



# Stacking tasks, piling risks

Public management letter for Municipalities

June 2012

---

NBA



Nederlandse  
Beroepsorganisatie  
van Accountants



The Royal NIVRA and NOvAA are set to merge, resulting in the establishment of a new organisation, the NBA (Nederlandse Beroepsorganisatie van Accountants - The Netherlands Institute of Chartered Accountants).

The NBA's membership comprises a broad, varied occupational group of over 20,000 professionals working in public accountancy practice, at government agencies, as internal auditors or in organisational management. Integrity, objectivity, professional competence and due care, confidentiality and professional behaviour are fundamental principles for every accountant. The NBA assists accountants in fulfilling their crucial role in society, both today and in the future.

To councillors and boards of Municipalities  
and other interested parties

Postbus 7984  
1008 AD Amsterdam  
Antonio Vivaldistraat 2-8  
1083 HP Amsterdam  
T 020 301 03 01  
nba@nba.nl  
www.nba.nl

Datum                      Onderwerp                      Referentie  
6 June 2012                  PML                                  NBA

Dear Sir/Madam,

The public management letter (PML) *Stacking tasks, piling risks* is a product of the NBA Sharing Knowledge programme. The focus is on municipalities, the most familiar face of government for many citizens. The 415 municipalities constitute an important administrative element in the Netherlands. With a budget of nearly 54 billion euro they make a significant contribution to the realisation of government objectives.

In this PML we set out five signals and recommendations. These are intended for councillors, Municipal Executives, provinces, central government and accountants in the sector. The signals that we would like to highlight are:

1. Stacking tasks, piling risks
2. Land development corporation's losses undermine financial position
3. When collaborating nobody appears to be responsible
4. Digitisation is an island
5. Auditor quality is under pressure

Municipalities' environment is changing rapidly. As part of decentralisation an increasing number of tasks are being transferred to municipalities. The increased workload virtually always goes hand in hand with budget cuts. The worrying position of the land development corporation at many municipalities is giving rise to complications and causing even greater pressure on the financial position.

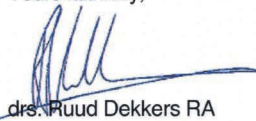
It is not surprising that municipalities are striving for efficiency improvements by collaborating, either with one another or with third parties. This creates a challenge in terms of the allocation of responsibilities. Digitising the operations has become essential, but is still approached too much as a detached issue.

Naturally we also have a message to our members: always go for quality. The climate for accountants has not become easier, which is why quality must always be the benchmark, even amidst the increasing pressure on prices in the tendering for auditing assignments.

This PML is based on the knowledge of our members who work in the sector. Various stakeholders including the Nederlandse Vereniging voor Raadsleden (Raadlid.nu; Netherlands Councillors Association), the Vereniging Nederlandse Gemeenten (VNG; Association of Netherlands Municipalities), the Ministry of the Interior and Kingdom Relations (BZK; Home Office), the Nederlandse Vereniging van Rekenkamers & Rekenkamercommissies (NVRK; Netherlands Association of Audit Offices & Audit Office Committees) and the Commissie Besluit Begroting en Verantwoording (BBV; Budget and Accounts Decree Commission) have given us their comments.

We are grateful to all of them for their contributions.

Yours faithfully,



drs. Ruud Dekkers RA  
Chairman of NIVRA



Leon van den Nieuwenhuijzen RA  
Member of the NBA Identification Board

Nederlandse  
Beroepsorganisatie  
van Accountants



# 00 | Content

Chapter	Page
01 Municipalities: the face of government	5
02 Five signals and recommendations	7
03 The five signals in detail	11
04 Summary of stakeholders' responses	20
Colophon	22

# 01 | Municipalities: the face of government

For the citizen municipalities are the most identifiable face of government. Most contacts that they have with government are through municipalities, right from their birth certificate. Alongside central government and the provinces, municipalities are the third layer of government in the Netherlands. Municipalities also play an important financial role in the economy. They derive their income from the 'gemeentefonds' (municipalities fund) and specific contributions from central government. There are also local taxes and levies, of which the property tax (onroerende zaakbelasting - OZB) is the best known.

As a result of the Administrative Agreements 2011 - 2015 between the Ministry of the Interior, the InterProvinciaal Overleg (Inter-Provincial Consultation - IPO), Unie van Waterschappen (Union of Water Boards) and the VNG, municipalities will be performing an increasing number of central government's tasks. This particularly relates to social tasks. Municipalities have already been performing tasks under the Wet Maatschappelijke Ondersteuning (Social Support Act - WMO) since 2007. With the forthcoming decentralisation of tasks, central government will transfer 6 billion euro per year to the municipalities, provinces and water boards. At the same time, savings of 2 billion euro will be made. These developments make high demands on the flexibility and quality of municipalities' managerial organisation and the local civil service. It requires greater professionalisation of the operations, risk management, collaboration between municipalities and liaison between the various administrative layers. One important social task for municipalities is ensuring sufficient living space and appropriate infrastructure. Many municipalities have opted for an active land development policy in previous years. The favourable economic prospects meant that demand for homes and offices increased. The economic tide has now turned completely, and the construction ambitions have been considerably scaled back. As a result municipalities are left with unsaleable land, whilst the associated financing costs continue. This

constitutes an increased burden on the already restricted municipal budget. Ambitions need to be adjusted.

The economic crisis and cost considerations mean that operations must be performed ever more efficiently. Citizens are also becoming more vocal and are demanding more digital access. Digitisation (ICT) plays an important role in these developments. The municipalities' greatly altered environment requires a reassessment of the financial policy, the exploration of possible scenarios and the constant adjustment of forecasts and long-term budgets. Effective business operations are vital, with sufficient attention for the financial role. The auditor plays a social role in this chain of accountability. He investigates the reliability and rightfulness of the municipality's annual accounts on behalf of the councillors. This is a statutory audit under the supervision of the Autoriteit Financiële Markten (AFM; Netherlands Authority for the Financial Markets). In times of austerity, municipalities are looking carefully at the auditor's costs and the price factor appears to play an important role in tenders. It is important that auditors continue to adopt quality as a benchmark, particularly in a climate where the performance of auditors is under close scrutiny from politicians.

