# FINANCIAL POLICY

# GUIDELINES

June 18, 2019


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Adopted on June 18, 2019

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## INTRODUCTION

For decades, the Town of Danvers has enjoyed political and administrative stability, which has translated into sound financial decision-making and long-term planning. The current Town Manager (hired in 2014) is only the fifth to serve in that role since the Danvers Town Manager Act was adopted in 1949, and the Board of Selectmen has enjoyed similar stability over the years. The purpose of this document is to codify the many unwritten best practices as well as the myriad adopted policies that have long guided financial decision-making in Danvers.

The document itself is intended to establish a set of written financial management guidelines, and not the procedures that identify specific methods and actions necessary to carry out these policies. Policies and guidelines are the terms which help guide and direct the town in making financial management decisions. They should be structured with the flexibility necessary to address the complexities of municipal finance that often include unique, unexpected, or extraordinary circumstances. Financial management policies and guidelines are established to support approaches and strategies as they are created or evolve to address ever-changing challenges that face municipalities in the Commonwealth.

Our hope is that this document will (1) provide the public with continued high levels of confidence in their local government's financial decision-making processes and (2) demonstrate to rating agencies and the financial markets that the Town has thoughtfully prepared for its future. These policy guidelines are tools that may be amended by the responsible public bodies, unless otherwise governed by MGL or local by-laws. These policy guidelines are annually reviewed by the Town Manager and designated staff, with recommendations provided, if needed, to the appropriate public bodies.

The framework for this policy guidebook was borrowed from Towns and Cities that took part in the State's Community Compact Best Practices Program. Much of this guidebook is also based on already existing Town policies which can be found on the Town of Danvers website.

### The objectives of the Financial Management Policy Guidelines are as follows:

- To guide the Board of Selectmen, Finance Committee, and Town Manager in making decisions that have significant financial impacts on the Town.
- To set forth planning and operating principles which require that the cost of government be clearly identified, and that financial risk be minimized.
- To maintain reasonable, balanced user fee structures that cover the costs associated with their respective services.
- To regularly evaluate the Town's financial capacity to meet present and future needs.
- To promote credible and sound financial management by providing accurate and timely information on the Town's financial condition to elected officials, staff, the public, and external stakeholders.
- To ensure that current and future capital needs are addressed in a comprehensive and financially sound manner.
- To promote improvement in the Town's credit rating and provide financial resources sufficient to meet the Town's obligations on all municipal debt and other long-term obligations.
- To establish effective internal controls that ensures the fiscal integrity of Town operations.
- To promote cooperation and coordination with other governments and the private sector in the financing and delivery of services.

## 1. GENERAL BUDGETING

**Balanced Budget**

**Background:** Every municipality in the Commonwealth of Massachusetts is required by law to annually produce a balanced budget. The Government Finance Officers Association (GFOA) notes a true structurally balanced budget is one that supports financial sustainability for multiple years into the future.

**Policy Guidelines:** The Town should adopt balanced budgets in which current revenues (recurring) equal or exceed current expenditures. Expenditures should be realistically budgeted and estimated revenues should be conservatively budgeted to allow for unanticipated events. The Town should present assumptions behind revenue estimates along with the balanced budget. The Town will strive to minimize the use of one-time or other nonrecurring revenues to fund ongoing expenditures. The Town should avoid using budgetary procedures that balance the budget at the expense of future years. The Town budget should support a financially sound operating position by maintaining reserves for emergencies and providing sufficient liquidity to pay bills on time, while continuing the long-standing practice of avoiding revenue anticipation borrowing.

**References:**
- *Achieving a Structurally Balanced Budget*, GFOA Best Practice, February 2012
- M.G.L. c.44, §31

**Submission of Budget and Budget Message**

**Background:** Two central principles of public budgeting are transparency and communication. The GFOA considers the preparation of the annual budget document as essential in providing detailed financial information, while also explaining the key issues that the community must address. It is also important to broadly distribute appropriate information to the staff, elected and appointed officials, and the public, in order to give them a greater understanding of the operations, financing, and key issues confronting the community. Thus, the annual budget document can be viewed as the key communication tool produced each year by a municipality.

