, the secretary shall
77 notify the municipality of the secretary's decision to terminate such
78 municipality's tier designation or redesignate such municipality to a
79 lower tier. A municipality shall retain its existing tier designation until
80 such notice is received. If the secretary fails to provide such notice prior
81 to the expiration of said sixty-day period, the municipality's tier
82 designation shall be deemed terminated on the sixty-first day following

83 such determination.

84 (2) A municipality redesignated to a lower tier pursuant to
85 subdivision (1) of this subsection shall (A) meet the requirements of this
86 chapter pertaining to such lower tier, and (B) not request a
87 determination from the Municipal Accountability Review Board
88 pursuant to subdivision (2) of subsection (a) of this section during the
89 one-year period following such redesignation.

90 Sec. 3. Section 7-576i of the general statutes is repealed and the
91 following is substituted in lieu thereof (*Effective July 1, 2024*):

92 (a) Any designated tier II, III, or IV municipality shall be eligible to
93 receive funding from the Municipal Restructuring Fund, which fund
94 shall be nonlapsing. A designated tier II, III or IV municipality seeking
95 such funds shall submit, for approval by the Secretary of the Office of
96 Policy and Management, a plan detailing its overall restructuring plan,
97 including local actions to be taken and its proposed use of such funds.
98 Notwithstanding section 10-262j, a municipality may, as part of such
99 plan and in consultation with its local board of education, submit a
100 proposed reduction in the minimum budget requirement related to its
101 education budget. The secretary shall consult with the Commissioner of
102 Education in approving or rejecting such proposed reduction. The
103 secretary shall consult with the [municipal accountability review board]
104 Municipal Accountability Review Board in making distribution
105 decisions and attaching appropriate conditions thereto, including the
106 timing of any such distributions and whether such funds shall be
107 distributed in the form of a municipal restructuring fund loan subject to
108 repayment by the municipality. The distribution of such assistance
109 funds shall be based on the relative fiscal needs of the requesting
110 municipalities. The secretary may approve all, none or a portion of the
111 funds requested by a municipality. In attaching conditions to such
112 funding, the secretary shall consider the impact of such conditions on
113 the ability of a municipality to meet legal and other obligations. The
114 board shall monitor and report to the secretary on the use of such funds
115 and adherence to the conditions attached thereto. The secretary shall

116 develop and issue guidance on the (1) administration of the [municipal
117 restructuring fund] Municipal Restructuring Fund, (2) criteria for
118 participation by municipalities and requirements for plan submission,
119 and (3) prioritization for the awarding of assistance funds pursuant to
120 this section. Any municipality that receives funding from the [municipal
121 restructuring fund] Municipal Restructuring Fund, in addition to the
122 other responsibilities and authority given to the board with respect to
123 designated tiers II, III and IV municipalities, shall be required to receive
124 board approval of its annual budgets.

125 (b) The secretary may distribute funds from the Municipal
126 Restructuring Fund to a third party on behalf of a designated tier II, tier
127 III or tier IV municipality. Funds received by a municipality pursuant to
128 this section may be used, in part, to pay an arbitrator selected pursuant
129 to clause (v) of subdivision (3) of subsection (a) of section 7-576e, as
130 amended by this act.

131 [(b)] (c) Notwithstanding the provisions of subsection (a) of this
132 section, in making distributions from the Municipal Restructuring
133 Fund, the board shall give immediate consideration to any municipality
134 that shall default on debt obligations by January 1, 2018, without an
135 immediate distribution of such funds.

136 Sec. 4. Subdivision (2) of subsection (a) of section 7-576e of the general
137 statutes is repealed and the following is substituted in lieu thereof
138 (*Effective July 1, 2024*):

139 (2) The Municipal Accountability Review Board may designate a tier
140 III municipality as a tier IV municipality based on a finding by the board
141 that the fiscal condition of such municipality warrants such a
142 designation based upon an evaluation of the following criteria: (A) The
143 balance in the municipal reserve fund; (B) the short and long-term
144 liabilities of the municipality, including, but not limited to, the
145 municipality's ability to meet minimum funding levels required by law,
146 contract or court order; (C) the initial budgeted revenue for the
147 municipality for the past five fiscal years as compared to the actual
148 revenue received by the municipality for such fiscal years; (D) budget