In this public management letter the Nederlandse Beroepsorganisatie van Accountants (NBA; Netherlands Institute of Chartered Accountants) highlights a number of risks at municipalities. The management letter is the product of the NBA's Sharing Knowledge programme. In this programme accountants' collective knowledge is used to identify risks in sectors of society at an early stage. The emphasis is on identifying organisational risks in the areas of finance and administration. The material gathered by the public and government accountants in the sector forms the basis for five signals and recommendations which are summarised below in chapter 02. Chapter 03 discusses the signals in more detail with positive and negative practical examples. Finally chapter 04 summarizes the responses from stakeholders.





# 02 | Five signals and recommendations

## For municipalities

### 1. Stacking tasks, piling risks

There has been a move towards decentralisation within government for several years. This is concisely stated in the Administration Agreements: decentralised where possible, centralised where necessary. The outline of the agreements defines municipalities as the first layer of government, the administrative layer which is closest to the citizen. An increasing number of social tasks are being transferred from central government to the municipalities, a constant increase in workload. New tasks or the expansion of existing tasks often go hand in hand with budget cuts. Whilst the improvement of the operations is still going on, the forecasts need to be re-examined. Not just because of the increased workload, but also because of the continuing economic crisis. Municipalities have to do more with less, the risk profile is growing.

Long-term forecasts and sensitivity analyses are important policy tools, but are adopted insufficiently when there are changes in strategy. This means that the financial position of municipalities is developing in a worrying way. Various supervisory authorities are looking at this, but each from their own perspective.

#### RECOMMENDATION

##### **Increased workload requires administrative guidance**

- Ensure that internal control is ready before the arrival of new tasks or the expansion of existing tasks. If the foundations of the operations are sound, the municipality can perform and control current and new tasks better. There is then sufficient capacity available to respond to changes in good time.
- Get a concrete picture of what risks can arise from the execution of the new or modified tasks and quantify them. This also applies to the division of responsibilities and powers. If there is a budget cut, then also examine how the tasks can be performed more efficiently. Also think about collaboration and prevention measures in order to be able to manage demand.
- Ensure sufficient substantial knowledge about the new or modified tasks, even if they are outsourced to third parties. This knowledge must not only be present at operational level, but also in the area of financial planning and control.
- Match the policy changes and strategic reassessments made in this context to a balanced long-term budget. Maintain an overview at corporate level and do not fragment too much across areas of policy, sectors and services. Apply sensitivity analyses, costing scenarios and forecasts, use external (benchmark) information and be aware of planning optimism and updating old policy. This will make the



long-term forecast a real tool for management and control. Also recognise that the councillors do not like surprises and want to be informed in good time - especially if things are not going well.

- Organise a periodic liaison meeting between the audit office, province and auditor, in order to carry out the supervision of the budgeted and actual financial position of municipalities.

## 2. Land development corporation's losses undermine financial position

Land development was a welcome boost to the budget for many municipalities. The economy and the real estate market were very healthy a few years ago, and the municipalities' planning optimism was virtually limitless. The returns achieved with the land development corporation were used to fund new development plans and particularly items from other policy programmes. The economic crisis completely changed this picture. The decrease in business activity and the decline in consumer confidence meant that demand for homes, commercial premises and offices diminished. Municipalities are left with unsaleable land and are forced to modify building plans. They suffered substantial capital losses. Instead of making a positive contribution to the budget, councils have to allow for interest charges and development costs which can no longer be covered through development. Municipalities must reposition their land development corporations and adapt policy accordingly. In this regard the Budget and Accounts Decree Commission published an amended memorandum on land development in February 2012.

### RECOMMENDATION

#### Manage changes to the plan at every level

- Update the current land portfolio. Determine whether the original level of ambition still matches the demands from the market. The assumptions, valuations and plans must be tested, adjusted and recalculated periodically using scenarios, cash flow adjustments and stress tests. Adjustment can lead to changes in contracts with project developers, a slowdown in the rate at which land is issued, the scrapping of programme elements, the modification of plot sizes and the recalculation of long-term forecasts. The analysis must be carried out at both portfolio level and the level of the individual plans.

- Ensure harmonisation with the province and surrounding municipalities in order to gain insight into the land holdings, planning and the (inter)regional supply and demand for real estate. Hence the total of the number of square metres for the individual municipalities cannot be more than the province's total. This relates to homes, offices and commercial property, in order to identify options for changing zoning and reducing vacancy levels. The public management letter 'Tell it like it is', published for commercial real estate, can serve as a guide.
- Ensure professional management of the land development corporation. The focus must be on risk management. The periodic reporting on the projects must include an up-to-date summary of the most important risks. If risks occur, the consequences must be calculated. Thereby apply a strict timetable.
- Inform councillors in good time and transparently about the assumptions and the effects of changes in the land development corporation's projects. Thereby also provide the impact on the financial position and the resilience paragraph. In an ideal situation the councillors' audit committee will be the body which supervises the municipal land development. The recently amended memorandum on land development from the Budget and Accounts Decree Commission can thereby serve as a starting point.

## 3. When collaborating nobody appears to be responsible

Municipalities are in a constantly changing environment. That is why they are always looking for a more efficient and effective execution of tasks and activities. This particularly applies to smaller municipalities, which have insufficient scale in some policy areas to be able to perform the tasks on their own.

Administrative merger is complicated. The required scale is therefore often sought through collaboration with third parties. These can be other municipalities or the private sector. The collaboration can take various legal and administrative forms, and be temporary or long-term. In practice management and control are often under-scrutinised: if a number of parties are responsible, it frequently appears that nobody has ultimate responsibility. This involves struggling to retain control over one's own policy space, risk management and the financial accounting. Collaboration and outsourcing do not relieve the municipality of its own responsibility and auditing. This demands a new professionalism.



## RECOMMENDATION

### Collaboration requires a new professionalism

- Make clear agreements with the collaborating party and record them. The agreements must enable the municipality to make its own responsibility clear, to be able to continue to bear this responsibility and to have adequate auditing carried out. Ensure that there is sufficient legal expertise and think about the most appropriate form of collaboration. Organise periodic consultation with the collaborating party about progress made on the performance and the financial consequences. Record the agreements made. Remain actively involved by participating in management and/or supervisory roles.
- When putting tasks out to tender ensure that you have sufficient in-house knowledge and sound specifications in which the quality of the service provision is specified. Make sure that the performance of the tasks is safeguarded. Include both knowledge of the subject area as well as procurement expertise in this. Ensure a clear contract, with sound agreements about the auditing of the financial and non-financial information which needs to be included in the municipal council's annual report.
- Carry out a stress test in advance, which includes the guarantees and securities which are provided to third parties in connection with the collaboration or outsourcing. Establish what will happen to the capital and liquidity position if third parties claim guarantees and securities.
- Draw up a governance summary of associated parties and joint ventures and update it regularly. Thereby identify the key points: goal, nature and scale of the financial flows, positions and risks involved, important management and control measures. Include this governance summary in the associated parties paragraph in the annual report.