**Policy Guidelines:** The Board of Selectmen's budget proposal to the Finance Committee will strive to include a financial plan including all general and enterprise funds and activities for the ensuing fiscal year, an accompanying budget message crafted by the Town Manager, and all relevant supporting documents. The budget message should provide context for the proposed budget for all Town departments. It should summarize financial policies for the Town for the ensuing fiscal year, describe the important features of the budget, indicate and explain any major differences in revenues and expenditures from the current fiscal year, summarize the Town's debt position, and include such other material as the Finance Committee deems desirable, or that the Board of Selectmen and Town Meeting may reasonably require.

The Town should work toward the implementation of a budget document that meets the high standards of the GFOA " Distinguished Budget Presentation Award Program."

**References:**
- *Town of Danvers Town Manager Act, Section 32*

## Revenue and Expenditure Forecast

**Background:** A critical step in maintaining a sound financial plan is the preparation of multi-year revenue/expenditure forecasts. Long-term financial planning, including revenue and expenditure assumptions, is one of the financial practices that credit rating agencies evaluate when assessing a municipality's credit worthiness. The Massachusetts Division of Local Services (DLS) states that a financial forecast, or multi-year revenue and expenditure forecast, allows a municipality to evaluate the impact of various government decisions over time. A forecast will provide decision-makers with an indication of the long-term fiscal impact of current policies and budget decisions, and will allow the Town Manager and staff, the Finance Committee, and the Board of Selectmen to test various scenarios and examine the fiscal impact on future budgets.

**Policy Guidelines:** Each year the Finance Director, in consultation with the Town Manager, will work to prepare a five-year Financial Forecast based on current service levels and current funding sources. The Town should strive to incorporate future anticipated Capital Improvement Program expenditures in the forecast.

The forecast should be used as a budget tool to enable Town officials to review operating needs, identify fiscal challenges and opportunities, and develop long-term budgeting policies as part of an overall strategic plan. The forecast may be utilized to examine the ramifications of changes in revenues and expenditures and allow for analyzing multiple scenarios.

As part of the forecasting process, the Finance Director will continue to conduct an annual Financial Summit detailing financial indicators and comparative benchmarks.

**References:**
- *Revenue and Expenditure Forecasting*, MA DLS Best Practice, February 2016
- *Financial Forecasting in the Budget Preparation Process*, GFOA Best Practice, February 2014

## Position Control / Vacancies

**Background:** A large segment of a town's budget is its personnel costs. Failure to accurately monitor the personnel budget can lead to: errors in budgeting, over or under staffing, incorrect grading, and other personnel costs.

**Policy Guidelines:** The Town will maintain a personnel system that accurately tracks authorized, filled, and unfilled positions as well as their funding source. Annual budgets will be prepared in such a way that they account for all costs necessary to cover positions that the Town has budgeted during the fiscal year. Proposed changes to personnel staffing levels should be identified during the budget review process. Proposed increases to personnel levels should be analyzed to ensure that all personnel costs and employee benefits, including pension and insurance liabilities, can be fully identified and calculated for consideration during the budget process.

## Personnel Policies and Labor Contracts

**Background:** The Town has approximately 770 full-time town and school employees and a total of 11 collective bargaining units.

**Policy Guidelines:** Pay plans and rates will be regularly monitored to ensure accuracy and compliance with labor contracts and personnel policies. Contract proposals and agreements will be fully costed out to understand the short and long-term impact on Town finances. To foster transparency in the provision of employment agreements and benefits, the Town will prepare and maintain documents that are publicly available including personnel policies, pay plans, classification plans, memorandums of agreement, collective bargaining agreements and side letters.

**Use of One-Time Revenue**

**Background:** The GFOA recommends that communities develop guidance on the use of one-time revenues to minimize service disruptions due to the non-recurrence of these sources. The DLS states that funding operations with one-time revenues, without identifying future available offsets, effectively postpones difficult decisions necessary to achieve a structurally sound, sustainable spending plan. One-time revenue is usually defined as nonrecurring revenue.

**Policy Guidelines:** The Town should strive to continue its practice of never using free cash to fund the annual Town operating budget. To the extent consistent with Town priorities, one-time revenues should be appropriated to reserve funds, used to fund one-time budget or capital costs, and/or address unfunded liabilities.