149 projections for the following five fiscal years; (E) the economic outlook
150 for the municipality; [and] (F) the municipality's access to capital
151 markets; and (G) evidence of unsound or irregular financial practices in
152 relation to commonly accepted standards in municipal finance that the
153 board believes may materially affect the municipality's financial
154 condition. For the purpose of determining whether to make a finding
155 pursuant to this subdivision, the membership of the board shall
156 additionally include the chief elected official of such municipality, the
157 treasurer of such municipality and a member of the legislative body of
158 such municipality, as selected by such body. In conducting a vote on
159 any such determination, the treasurer of such municipality shall be a
160 non-voting member of the board. The board shall submit such finding
161 and recommended designation to the secretary, who shall provide for a
162 thirty-day notice and public comment period related to such finding
163 and recommendation. Following the public notice and comment period,
164 the secretary shall forward the board's finding and recommended
165 designation and a report regarding the comments received in this regard
166 to the Governor. Following the receipt of such documentation from the
167 secretary, the Governor may approve or disapprove the board's
168 recommended designation.

169 Sec. 5. Section 7-393 of the general statutes is repealed and the
170 following is substituted in lieu thereof (*Effective July 1, 2024*):

171 Upon the completion of an audit, the independent auditor shall file
172 certified copies of the audit report with (1) the appointing authority, (2)
173 in the case of a town, city or borough, with the clerk of such town, city
174 or borough, (3) in the case of a regional school district, with the clerks of
175 the towns, cities or boroughs in which such regional school district is
176 located and with the board of education, (4) in the case of an audited
177 agency, with the clerks of the towns, cities or boroughs in which such
178 audited agency is located, and (5) in each case, with the Secretary of the
179 Office of Policy and Management. Such copies shall be filed within six
180 months from the end of the fiscal year of the municipality, regional
181 school district or audited agency, but the secretary may grant an
182 extension of not more than thirty days, provided the auditor making the

183 audit and the chief executive officer of the municipality, regional school
184 district or audited agency shall jointly submit a request in writing to the
185 secretary stating the reasons for such extension at least thirty days prior
186 to the end of such six-month period. If the reason for the extension
187 relates to deficiencies in the accounting system of the municipality,
188 regional school district or audited agency the request must be
189 accompanied by a corrective action plan. The secretary may, after a
190 hearing with the auditor and officials of the municipality, regional
191 school district or audited agency, grant an additional extension if
192 conditions warrant, provided such extension shall not exceed six
193 months from the date the auditor was required to file such copies. Said
194 auditor shall preserve all of his or her working papers employed in the
195 preparation of any such audit until the expiration of [three] five years
196 from the date of filing a certified copy of the audit with the secretary
197 and such working papers shall be available, upon written request and
198 upon reasonable notice from the secretary, during such time for
199 inspection by the secretary or his authorized representative, at the office
200 or place of business of the auditor, during usual business hours. Any
201 municipality, regional school district, audited agency or auditor who
202 fails to have the audit report filed on its behalf within six months from
203 the end of the fiscal year or within the time granted by the secretary shall
204 be referred by the secretary to the Municipal Finance Advisory
205 Commission established pursuant to section 7-394b, assessed a civil
206 penalty of not less than one thousand dollars but not more than [ten]
207 fifty thousand dollars or both, except that the secretary may waive such
208 penalties if, in the secretary's opinion, there appears to be reasonable
209 cause for not having completed or provided the required audit report,
210 provided an official of the municipality, regional school district or
211 audited agency or the auditor submits a written request for such waiver.
212 The secretary may impose any civil penalty assessed pursuant to this
213 section against a municipality, regional school district or audited agency
214 in the form of a reduction in the amount of one or more grants awarded
215 by the secretary, including, but not limited to, any grant payable
216 pursuant to section 12-18b.

This act shall take effect as follows and shall amend the following sections:		
Section 1	July 1, 2024	7-576a
Sec. 2	July 1, 2024	7-576f
Sec. 3	July 1, 2024	7-576i
Sec. 4	July 1, 2024	7-576e(a)(2)
Sec. 5	July 1, 2024	7-393

Statement of Legislative Commissioners:

In Section 2(a)(2)(C)(iii), "5-576j" was changed to "7-576j" for accuracy.