## 4. Digitisation is an island

Digitisation is playing an ever greater role in society. Citizens and companies are increasingly using the social media and expect the government to do so too. More and more municipalities are investing efforts in developing digital service portals. Such IT projects demand substantial investments and the use of specialist knowledge. The increased use of digital resources also brings risks with it in the area of in-

formation security. Yet many municipalities still view digitisation as an island, a separate entity: a necessary evil for maintaining the internal processes and meeting the needs of citizens and companies.

There is often dependence on suppliers and the responsibility for digitisation is primarily assigned to the ICT role. The link with and intended contribution to productivity and the municipal council's goals is often missing. ICT projects are not well-managed, cost more than expected and do not deliver what was intended. Smaller municipalities have trouble setting up a full ICT role due to the lack of scale and strive for collaboration or outsourcing.

## RECOMMENDATION

### Also ensure digital governance and control

- Embed ICT within the strategic policy and the governance of the municipality. Approach ICT as the backbone of the operations and the basis for service provision and improvements in (labour) productivity. Make a choice to which extent ICT is carried out in-house or is outsourced. Ensure that ICT governance is in order. Thereby think of risk inventory, developing guidelines and procedures, codes of conduct and the incorporation of ICT into the planning and control cycle. If the choice is made to outsource, formalise the agreements by means of a contract (service level agreement) and ensure adequate monitoring during the execution. Final responsibility for ICT must be assigned high up in the organisation. Ensure that ICT is a regular item on the agenda for the Municipal Executive, the audit committee and meeting of councillors.
- Arrange overall project management for ICT projects which looks beyond the project itself and views projects in relation to one another. Pay attention to the interface with existing ICT services. Choose for standard solutions as much as possible and avoid expensive tailor-made systems, but watch out for unnecessary expense. Monitor the execution and ensure regular reports. Inform councillors in good time if there is a risk of additional expenses or a risk of project objectives not being achieved.
- Place information security more prominently on the agenda of the Municipal Executive and the meeting of councillors. It should be part of the ICT governance. Regularly scrutinise security and reliability of ICT systems. Do not hesitate to call in external expertise for this.

- Ensure good liaison between the ICT role and the users within the municipality. Appoint an information manager or assign this role to a special member of staff. Discuss projects within an ICT team of civil servants and work with user panels. On ICT projects with an external impact, such as the design of a digital services portal, it would be a good idea to involve citizens and companies in the evaluation of projects as well, e.g. through a survey.

## For accountants and municipalities

### 5. Auditor quality is under pressure

As a result of economic crisis, the financial position of municipalities is developing in a worrying way. Municipalities are assiduously searching for opportunities to reduce the fixed overheads on their operations, including the costs of the auditor. In times of austerity the price factor appears to be playing an important role in tenders - an attitude which accountancy firms appear to be adopting as well. For municipalities the auditor quality is not clear. They consider the differences in the quality of the audit to be minor.

But here too are grounds for concern, which was also shown by the AFM's 2010 report. A recent letter from Minister Spies about single review concluded that when setting specific contributions one could not automatically rely on the audit. For accountancy firms there is a need to ensure strengthened centrally managed internal quality assurance. Quality must be the benchmark.

Insight into the risks and the quality of the municipal council's operations is essential when awarding contracts. A lack of clarity about this can lead to additional work and therefore additional costs. Disputes about the costs can pose a threat to the quality of the audit. The development of the accountant's cost of audit and advice must be transparent and periodic discussion of the audit activities in the audit committee are important.

## RECOMMENDATION

### Choose quality

- **Accountant:** Adequate knowledge of the municipalities sector is a pre-requisite. The quality of the execution and the internal quality assurance of the work should not be open to debate. When tendering ensure clear insight into the risks and the quality of the operations and ask for more information if necessary. It must be clear what the likelihood is that the actual delivery can take place as agreed. With the tender provide insight to the qualitative and quantitative use of accountancy staff. With regard to the land development corporation, study the amended memorandum on land development from the Budget and Accounts Decree Commission, NBA Praktijkhandreiking 1117 Risk analysis real estate audit (Risicoanalyse accountantscontrole vastgoed) and NBA Audit Alert 23 The contribution of auditors to relevant reporting during the crisis (De bijdrage van accountants aan relevante verslaggeving tijdens de crisis).
- **Municipality:** Maintain a good balance between price and quality aspects. Describe the desired team composition (experience and expertise), the reports to be delivered alongside the auditor's opinion and the number of hours that has been costed for - for example - questions and guidance for the audit or accounts committee. On the other side pay close attention to what is expected of the municipality, particularly whether this is realistically achievable. Include the audit committee and someone in the financial role in the tendering process in order to be able to assess this. Provide the accountant with enough information to be able to submit a good and realistic tender during the tendering process. If the municipality wants to do more work itself in order to reduce accountancy costs, then consider a growth model spread over several years so that the chance of success is greater. In this context draw up a joint handbook (and specifications) for buyers, principals, audit committee and auditors. Be realistic in the detailing of and the number of questions in that handbook.
- **Municipality and legislators:** Ensure improved transparency for councillors about the breakdown of the accountancy costs across audit and advice. It would be a good idea to declare that legally prescribed itemisation of accountancy costs in annual accounts (Civil Code section 2:382a), which is compulsory in other sectors, applies correspondingly to municipalities.