## 2. ENTERPRISE FUNDS

**Background:** Enterprise Funds provide a separate accounting and financial reporting mechanism for municipal services for which a fee is charged in exchange for goods and services. Under enterprise accounting, the revenues and expenditures of the service are segregated into a separate fund with its own financial statements, rather than commingled with revenues and expenditures of all other government activities. Enterprise accounting allows a community to demonstrate to the public the total cost of providing a service.

The Town of Danvers has three Enterprise or Business Divisions: Water, Sewer, and Electric. All are overseen by the Town Manager, with rates being set for Water and Sewer by an appointed Water and Sewer Commission, and for Electric by an appointed Municipal Light Board. Budgets for these divisions are approved annually at Town Meeting. Water and Sewer financial policies were codified in 2016, with Electric policies being developed in 2019 based on an independent assessment.

**Policy Guidelines:** Enterprise Funds will be fully supported by the revenue from their rates, fees, and other revenue generating operations. The methodology for calculating indirect costs should be explicitly documented and agreed upon by Finance Director, Town Accountant, Treasurer, and DPW Business Manager. Rates and fees for services will be set at a level to provide for self-supporting enterprise operations, including direct and indirect costs. Capital projects should be financed from enterprise revenues and grants.

Enterprise Funds should be reviewed annually by the responsible parties to project revenues and expenditures for the next fiscal year, as well as retained earnings, in order to prevent the need for subsidy by the General Fund operating budget. Estimates of capital project costs, debt service, and other liabilities should be included in this analysis in order to project future enterprise fund budgets and revenues necessary to maintain self-sufficiency.

**References:**

- M.G.L. c.44, §53F ½
- *Enterprise Funds*, MA Department of Revenue
- *Town of Danvers Town Manager Act, Sections 17 & 22*
- *Town of Danvers Water & Sewer Enterprise Funds – Financial Policies*, June 2016

## 3. RESERVE FUNDS / FUND BALANCES

**Background:** Formal written policies for funding and maintaining reserves can help a community sustain operations during difficult economic periods. Reserves can be used to finance unforeseen or emergency needs, to hold money for specific future purposes, or in limited instances, to serve as a revenue source for the annual budget. Reserve balances can also impact a community's credit rating and, consequently, long-debt costs. The major reserves that credit rating agencies generally focus on are fund balances, free cash, stabilization funds, and special purpose stabilization funds.

The Board of Selectmen approved formal written policies on reserves and fund balances in 2016. These policies formalized long-standing practices of the Town to maintain adequate reserves and fund balances.

### <u>Fund Balances</u>

**Background:** Fund balances are segregated to account for resources that are either not available for expenditure in the future or are legally set aside for a specific future use. The Town implemented GASB Statement No. 54 (GASB 54), *Fund Balance Reporting and Governmental Fund Type Definitions*, which enhances the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying existing governmental fund type definitions.

Town funds are classified in the following categories, which are defined in the glossary: non-spendable, restricted, committed, assigned, and unassigned. Credit rating agencies, such as Moody's and S&P, determine the adequacy of the unassigned fund balance using a complex series of financial evaluations. The size of the fund balance is one of many important considerations in the Town's bond rating.

**Policy Guidelines:** The Town should maintain an unassigned fund balance in the range of 8-12% of the Town's annual operating expenditures. The Town should view a balance of less than 5% to be cause for concern, and work to restore the balance above that level as soon as possible.

Pursuant to Massachusetts General Laws related to establishing reserves, a portion of the unassigned General Fund balance, typically free cash, may be transferred to the Town's General Stabilization Fund. Balances in the General Stabilization Fund are included in the unassigned fund balance and are therefore included in the calculation of the Town's 8-12% goal. It is the goal of the Town to maintain total fund balances, in the aggregate, above 15% of the Town's annual operating expenditures.

**References:**

- *Town of Danvers Fund Balance Policy*, March 2016

**Free Cash**

**Background:** The DLS Municipal Finance Glossary (May 2008) defines Free Cash as remaining, unrestricted funds from operations of the previous fiscal year including unexpended free cash from the prior year, actual receipts in excess of revenue estimates shown on the tax recapitulation sheet, and unspent amounts in budget line items. Unpaid property taxes and certain deficits reduce the amount that can be certified as free cash. Free cash is a component of the Town's overall unassigned fund balance. The calculation of free cash is based on the balance sheet as of June 30, which is submitted by the community's auditor, accountant, or comptroller. Free cash is not available for appropriation until certified by the State.