PD *Joint Favorable Subst.*

The following Fiscal Impact Statement and Bill Analysis are prepared for the benefit of the members of the General Assembly, solely for purposes of information, summarization and explanation and do not represent the intent of the General Assembly or either chamber thereof for any purpose. In general, fiscal impacts are based upon a variety of informational sources, including the analyst's professional knowledge. Whenever applicable, agency data is consulted as part of the analysis, however final products do not necessarily reflect an assessment from any specific department.

OFA Fiscal Note

State Impact: None

Municipal Impact: See Below

Explanation

The bill makes various changes to the procedure and criteria for municipal tier designation by the Municipal Accountability Review Board (MARB) or the Municipal Finance Advisory Commission (MFAC). Any fiscal impact to municipalities is dependent on changes to tier designation. Under current law, the Office of Policy and Management (OPM) may distribute money from the Municipal Restructuring Fund to tier II, III, and IV municipalities.

The bill also makes the following changes to municipal auditing requirements; (1) increases from the maximum penalty that OPM can assess on a municipality for missing an audit filing deadline from \$10,000 to \$50,000, (2) allows OPM to assess the penalty as a reduction in one or more grants, and (3) limits the amount of additional time OPM may grant a municipality to file its audit.

This results in a potential cost or revenue loss to municipalities beginning in FY 25 to the extent that a penalty is assessed on a municipality for missing an audit filing deadline.

The Out Years

The annualized ongoing fiscal impact identified above would continue into the future subject to penalties assessed.

OLR Bill Analysis**sHB 5472****AN ACT CONCERNING MUNICIPAL FINANCE AND AUDITS.****SUMMARY**

This bill makes various changes to the Municipal Accountability Review Board (MARB) law, including:

1. changing the procedure for designating municipalities referred by the Office of Policy and Management (OPM) to the Municipal Finance Advisory Commission (MFAC) as tier I municipalities,
2. modifying the criteria and procedure used for determining whether a municipality retains its tier designation,
3. authorizing Municipal Restructuring Fund distributions to be used to pay an arbitrator selected under MARB's existing binding arbitration requirements, and
4. expanding the criteria MARB must use in determining whether to designate a tier III municipality as a tier IV municipality.

The bill also amends the law on municipal audits to, among other things, (1) increase the maximum civil penalty the OPM secretary can assess a municipality, regional school district, audited agency, or auditor that misses the audit filing deadline and (2) allow him to assess the penalty by reducing state grants awarded to the entity.

EFFECTIVE DATE: July 1, 2024

§ 1 — DESIGNATION AS TIER I MUNICIPALITY

The bill gives MFAC discretion to designate a municipality referred to it by OPM as a tier I municipality, rather than automatically

designating these referred municipalities as tier I. Under the bill, MFAC must base its decision on an evaluation of the municipality's financial condition and practices. As under existing law, designated tier I municipalities must prepare and present a five-year financial plan to MFAC for its review and approval.

By law, OPM must refer a municipality to MFAC if it (1) was not referred previously (e.g., because of evidence of unsound or irregular financial practices or specified deficiencies in its audit report) and (2) meets one of several fiscal distress criteria (e.g., if it has a negative fund balance, reported a fund balance percentage of less than 5% in the three immediately preceding fiscal years, or received a bond rating below A).

§ 2 — CONDITIONS FOR RETAINING TIER DESIGNATION

The bill changes the criteria for determining whether a municipality retains its tier designation. Under current law, a municipality in any tier retains its designation (regardless of any positive changes in the factors that led to its designation) until it meets the following four criteria in the fiscal years after its designation:

1. it had no audited general fund operating deficits for two consecutive fiscal years;
2. its bond rating either improved or remained unchanged since its most current designation;
3. it presented, and either MFAC or MARB approved, a financial plan that projects a positive fund balance for the next three fiscal years, with a positive fund balance of at least 5% projected for the third fiscal year; and
4. its audits for these three years have been completed and have no general fund deficit.

The bill eliminates these requirements for tier I municipalities and instead requires that they retain their designation until MFAC unanimously votes to end it based on its evaluation of the municipality's

financial condition and practices.