# 03 | The five signals in detail

## **SIGNAL 1: Stacking tasks, piling risks**

*There has been a move towards decentralisation within government for several years. This is concisely stated in the Administration Agreements: decentralised where possible, centralised where necessary. The outline of the agreements defines municipalities as the first layer of government, the administrative layer which is closest to the citizen. An increasing number of social tasks are being transferred from central government to the municipalities, a constant increase in workload. New tasks or the expansion of existing tasks often go hand in hand with budget cuts. Whilst the improvement of the operations is still going on, the forecasts need to be re-examined. Not just because of the increase workload, but also because of the continuing economic crisis. Municipalities have to do more with less, the risk profile is growing.*

*Long-term forecasts and sensitivity analyses are important policy tools, but are adopted insufficiently when there are changes in strategy. This means that the financial position of municipalities is developing in a worrying way. Various supervisory authorities are looking at this, but each from their own perspective.*

### **In further detail**

As a result of decentralisation, more and more of central government's tasks are being transferred to the municipalities: new tasks or expansions of existing tasks, almost

always going hand in hand with budget cuts. Following the WMO (Social Support Act) in 2007, child welfare and the care provision outside healthcare institutions (extramural care) will be added to this in due course. Municipalities are also going to be implementing the Wet Werken naar vermogen (Working According to Ability Act - WWnv), the replacement for the Wet Werk en bijstand (Work and Support Act - WWb). This also has consequences for sheltered workplaces and young disabled people (Wajong - Work and Support for Young Disabled Persons Act). The performance of these tasks makes demands on the flexibility and management of internal processes. Missing knowledge needs to be acquired or bought in from outside. New administrative systems must be set up with the associated planning and control cycle. In addition to this increased workload and budget cuts, municipalities are also suffering from the general worsening of the economic climate. Income is declining, expenditure is rising. The options for increasing the councils' own tax income are limited - in many municipalities the property tax level is already at the permitted maximum. This unavoidably means that there will need to be cuts to social securities, and that policy will need to be modified.

Since the Wet dualiserend gemeentebestuur (Dualisation of Municipal Control Act) the supervisory role of councillors has meant that councillors have also taken more interest in the quality of the operations. Significant progress has been made in this area in recent years. The internal control has not worked well in all cases. Process control is not commonplace in all municipalities. It is often linked too much to the

audit instead of seeing it as the council's own responsibility, with independent accounting by the Municipal Executive to the councillors through an in control management statement. On the other hand it is also sometimes the case that the Municipal Executive explicitly gives an account on the quality of the internal operations in the operations paragraph. Whilst the improvement of the operations has not yet been completed, the forecasts need to be examined again as a result of the accumulation of tasks from central government and the need for cuts as a result of the economic crisis. Municipalities must do more with less. The risks are increasing, particularly on tasks which involve an open-ended programme. Insufficient control of these tasks can lead to financial problems. This can harm the quality of the execution, resulting in political damage and claims.

Municipalities must create an increasingly professional and efficient structure for their basic activities and primary processes, with the citizens and companies as the most important customers. The (financial) management in various policy areas is often not yet properly organised because of the lack of clear frameworks and adequate knowledge. Examples are European tendering and the design of subsidy schemes. In the latter case companies and institutions which work for multiple municipalities can encounter different forms of accountability for the same subsidy scheme. This leads to extra administrative burdens. The question arises as to whether small municipalities have sufficient capacity and quality to deal with the increased workload independently.

Adequate operations start with thinking about strategic choices: what sort of government do we want to be, what can we do ourselves and what scope is there for the private sector. Long-term forecasts and sensitivity analyses are important policy tools. Any change in strategy must be provided with a financial underpinning and be reflected in the forecasts. At many municipalities a lot of fluctuations are found to take place between the original budget, autumn statement, spring statement and the final figure. The factors of time and capacity play an important role. Instead of incorporating the effects of policy changes, the new budget is mainly an update of the existing budget. The idea is then that this will be corrected again in the spring and autumn statement. However, the pitfall lies in the fact that the same problem will occur there. Municipalities are thereby missing out on an important guidance and measurement tool to monitor whether amended policy actually leads to change and has sufficient financial effect.

The province plays a special role in this. As the higher administrative level it is charged with the statutory supervision

of municipal finances. The province strives within a national context to identify potential problems at the earliest possible stage (through the budget). It draws the municipalities' attention to these and works with them to find a solution. Research should be carried out into whether periodic consultation between province, municipality, audit office and auditor, each working in a different phase of the process, can lead to a strengthening of the supervisory chain and the financial position of municipalities.

### Negative example

#### **Problematic restructuring of operations**

Municipality A has overhauled its operations substantially over the past year. This has had a major impact on the tasks and responsibilities of staff, the way in which internal processes are managed and the internal reporting chain. The basis for the restructuring was the inadequate functioning of the operational processes. Standards and guidelines were unclear, the planning and control cycle was not working well and the quality and reliability of the internal reports were insufficient. European tendering was not carried out well, the land development corporation was insufficiently managed and insufficient control was exercised when collaborating with third parties. However, after the restructuring it was found that the new agreements and procedures were not considered to be clear and self-evident. The restructuring was found not to have been fully completed and the organisation was not ready for future new tasks. This meant that additional actions were required which could have been avoided if the change process had been better prepared and managed.

### Positive example

#### **Municipality working with motion on in control management statement**

The following motion from 2007:

“The Council of municipality B, meeting on date [...]

Considering that: the quality of the internal (financial) control is a very important success factor for achieving the plan as expressed by the Council in its budget; [...].



Noting that: the auditor finds that the internal control in year X has worsened by comparison with preceding years; [...]

[...] asks the Municipal Executive:

- To make efforts to produce a management statement with the annual accounts as soon as possible in which the Municipal Executive declares that it is in control;
- To link these efforts to the activities of the administrative taskforce on the control of projects;
- To discuss the plan of action in accordance with the Accounts Committee's recommendation with the Accounts Committee after the summer and then to report on progress once every three months;
- In all future organisational changes to safeguard that the internal control will be of sufficient quality and to inform the Council of the consequences for internal control when proposals are made in this regard;

[...] and passes to the order of the day.”

resulted in the first in control management statement for 2011.

## **SIGNAL 2: Land development corporation's losses undermine financial position**

*Land development was a welcome boost to the budget for many municipalities. The economy and the real estate market were very healthy a few years ago, and the municipalities' planning optimism was virtually limitless. The returns achieved with the land development corporation were used to fund new development plans and particularly items from other policy programmes. The economic crisis completely changed this picture.*

*The decrease in business activity and the decline in consumer confidence meant that demand for homes, commercial premises and offices diminished. Municipalities are left with unsaleable land and are forced to modify their building plans. They suffered substantial capital losses. Instead of making a positive contribution to the budget, councils have to allow for interest charges and development costs which can no longer be covered through development. Municipalities must reposition their land development corporations and adapt their policy accordingly. In this regard the Budget and Accounts Decree Commission published an amended memorandum on land development in February 2012.*

## **In further detail**

Housing has long been one of the municipalities' core tasks. In most municipalities the land development corporation occupies an important position, also in connection with the management of roads, infrastructure and house building. Since the 1990s municipalities were increasingly dealing with project developers who had their own land holdings. As a result the land development corporation shifted from being active to facilitating, whereby all sorts of public-private arrangements were possible. In the extreme case a third party took responsibility for both the land development and the construction. Collaboration with private parties requires specialist knowledge in order to avoid possible losses being borne entirely by the municipality. As long as the prospects are good, there is nothing to worry about. Because the land development corporation generated big returns, the ambitions constantly got bigger and a lot of land was purchased with an eye to the future.