Free Cash provides a safeguard against events such as a sudden loss of a revenue source, an economic downturn, and an emergency or other unanticipated expenditure. Accumulated free cash can serve as a source to fund key areas such as capital needs and reserves. DLS recommends that a municipality strive to generate free cash in an amount equal to 3-to-5% of its annual budget, less enterprise funds.

The Town codified its free cash policy in 2016, stating that the desirable remaining balance for free cash, after appropriation by Town Meeting, is no less than one percent (1%) of the annual operating budget.

**Policy Guidelines:** The Town will continue it's long-held policy of not utilizing free cash to fund the operating budget and will continue efforts to move other recurring expenses, such as capital and reserve funding, into the operating budget to reduce the reliance on free cash.

The Town will maintain its policy of retaining a free cash balance not less than 1% of the annual operating budget. In addition, any potential usage of excess free cash should be made only after reviewing the state of the Town's unassigned fund balance.

References:

- *Fund Balance Guidelines for the General Fund*, GFOA Best Practice, September 2015
- *Free Cash*, MA DLS Best Practice, February 2016
- *Town of Danvers Reserve Policy*, March 2016

**Stabilization Funds**

**Background:** A stabilization fund allows a Town to maintain a reserve to enhance the Town's fiscal stability. By Massachusetts General Law, it allows a town to set aside monies to be available for future spending purposes, including emergencies or capital expenditures, although it may be appropriated for any lawful purpose. The Town has a General Stabilization Fund as detailed in its Reserve Policy.

A community may establish one or more special purpose stabilization funds and may appropriate into and from them in any year. Generally, a majority vote of town meeting is required to establish, amend the purpose of, or appropriate money into a stabilization fund, and a two-thirds majority vote is required to appropriate money from a stabilization fund. Any interest generated by a stabilization fund must be retained within the fund and become part of the balance. In accordance with MGL Chapter 40, Section SB, the total of all stabilization fund balances should not exceed 10% of a municipality's equalized value (the sum of the valuation of all property in town).

**Policy Guidelines:** The Town should strive to continue to build the General Stabilization Fund to guard against unexpected needs or a downturn in economic conditions. The Town should target an eventual balance of at least 8-10% of the annual operating budget, as is considered a best practice.

The Town will continue to utilize special purpose stabilization funds, such as the School Construction Stabilization Fund, to provide budgetary consistency and solvency over the short and long-term.

**References:**
- M.G.L. c. 40, §5B
- *Special Purpose Stabilization Funds*, MA DLS Best Practice, March 2018
- *Town of Danvers Reserve Policy*, March 2016

## 4. CAPITAL IMPROVEMENT PLAN

**Background:** Planning for and financing the replacement, repair, and acquisition of capital assets is a critical component of any municipality's budget and operations. Prudent planning and funding of capital assets ensures that a municipality can provide quality public services in a financially sustainable manner. A balance must be maintained between operating and capital budgets, so as to meet the needs of both to the maximum extent possible. The development of a Capital Improvement Program (CIP) is the mechanism that a municipality uses to identify projects, prioritize funding, and create a long-term financing plan that can be achieved within the limitations of the budget environment. Long-term capital planning is another one of the important local government financial practices that credit rating agencies evaluate when assessing municipalities for credit worthiness.

**Policy Guidelines:** The Town will continue to annually provide a five-year capital improvement plan as part of the budget document. This plan will be based on input from all Town departments and a thorough review by any relevant stakeholders such as public works and finance.