For tier II, III, and IV municipalities, the bill authorizes MARB to determine whether a municipality must retain its designation, but allows it to do so at its own discretion or at a municipality's request. MARB must do so using the current criteria described above, with the following changes:

1. additionally requires that the municipality have a long-term bond rating from one or more rating agencies that is investment grade or higher,
2. additionally requires (a) each fiscal year of the municipality's approved financial plan be based on recurring revenue and expenses and (b) the plan exclude funding received as contract assistance or from the Municipal Restructuring Fund,
3. requires the audits to report an audited fund balance for the municipality's general fund of at least 5%, and
4. additionally requires that there be no evidence that the municipality has engaged in unsound or irregular financial practices related to commonly accepted municipal finance standards.

Under the bill, if MARB determines that a municipality meets these criteria, the OPM secretary must end the municipality's designation or redesignate it to a lower tier, but not tier I. (This effectively allows MARB to redesignate only tier III and IV municipalities to a lower tier.) The secretary must do this at his discretion and considering the municipality's fiscal condition and state's best interests. Within 60 days after MARB's determination, the OPM secretary must notify the municipality of his decision to redesignate or end the municipality's designation. A municipality must keep its existing designation until it receives this notice. If the secretary does not provide it within the 60-day period, the municipality's tier designation terminates on the next day.

Any tier III or IV municipality redesignated to a lower tier (1) must meet the statutory requirements for that tier and (2) may only ask MARB to determine whether it should be ended after a year has passed.

§ 3 — MUNICIPAL RESTRUCTURING FUND

By law, the Municipal Restructuring Fund provides financial assistance to designated tier II, III, and IV municipalities. To receive assistance, an eligible municipality must submit a plan for approval to the OPM secretary that details the municipality's overall restructuring plan, including the local actions it will take and how it will use the funds.

The bill authorizes (1) the OPM secretary to distribute money from the Municipal Restructuring Fund to a third party on behalf of a designated tier II, III, or IV municipality and (2) these funds to be used to pay an arbitrator selected under MARB's existing binding arbitration requirements.

§ 4 — TIER IV DESIGNATION

The bill expands the criteria MARB must use in determining whether to designate a tier III municipality as a tier IV municipality to include whether there is evidence of unsound or irregular financial practices related to commonly accepted municipal finance standards that MARB believes may materially affect the municipality's financial condition.

As under existing law, MARB may designate a tier III municipality as a tier IV municipality based on its finding that the municipality's fiscal condition warrants it, based on its evaluation of specified criteria (e.g., the municipality's reserve fund balance, liabilities, economic outlook, access to capital, and budget projections for the next five years).

§ 5 — MUNICIPAL AUDITING ACT

By law, municipalities, regional school districts, and other local and regional entities (i.e., audited entities) must have their financial statements and accounts audited by an independent auditor at least once every year and submit the audit reports to various local officials and the OPM secretary. (These audited entities include special taxing

districts, municipal utilities, the Metropolitan District Commission, regional councils of government, and other local entities with more than \$1 million in annual revenues.)

The bill makes the following changes to these auditing requirements:

1. limits the amount of additional time the OPM secretary may grant an audited entity to file its required audit report to six months from the date it was due;
2. increases, from three to five years after the filing date, the length of time auditors must preserve the working papers they used to prepare the audit and make them available to OPM for inspection;
3. increases, from \$10,000 to \$50,000, the maximum civil penalty the OPM secretary can assess an entity or auditor that misses the filing deadline; and
4. allows the secretary to assess the penalty as a reduction in one or more grants he awards to the entity, including a payment in lieu of taxes (PILOT) grant.

Under current law, this civil penalty must be between \$1,000 and \$10,000. By law, unchanged by the bill, the secretary can waive the penalty for reasonable cause if the auditor or an official of the audited entity request it in writing.

BACKGROUND

MARB

MARB is an 11-member board charged with providing technical, financial, and other assistance and oversight to municipalities experiencing fiscal distress. It is composed of state officials and members with business, labor, and municipal government expertise appointed by the governor or legislative leaders. Under the MARB law, distressed municipalities are designated as tier I, II, III, or IV, based on specified factors, including their fund balance, bond rating, equalized

mill rate, and levels of state aid. The higher numbered tiers indicate higher levels of fiscal distress and MARB oversight.

MFAC

MFAC is an eight-member commission that advises the OPM secretary about standards and practices for preparing and submitting audits and that works with any municipality referred to it by OPM to improve its fiscal condition. Its members include the secretary and finance experts, including four municipal executive or fiscal officers.

COMMITTEE ACTION

Planning and Development Committee

Joint Favorable Substitute

Yea 21 Nay 0 (03/22/2024)