The economic downturn has resulted in a decline in construction, innumerable projects are not going ahead and project developers are also experiencing increasing difficulty in financing new projects. As a result, municipalities are in danger of being stuck with unsaleable land or are being forced to drastically modify their building plans. This can result in the actual value of the land dropping well below the earlier book value, resulting in write-offs and large capital losses. Instead of a positive contribution to the budget, municipalities must allow for interest charges which can no longer be covered through development. Additional cuts and/or increases in taxes are needed alongside the tasks imposed by central government. Out the eight municipalities which have been placed under preventative supervision of the provinces, the land development policy pursued is the main cause at three councils.

According to a letter from the Home Secretary written mid-March 2012, a large number of municipalities are suffering (rising) deficits, but municipalities are working hard to eradicate them. This can lead to cuts in local social securities, increased taxes or the reprioritising and scrapping of (new) policy. The ongoing crisis could result in the deficits on land development rising further, particularly at municipalities which have operated an active land development corporation in the past with the associated risks. That is why a follow-up investigation will be carried out by the provinces in the second half of 2012.

Land development is a complex issue. There is often a long turnaround time and a large number of assumptions. Deviations can have major financial consequences, particularly if there is a delay in completion. The risks are varied, from unexpected archaeological finds to changes to the specifications which are made at the last minute. Everything has often been properly costed at the start, but things go wrong with the control later. The complexity means that it is often difficult for councillors to maintain an overview and correctly assess the effects of changes during the process.

For municipalities with challenging land holdings, losses on the land development corporation and interest charges which are not covered, it will require a lot of effort to maintain a balanced budget over the coming years. Provinces can also have land holdings, which can cause complications. It will be harder to execute and finance new projects. In any case there is a great need for financial expertise and quality with regard to risk management. It starts with a reassessment of the policy. Many municipalities are still wrestling with this - it takes a lot of effort to downgrade ambitions, make choices and clearly identify and accept the financial consequences.

### Negative example

#### Planning optimism has a major negative impact

At the council meeting of municipality C a question was raised about the financial position of the land development corporation. At the start of the year a shortfall of historic proportions was uncovered. A committee was established to investigate the performance of the land development corporation.

This came up with a number of serious findings about those involved:

- there was too much planning optimism, with an excessively positive assessment of risks;
- the municipality bought land on a large scale;
- house building slowed down on land with an agricultural zoning (expansion area);
- warnings about over-programming were not picked up by the Municipal Executive;
- the economic crisis was not so much the cause as the catalyst.

### Positive example

#### The council doing its own development can offer an alternative

Municipality D owned nearly all the land for a construction project. Project developers were only prepared to purchase with an ever higher pre-sale percentage, without guarantees. Because all the risks would be borne by the municipality anyway, the decision was made that the council would develop the land itself. A division was made between land development and property development within the project. Experts were hired on fixed price contracts. In total a residential district with 1,100 homes, a supermarket, a school, a nature park and events site was developed. Specifications were put out to tender at European level. The municipality arranged the pre-sale itself with investors and housing corporations as backstop. Because the profit margin on the property development could be less than for a commercial developer, a buffer was created for the land development. Local estate agents advised the municipality when setting the sale prices. The land issue in the land development went smoothly. One large advantage was that the costs of preparing the land for building were only incurred when the revenues were virtually assured. This meant that the work in progress did not increase. An assessment was made annually of what housing types and plots were most popular, so that supply and demand could be matched. One important factor for the success was the conscious involvement of external expertise in order to ensure that the municipality would remain sufficiently engaged in a complex project. By having a second opinion carried out periodically, wishful thinking and erroneous optimism were avoided. Assumptions and suppositions were regularly examined and adjusted.

#### **SIGNAL 3: When collaborating nobody appears to be responsible**

*Municipalities are in a constantly changing environment. That is why they are always looking for a more efficient and effective execution of tasks and activities. This particularly applies to smaller municipalities, which have insufficient scale in some policy areas to be able to perform the tasks on their own. Administrative merger is complicated. The required scale is therefore often sought through collaboration with third parties. These can be other municipalities or the private sector. The collaboration can take various legal and admini-*



**TE KOOP**



**06 41 24 64 05**  
[www.leukehuizen.nl](http://www.leukehuizen.nl)





strative forms, and be temporary or long-term. In practice management and control are often under-scrutinised: if a number of parties are responsible, it frequently appears that nobody has ultimate responsibility. This involves struggling to retain control over one's own policy space, risk management and the financial accounting. Collaboration and outsourcing do not relieve the municipality of its own responsibility and auditing. This demands a new professionalism.

### In further detail

Collaboration between municipalities is a common occurrence, for example for the WMO (Social Support Act), the WWb (Work and Support Act) and the WWnv (Working According to Ability Act), but also in the area of levying and collecting municipal taxes, payroll processing or parts of the operations. The administration, human resources or even the entire digitisation is outsourced. At smaller municipalities in particular the costs are often not in proportion to the revenues because the scale of the investments is too small. More standardisation in the operations and the information processes can offer a solution. There are municipalities which outsource their entire operations to a shared service centre and thus achieve major cost savings. It even happens that municipalities and water boards combine their separate tax collection in a joint operational organisation. This regional combination of forces can offer many benefits of scale and expertise. But municipalities also collaborate with housing corporations, institutions and private companies in carrying out projects relating to civil and social infrastructure.