**As has been the case in recent years, the following principles will guide the development of the CIP:**

- The Finance Director will prepare forms and instructions and coordinate development of the capital improvement budget.
- Future operating costs associated with new capital improvements will be projected and included in operating budget forecasts, as appropriate.
- Capital projects should be prioritized based upon criteria established by the Town Manager.
- Federal, state, or private grants should be used to finance only those capital improvements that are consistent with the Town's capital improvement plan and priorities, and for which operation and maintenance costs have been included in budget forecasts.
- The Town should maintain all assets at a level that is sufficient to protect the Town' s capital investment, and to minimize future maintenance and replacement costs.
- The Town should identify ongoing maintenance needs, preventative maintenance activities, and replacement schedules on an annual basis.
- The Town should develop and project maintenance schedules in consultation with professional and experienced facilities management personnel and/or qualified consultants.
- The Town should project all capital needs for the next five years when developing this CIP. Once established, the projection should be updated each year.

- The estimated costs and potential funding sources for each proposed capital project should be identified before it is submitted to Board of Selectmen and the Finance Committee for Town Meeting appropriation.

**References:**

- *Capital Planning Policies*, GFOA Best Practice, September 2013
- *Capital Improvement Planning Guide*, MA DLS, August 2016

## 5. DEBT MANAGEMENT

**Background:** Debt management is essential to the overall financial planning of any municipality. Borrowing funds and repaying over time allows the Town to finance essential projects that it could not afford to pay from current operating dollars. Long-term financing also spreads the cost across citizens who will be benefitting from the capital investment. It is critical to develop policies and guidelines for the issuance, timing, and tax impact of current and future debt. For those projects supported by user fees, it is important to identify the impact on user rates resulting from debt service costs.

Debt management is guided by the Town's Debt Policy adopted in 2016.

**Policy Guidelines:** The Town will produce a rolling five-year capital improvement program to be included in the annual budget document as described in the Capital Improvement Plan policy guidelines.

**The financing for the program will be based on the following guidelines:**

**Outside Funding:** State, federal, or private grant funding will be pursued and used to finance capital projects whenever possible.
**Pay-As-You-Go:** The first source of Town funding for a capital need should be direct funding, as currently funded through free cash. The Town should strive to incorporate an appropriate amount into the operating budget so that this funding mechanism can be more sustainable.
**Debt Service as % of Operating Budget:** The Town's annual general fund debt service will not exceed 10% of its annual net operating budget. The Town will utilize other revenue sources, such as special purpose stabilization funds or program revenues, in an attempt to keep the operating budget impact below 6%.
**Debt Financing/Borrowing:** If it is determined that the most prudent course is the issuance of debt, the term of the debt must not extend beyond the useful life of the investment. When possible, on a case-by-case basis, efforts should be made to borrow for a reduced term thus saving in interest payments. The structure of the debt (level debt versus equal principal) should be vetted in each instance as well, with a preference for declining debt. Refunding opportunities will be continuously be evaluated by the Treasurer and the Town's Financial Advisor to consider the possibility of future interest cost savings.
**Water, Sewer, and Electric Debt:** The enterprise divisions operate so that all costs (direct, indirect, and debt service) should be covered by division-generated revenues. Projects funded by debt will have a careful review of the timing and impact on user rates. Debt planning and borrowing will be coordinated with all relevant parties. Interdepartmental coordination will help to ensure the identification of financial impacts on borrowing capacity and the overall financial condition of the Town.

**References:**

- *Town of Danvers Debt Policy*, March 2016
- *Town of Danvers Water & Sewer Enterprise Funds – Financial Policies*, June 2016

## 6. GRANT MANAGEMENT GUIDELINES

**Background:** The DLS recommends analyzing the current and future impact of grants on the operating budget, capital improvement program, and debt management. The GFOA recommends that governments establish processes to promote awareness throughout the government that grants normally come with detailed requirements.

**Policy Guidelines:** The Town will ensure that grants are efficiently and appropriately managed by the respective Boards/Commissions/Committees/Departments that receive the grant. Prior to acceptance of a grant award, the Town will identify and consider any special requirements that apply to the general operations of the grant, specific compliance rules, monitoring of other parties that may receive resources, specialized reporting requirements, and any long-term commitments required by the grant, such as the requirement to financially maintain a program or asset after the expiration of the grant. There must also be sufficient staff available to effectively manage the grant, as well as resources identified for any matching requirement, such as cash and/or in-kind services. Effective grant management helps promote the pursuit of grants that are in the Town's best interest and assures timely reimbursements to optimize cash flow, and to guard against year-end account deficits. As a legal contract, every grant agreement must be fulfilled in accordance with its prescribed terms and conditions, as well as applicable federal, state, and local regulations. Failure in this regard exposes the Town to legal and financial liabilities and compromises future grant funding.