One important area for attention is that although these schemes, tasks and projects are carried out with and by third parties, the associated financial streams remain within the municipal council's budget and responsibility. The municipality is and remains responsible for the rightful execution of the schemes and for the rightful and effective spending of the associated funds. In many cases these financial streams are not included separately in the joint venture's budget and accounting. If that is the case, they are often audited in a way which is different from that which is customary at the municipality. This creates risks in the spending, auditing and accountability. Municipalities must identify these risks in advance, adequately confront them and actively monitor them during the execution. Sometimes it goes wrong as early as the tendering, because the municipality has insufficient in-house knowledge or draws up incomplete specifications. In addition to procurement expertise, there is a need for substantial knowledge. Municipalities also pay insufficient

attention to the potential consequences of guarantees and securities provided to third parties.

In selecting the collaboration, control of the administrative (auditing) burdens is an important area for attention. The division of powers is important, particularly when collaborating with private companies. Municipalities sometimes have trouble finding the right arrangement for control and supervision. Adequate and above all timely reporting is essential, in order to ensure that a municipality is not unexpectedly confronted with additional costs.

The increasing level of collaboration and outsourcing of tasks is expressed in municipalities' annual report through the associated parties paragraph.

### Negative example

#### Insufficient monitoring of progress

A collaboration agreement is concluded between municipality E and the private foundation P about a construction project, and a budget is agreed. The municipality provides a financial contribution to the foundation in connection with the construction project to cover the costs, whilst the foundation in turn engages a construction company to supervise the progress of the construction project. The anticipated turnaround time for the project is around eighteen months. During the execution of the project there is little communication between the municipality and the foundation about progress and achievements. In view of the agreement, the municipality believes that everything is well in hand.

At the end of the project the foundation unexpectedly sends the municipality a letter asking for a substantial extra contribution because of project delays. The municipality is caught by surprise by the request and is forced to give an urgent additional assignment to its accountant, who is asked to investigate the legitimacy of the construction costs. Hence the municipality is confronted with double costs: a more expensive construction project and additional accountancy costs in order to identify the cause.

## Positive example

### Adequate supervision framework

Municipality F has decided to outsource tax levying to a new communal body with three other municipalities. They want to enter into the arrangement well-prepared, and carry out an analysis of the strategic, operational and financial risks, including rightfulness and fraud risks, associated with the scheme and the method of implementation. Details of how to prevent and manage them are recorded. The reporting, information, accountability and audit obligations are also recorded. All significant requirements from existing schemes and protocols are listed. A Service Level Agreement (SLA) is concluded with the communal body. A separate risk paragraph contains agreements about the required risk measures.

The municipality has assigned the monitoring of compliance with these agreements to the department with operational responsibility and the sector controller. Both are required to report periodically on the progress and specifics in their management reports. The town treasurer is one of the directors of the communal body. Consideration has been given in advance to a separation of the substantial involvement of the director and the supervising role of the municipality with regard to compliance with the agreements.

An employee of municipality F prepares questions and assesses the answers to these. This arrangement means that the results and performance, their financial consequences and the risks are monitored and that deviations and specifics are identified and reported in good time.

### SIGNAL 4: Digitisation is an island

*Digitisation is playing an ever greater role in society. Citizens and companies are increasingly using the social media and expect the government to do so too. More and more municipalities are investing efforts in developing digital service portals. Such IT projects demand substantial investments and the use of specialist knowledge. The increased use of digital resources also brings risks with it in the area of information security. Yet many municipalities still view digitisation as an island, a separate entity: a necessary evil for maintaining the internal processes and meeting the needs of citizens and companies.*

*There is often dependence on suppliers and the responsibility for digitisation is primarily assigned to the ICT role. The link with and intended contribution to productivity and the municipal council's goals is often missing. ICT projects are not well-managed, cost more than expected and do not deliver what was intended. Smaller municipalities have trouble setting up a full ICT role due to the lack of scale and strive for collaboration or outsourcing.*

### In further detail

All municipalities in the Netherlands are working on digitising their services to citizens and companies. Not just because there is demand for this, but also for cost reasons. The increased workload, budget cuts and the economic crisis mean that operations need to be carried out with ever greater efficiency. However, managing ICT projects and ICT services demands special management skills. The island mentality at many municipalities means that things regularly go wrong. The size of the municipality plays a role in this. Large municipalities generally have sufficient capacity to set up professional ICT departments. Smaller municipalities particularly need to outsource IT to third parties or assign it to a collaboration with other municipalities. Medium-sized municipalities are in between. Having a professional ICT department is, incidentally, no guarantee that things will always go right.

Many municipalities lack an overall vision with regard to digitisation. ICT nowadays is the backbone of the operations and thus the basis for service provision and improvements in (labour) productivity. This should also be embedded in the municipal council's strategic policy and governance, whereby responsibility for ICT is assigned at management level. ICT is often structured operationally with little intervention and feedback from senior management. The controller has an operational responsibility for the quality of the automated processes, but lacks an overall view. As a result, there is a risk that ICT projects are too isolated and are not linked together within an overall policy vision. This creates a patchwork of solutions which need to be connected together using complicated interfaces. Instead of opting for cheap standard solutions, the focus is on tailor-made systems. This gives a greater risk of errors and makes it harder to make changes in the future. Municipalities are also making increasing use of open source software in order to economise as much as possible. There are also experiments with cloud computing whilst the pros and cons of data storage elsewhere have not yet been worked out. This is inadvisable on security grounds.



Information security still occupies too little space on the municipal agenda. Because they are often dealing with privacy-sensitive data, additional attention would be desirable. An annual study of municipalities' digi-services shows that there is still room for improvement in the periodic assessment of the security and reliability of ICT systems.

The communication between the ICT role and the rest of the organisation is also open to improvement at various municipalities. ICT projects are still approached too often from a technical perspective rather than the needs of the users. Solutions are devised which do not match adequately with the operation, whilst the users are unable to communicate their wishes clearly to the ICT department.

### Negative example

#### Incomplete ICT policy

In general it can be stated that the IT at municipality G has been set up to an acceptable level.

Nonetheless, a number of important shortcomings can be identified which need to be improved:

- No use is made of quality targets such as availability, integrity and confidentiality, nor of measuring standards linked to these aspects.
- There is no strategic balance between technology and user needs.
- The management of ICT must be organised in a more systematic and structured way.
- There is a lack of clarity about the issue of security. The municipality is dependent on host provider X, whereby it is not clear for all components who is responsible for what.
- ICT-oriented decision-making prevails too much over the demands from users. This means that ICT is not used effectively for the operations and it is mainly a cost item.