No department should expend grant funds until after a fully executed agreement has been completed and notification has been given to all relevant parties, such as the Town Accountant and Treasurer. Further, no grant funds should be used to supplant an existing expense for the purpose of diverting current funds to another use. The Town Accountant is responsible for consulting with departments on grant budgetary matters, accounting for grants in the general ledger, monitoring grant expenditures in excess of revenues, and distributing monthly reports of grant expenditures to departments. The Town Accountant will also maintain a database of all grants and grant activity from inception to closure. The relevant Board/Commission/Committee/Department is responsible for ensuring consistency with award requirements and tracking the timeliness of reimbursement requests.

When positions are funded by grants, the current and future impact on the operating budget should be analyzed. When allowable, the cost for providing benefits, such as health insurance, should be included in the grant budget to cover the Town's cost for providing that benefit.

When grants are accepted for capital purposes, the Town should include in its capital improvement program any share of costs associated with the grant and project the Town's share of debt service in its debt management plan. Any future increase or decrease in operating costs associated with the grant should be identified in the Town's revenue /expenditure forecast.

**References:**

- *Grants Administration*, GFOA Best Practice, May 2013

## 7. ESTABLISHMENT OF FEES AND CHARGES

**Background:** The GFOA recommends that when certain services provided especially benefit a particular group, governments should consider charges and fees on the service recipients. Well-designed charges and fees not only reduce the need for additional revenue sources but promote service efficiency. Regular and consistent review of all fees is necessary to ensure the costs associated with the delivery of specific services have been appropriately identified and that a municipality is collecting reasonable revenue.

The DLS recommends communities adopt written policies for setting charges and fees. A policy should identify what factors are to be taken into account when pricing services. It should also state whether the community intends to recover the full cost of providing the service or benefit and under what circumstances a charge or fee is set at less than full recovery. Such policy and the fee structures should be reviewed periodically to ensure they remain current and should be communicated clearly to the public.

**Policy Guidelines:** Town fees and charges are reviewed periodically by the public bodies that set those fees and charges in relation to the cost of providing those services. The Town will compare rates with nearby communities to determine if the fees established are competitive. The Town may decide against full cost recovery where greater public benefit is demonstrated. Exceptions to full recovery costs include cases where the fee maximums are established by the General Laws of Massachusetts (MGL) or where a policy decision has been made otherwise.

**References:**

- M.G.L. c.140
- Costing Municipal Services: Workbook and Case Study, MA Department of Revenue, September 2017

## 8. UNFUNDED LIABILITIES

**Background:** Defined as "the actuarial calculation of the value of future benefits payable less the net assets of the fund at a given balance date", unfunded liabilities represent a significant financial obligation for all levels of government across the country. In Danvers and other Massachusetts municipalities, the two primary unfunded liabilities are for Pensions and Other Post-Employment Benefits (OPEB).

**<u>Pensions/Retirement</u>**

**Background:** The Mass. Public Pension System is a defined benefit program that is governed by M.G.L., Chapter 32 and is regulated by the Public Employee Retirement Administration Commission (PERAC), the oversite agency of all 105 Massachusetts Retirement Systems. Funding for the Danvers Retirement System covers the costs of employees who meet the eligibility requirements as adopted by the Danvers Retirement Board. Danvers Public School Teachers and School Administrators are not included within the Danvers Retirement System, as their pensions are funded by the Massachusetts Teachers Retirement System. The Town of Danvers, Danvers Housing Authority, and the Town's enterprise/business-type funds consisting of Water, Sewer, and Electric pay an annual appropriation to the Danvers Retirement System.

The Danvers Retirement Board, in partnership with the Municipal Light Board, has established a funding schedule to fully-fund this liability for the Electric Division by 2027; with all others fully-funded by 2035.

- Per state law, the funding schedule is determined through the biennial retirement valuation.
- The valuation is conducted by a qualified independent actuarial firm hired through the Massachusetts public procurement processes and the Danvers Retirement Board with oversite of the procurement process by the compliance unit of PERAC.