### Positive example

#### Security first

Since 2011 municipality H has been focusing on the issue of security. A detailed information security plan has been drawn up which complies with the ISO 27002 standards. Information security is included in the risk inventory and the plan is evaluated annually. Responsibility for this issue is embedded high up in the municipal management framework. Attention for security is reflected in Municipal Executive decisions.

### SIGNAL 5: Auditor quality is under pressure

*As a result of economic crisis, the financial position of municipalities is developing in a worrying way. Municipalities are assiduously searching for opportunities to reduce the fixed overheads on their operations, including the costs of the auditor. In times of austerity the price factor appears to be playing an important role in tenders - an attitude which accountancy firms appear to be adopting as well. For municipalities the auditor quality is not clear. They consider the differences in the quality of the audit to be minor.*

*But here too are grounds for concern, which was also shown by the AFM's 2010 report. A recent letter from Minister Spies about single review concluded that when setting specific contributions one could not automatically rely on the audit. For accountancy firms there is a need to ensure strengthened centrally managed internal quality assurance. Quality must be the benchmark.*

*Insight into the risks and the quality of the municipal council's operations is essential when awarding contracts. A lack of clarity about this can lead to additional work and therefore additional costs. Disputes about the costs can pose a threat to the quality of the audit. The development of the accountant's cost of audit and advice must be transparent and periodic discussion of the audit activities in the audit committee are important.*

#### In further detail

Accountancy firms sometimes quote the lowest possible price when tendering for auditing the annual accounts of municipalities because the determining factor appears to be price, not quality. This tendency is also manifesting

itself in other sectors. The choice is thereby often made for a tender based on the assumption that the municipality has an adequate administrative organisation, internal control and a strong financial function, which delivers a perfectly prepared annual accounts dossier. Should that turn out not to be the case, the auditor hopes to possibly offset this by means of a bill for additional work. This is important when accepting the assignment and both parties need to have and provide a realistic insight into this.

The councillors are formally responsible for the awarding of the contract, but generally have insufficient insight into the quality of the operations in this regard. This means that councillors find it hard to establish a link to the costs of auditing the annual accounts, and it is difficult to assess invitations to tender and tenders on this point. Municipalities sometimes choose to do extra work themselves in order to reduce the accountant's costs, but often underestimate the amount of effort required for this. Accountancy firms which want to submit a tender are often provided with only limited information about the quality of the organisation. Municipalities then have trouble meeting the assumptions of the selected auditor. After all, many municipalities are still improving their control function. An audit committee can play an important role in this process.

Tendering for audits in the municipalities market at a price which is too low has a double effect. Municipalities expect the audit to be carried out more cheaply, because other municipalities are also managing to reduce the price. On the other hand they are disappointed by the end-cost because the actual costs are often considerably higher due to (unexpected) additional work. It also results in a threat to the quality of the audit that is carried out: in order to still make the assignment profitable, there could be a temptation to stretch the audit boundaries and limit the work done to the absolute minimum. Transparency about the development of the accountancy costs is important for quality in this sector as well. The AFM's report and the finding of central government's annual single review of the audits for the SiSa appendix in the 2010 municipal annual accounts appear to point in this direction. The Home Secretary recently informed the NBA and the Municipal Executives that she is concerned about the available knowledge of the sector and declining quality of the auditing at municipalities and provinces. This also has an undesirable impact on the reputation of the profession. The NBA responded to this at the start of May. Quality must be and remain the benchmark.

## Negative example

### Insufficient auditing of the annual accounts

The following example is based on the AFM's Report of general findings concerning the quality of audit and quality assurance (Rapport algemene bevindingen kwaliteit accountantscontrole en kwaliteitsbewaking) from 2010.

Audit client I is a large municipality. The annual accounts state that the balance sheet item 'stock of building land' is valued at acquisition or production cost. If the market value is lower than the acquisition or production cost, the applicable annual accounts regulations require that the value be written off to this lower market value (a so-called impairment). The market value of the building land which is not being developed is partly dependent on the zoning of the land in question. The auditor's audit dossier contained no records that indicate that the book value of the stock of building land has been assessed against the market value. Nor does the audit dossier contain records which show that the auditor obtained control information about the zoning of the building land which is not being developed.

## Positive example

### Adequate tendering information

The recent invitation to tender from the municipality J included more detailed information on the number of hours that the auditor was expected to spend on the audit. Attention was also paid to the composition of the hours in terms of the level of expertise. This was not confined to the hours of the audit leader and the responsible partner. There was also consideration of the desired audit products. This made it possible for the tendering accountancy firms to submit a realistic tender.

# 04 | Summary of stakeholders' responses

Five stakeholders in the sector were requested to respond to the public management letter and their comments have been included in their entirety in the Dutch PML. What follows is a brief summary:



## **Nederlandse Vereniging voor Raadsleden (Raadslid.nu; Netherlands Councillors Association)**

Raadslid.nu greatly appreciates the PML and sees it as a welcome comprehensive supplement to the reports from the individual auditor. With 5 signals and 5 recommendations the PML provides a salient picture of the current risks which come as no surprise to those familiar with the field. Councillors can make good use of this when defining frameworks and monitoring their own local municipality. The auditor can also draw the PML to the attention of the accounts committee. The final signal relates to the auditor quality which is under pressure, and the role of those involved. The councillors are the principals. Raadslid.nu would like to enter into discussions with the NBA in order to work with those involved to draw up a guide to being a good principal with respect to the municipal auditor with regard to both quality and cost.



## **Vereniging van Nederlandse Gemeenten (VNG; Association of Netherlands Municipalities)**

The VNG has read the PML with interest and feels that the five topics are important, and has discussed them briefly in its response. Municipalities have shown in the past that they can manage big changes well. Freedom of action, adequate resources and preparation time and the expansion of the local taxation domain are important for the current developments, otherwise this can result in tension in the performance. The VNG has long supported the positive example in the PML whereby the Municipal Executive draws up the financial rightfulness statement and the auditor includes this in his auditor's opinion. The legislation needs to be amended in this regard. The VNG shares the concerns with regard to the negative financial development of many municipal land development corporations. The VNG would highlight the pressure from higher levels of government in the past to achieve a high level of housing delivery by securing land as advantageously as possible. The VNG is supporting the importance of collaboration in signal 3 with the 'Slim Samenwerken' ('Smart Collaboration') programme. Defining frameworks, direction and auditing joint arrangements is a challenge for municipalities. VNG opposes consolidated annual accounts in this regard, and is far more in favour of the associated parties paragraph in the annual report. Municipalities have established the Kwaliteits Instituut Nederlandse Gemeenten (KING; Netherlands Municipalities Quality Institute) in order to implement digitisation effectively. It is important that municipalities make clear choices, particularly at a time of ever-shrinking resources. The VNG believes that price-sensitive tendering is not to blame for the fact that the quality of audits is under pressure. Qual-



ity must be the benchmark. That is the basis on which the auditor submits a tender.