**Policy Guideline:** In accordance with state law, PERAC regulation, and government accounting standards, the Danvers Retirement Board, The Town of Danvers, Danvers Housing Authority, and the Town's enterprise/business-type funds, consisting of Water, Sewer, and Electric, will continue to fund this liability in the most fiscally prudent manner, recognizing the fact that the adoption of the funding schedule is, by law, the responsibility of the Danvers Retirement Board.

**Other Post-Employment Benefits**

**Background:** OPEB consists primarily of the costs associated with providing health insurance for retirees and their spouses. The GASB sets reporting standards and requires that accrued liabilities be determined by a qualified actuary using acceptable actuarial methods.

**Policy Guidelines:** While there is currently no legal requirement to fund OPEB, the Town of Danvers has long recognized the importance and financial advantage of initiating early and regular funding for these long-term obligations. To that end, the Town began funding an OPEB account in 2006. In 2016, the Town formally created, and transferred accrued assets into, an OPEB Trust established under MGL c. 32B §20.

- To help determine the appropriate funding schedule, the Town will continue its current practice of having an independent actuary prepare biennial valuations, in compliance with GASB's requirement.
- The valuation is conducted by a qualified independent actuarial firm hired through the Massachusetts public procurement processes by the Town.

**OPEB Funding Strategies:** To address the OPEB liability, decision-makers will annually analyze a variety of funding strategies and subsequently implement them as appropriate with the intention of fully funding the obligation. The Town currently has a funding strategy based on a rolling five-year schedule, increasing each year by $50,000. This funding is a combination of free cash and contributions from Water, Sewer, and Electric. The Town will strive to incorporate the general fund portion within the tax levy in order to make the source more sustainable. Once the Town fully funds its pension obligation in 2035, this funding source will transition to reducing the OPEB liability. In the meantime, the Town will work to more aggressively fund the OPEB Trust in order to reduce the liability and capitalize on what has thus far been very positive market results.

**References:**

- M.G.L. c.32, §20
- *Town of Danvers Reserve Policy*, March 2016

## 9. RISK MANAGEMENT

**Background:** Given local government's almost daily exposure to risk associated with property loss, personal injury, and liability, the GFOA recommends that municipalities develop a comprehensive risk management program that identifies, reduces or minimizes risk to its property, interests, and employees. Costs and consequences of harmful or damaging incidents arising from those risks should be contained.

**Policy Guidelines:** The Town's insurance programs will strive to be aimed at covering the potential impact of the types of property loss, personal injury, and liability the Town is exposed to on a regular basis. The Town should strive to develop and maintain a risk management program to protect against the financial consequences of accidental loss of property, liability, fraud and personal injury to the extent possible through effective prevention and loss control policies and practices.

References:

- *Creating a Comprehensive Risk Management Program*, GFOA Best Practice, March 2009

## 10. ACCOUNTING / AUDITING / FINANCIAL REPORTING

**<u>Annual Audit</u>**

**Background:** The objective of an audit is to obtain independent assurance that a community's year-end financial statements are reliable, accurate, and complete. An audit also helps to ensure that financial checks and balances are in place to protect public assets. Consequently, it can be a powerful tool by which a community can build taxpayer confidence in government operations.

The GFOA recommends a competitive selection process and a rotation of auditors provided there is adequate competition among qualified auditors. Where competition is limited, participation of the current auditors is acceptable, assuming their past performance has been satisfactory and in conformance with industry standards. In the event the Town chooses to remain with an audit firm, it is advisable to rotate the audit manager on a regular basis.

**Policy Guidelines:** The Town will utilize accounting practices that conform to generally accepted accounting principles (GAAP) as set forth by the GASB. The Town will have an independent outside audit performed by a certified public accountant each year. The Board of Selectmen will provide for such an audit by an accountant or a firm of accountants, who have no personal interests, direct or indirect, in the fiscal affairs of the Town government or of any of its officers or employees. The Town will require a Management Letter be provided as part of the independent public accounting firm as a companion document to the annual audit. The Town will either re-advertise for auditing services every five to eight years or ensure that there is a regular rotation of audit managers within a particular firm, if it elects to stay with a given audit firm. The Town begins the annual audit in October and aims to complete the process by mid-December.