**Ministerie van Binnenlandse Zaken en Koninkrijksrelaties**

### **Ministry of the Interior and Kingdom Relations (BZK; Home Office)**

The Ministry appreciates the NBA's initiative to use the knowledge of the members of the professional organisation to prepare the PML. As an autonomous layer of government, municipalities are responsible for their own organisation and operations. The Ministry acknowledges the importance of the signals. In its response the Ministry discusses the signals and the current Ministry measures. It is important that municipalities also anticipate the expansion of their tasks in terms of their operations and thereby make use of the relationships between the decentralisations and the transitional agencies. The current crisis means that municipalities must take steps to absorb the rising deficits with an active land development policy. Municipalities will also have to make a more conscious choice between an active or facilitating land development policy in the future. Central government will be providing municipalities with more tools to implement land development and is a supporter of the collaboration and increased scale which is desired. The PML contains sound recommendations. The responsibility of municipalities remains important. The Ministry has initiated a number of measures in connection with collaboration, including an appropriate division of regions. The Ministry endorses the recommendations with regard to digitisation. Digitisation can form the basis for efficient operations through the use of digital channels with citizens and companies. In order to achieve the e-Government top position, more attention is particularly being paid to the implementation and joint procurement and management. The monitoring of and accountability to councillors for the social effects are very important. The Ministry stresses the importance of auditor quality. The results of single review 2010 are therefore disappointing. It is good that the NBA and accountants have agreed actions.



**Nederlandse Vereniging van Rekenkamers & Rekenkamercommissies (NVRK; Netherlands Association of Audit Offices & Audit Office Committees)**

The PML contains a number of important signals of which municipalities are aware, but they do not always have the time and money available to tackle them quickly and efficiently. Special attention should be paid to the functional collaborations. The question is whether there is sufficient overview and management from senior managers and councillors to be able to fulfil their framework-defining and supervisory role. The pressure on the finances means that the SiSa system and the audit are suffering, with the risk of pressure on quality at municipalities and auditors. In this regard the NVRK would also like to look at the quality of the auditor's reports.



### **Commissie Besluit Begroting en Verantwoording (Commissie BBV; Budget and Accounts Decree Commission)**

The Commission is responsible for the consistent execution and application of the reporting rules and the rightfulness. The response focuses primarily on this. The Budget and Accounts Decree Commission appreciates the efforts of the NBA and its members working in the municipal sector in preparing the PML. The Commission stresses that municipalities must have the audit properly arranged as part of the process management, including in the context of the increased workload. It is therefore of the view that an explicit financial rightfulness statement from the Municipal Executive in the annual accounts is worth investigating. The auditor can include this statement in his auditor's opinion. This reflects the division of managerial responsibility better. The highlighted negative developments in the land development corporations have prompted the Budget and Accounts Decree Commission to clarify the Land Development memorandum (Notitie grondexploitatie). In terms of collaboration, the Commission would point to a clear 'associated parties paragraph' in the annual report. This provides councillors with the requisite transparency. The Budget and Accounts Decree Commission endorses the importance of reliable ICT and the management thereof. The decentralised government bodies could provide good accountability in this regard in the 'operations paragraph'. The Commission is also concerned about the pressure on auditor quality. Municipalities and auditors must take on their share of the responsibility for this. Accountability with regard to the accountancy costs and the analysis of those costs could thereby be beneficial.

# Colophon

## Sharing Knowledge at Municipalities

In this public management letter (PML) the NBA is presenting five signals and recommendations to stakeholders and interested parties in the municipalities. The municipalities are the sixth sector which has been selected by the NBA's Identification Board for the Sharing Knowledge programme. A working group of public and government accountants in the sector gathered anonymised findings and discussed them. This was then discussed at a meeting with stakeholders. The Identification Board then applied a social assessment to the signals. Sector organisations and other stakeholders in the sector were willing to respond in writing to the public management letter. Coordination was provided by the Sharing Knowledge programme team.

## More information

A public management letter is one of the publications from the Sharing Knowledge programme. The NBA previously published public management letters about Insurance (June 2010), Long-term Care (November 2010), Commercial Property (June 2011) and Greenhouse Horticulture (November 2011) as well as an open letter about Pensions (February 2011). All publications are public and are intended for a broad audience.

For more information about the content of this public management letter please contact drs. P.J.J. Vos RA, tel. 0031 20 - 30 10 347 or k.vos@nba.nl.

More information about the Sharing Knowledge programme can be found on the NBA's website.

## Identification Board

prof. dr. mr. F. van der Wel RA (chairman)  
H. Geerlofs AA  
prof. dr. M.N. Hoogendoorn RA  
R.J. van de Kraats RA  
L.A.M. van den Nieuwenhuijzen RA  
Drs. M. A. Scheltema

## Municipalities working group

A. Elsenaar RA RE (Deloitte)  
Drs. A.E. Gerritsma RA (PWC)  
Drs. M.J.A. Koedijk RA RE (ACAM)  
Drs. M.J.G. Mennen RA RE CRISC (RSM)  
Drs. J.K. Poot RA (Baker Tilly Berk)  
Drs. J.L.C. van Sabben RA (KPMG)  
Drs. M.E. Westerhout-van Kimmenade RA MGA (E&Y)

## Sharing Knowledge Programme Team

drs. R.B.M. Mul MPA (chairman)  
M.J.P. Admiraal RA  
drs. I.H. Kramer RC  
drs. P.J.J. Vos RA

## Image material

De Nationale Beeldbank







Nederlandse  
Beroepsorganisatie  
van Accountants

**NBA**

Antonio Vivaldistraat 2 - 8  
1083 HP Amsterdam  
Postbus 7984  
1008 AD Amsterdam

T 020 301 03 01  
F 020 301 03 02  
E [nba@nba.nl](mailto:nba@nba.nl)  
I [www.nba.nl](http://www.nba.nl)