**References:**

- *Annual Audits*, MA DLS Best Practice, March 2019

**Annual Financial Report**

**Background:** A Comprehensive Annual Financial Report (CAFR) is a set of Government financial statements comprising the financial report of the municipal entity that complies with the accounting requirements promulgated by the GASB. The GASB provides standards for the content of a CAFR in its annual updated publication *Codification of Government Accounting and Financial Reporting Standards*. A CAFR is compiled by the municipal accounting staff and audited by an external Certified Public Accounting firm utilizing GASB requirements. It is comprised of three sections: Introductory, Financial, and Statistical. It combines the financial information of fund accounting and Enterprise Authorities accounting.

**Policy Guideline:** The Town should continue to work towards the preparation of a CAFR that meets the criteria established by the GFOA's Certificate of Achievement in Financial Reporting Program. This program encourages the preparation of a comprehensive report that goes beyond the annual audit report and presents information that enhances government transparency and disclosure. The Town has received the award annually since 2004.

**Monthly Reporting**

**Background:** Monthly reporting helps a community to determine whether sufficient funds are available to cover current obligations, any surplus can be invested, or if a shortfall exists that may require temporary borrowing. It enables the Town to take prompt management action if fiscal problems are indicated or to adjust spending behavior in order to meet financial challenges.

**Policy Guideline:** The Accounting Department will produce and distribute, to department heads, monthly budget-to-actual reports. If financial problems are indicated, the Finance Director and Town Accountant will review with the Town Manager at the line item level.

**Cash Collections**

**Background:** One of a government's functions is to collect taxes and other revenues. The process involves many actors, including the Treasurer/Collector's office, Accounting, Assessing, Legal, other departments or agencies, other governments at the state and/or local level, commercial banks, and, in some jurisdictions, private collection agencies.

**Policy Guidelines:** The Town should collect all revenue using fair and consistent methods, exercising all powers provided by law. On or before June 30th, the Town should strive to commence tax title proceedings against all properties that owe property taxes for the prior fiscal year to the Town.

The Treasurer/Collector will establish and maintain reliable record keeping systems and enforce a timely collections process. All amounts committed must be supported with a warrant and a detailed listing of all amounts due. All monies received shall be turned over to the Treasurer/Collector's office, at a minimum weekly, so they may be deposited in the bank in a timely manner.

The Treasurer/Collector will pursue the collection of delinquent accounts and with assistance from the Deputy Collector and other Town officials to pursue collection of outstanding real estate taxes, personal property taxes, excise taxes, and fines. The execution of a systematic and deliberate program to collect taxes owed is intended not only to capture revenue, but also to establish a clear policy that tax delinquents will be aggressively pursued. The Treasurer/Collector should execute in a timely manner collection remedies such as issuance of demands immediately after bills become past due and initiate tax taking shortly afterwards to increase the rate of collection of municipal monies, thereby assisting in the financial stability of the Town.

**References:**

- M.G.L. c.60
- *Revenue Collection*, GFOA Best Practice

**Reconciling Cash and Receivables**

**Background:** Two of the largest assets for a community are cash and receivables. Information pertaining to these is kept by the Treasurer/Collector and the Town Accountant. A Treasurer is the custodian of the community's revenues, tax titles, and tax possessions, while a Collector keeps listings of outstanding receivables due to the community. The Town Accountant is responsible for maintaining the accounting records. Prompt and frequent reconciliations between these offices are essential in order to maintain control and ensure checks and balances are in place.

**Policy Guidelines:** Within thirty days after the end of each month, the Treasurer/Collector should internally reconcile the cashbook to all bank statements, and the Treasurer/Collector should internally reconcile all receivable balances with the receivable control. The results of these activities should be forwarded to the Accountant's office and compared to the general ledger records. If differences are determined, the Treasurer/Collector and Accountant will immediately reconcile any variances, such as missing information, errors, and timing differences. The Town should reconcile revenues and expenditures for each fiscal year within one to two months of the end of the fiscal year.

**References:**

- *Reconciling Cash and Receivables*, MA DLS Best Practice, February 2016

**Cash Flow Forecasting and Budgeting**

**Background:** The purpose of cash flow forecasting is to determine whether adequate funds are available to cover current obligations, invest any available surplus, or, if any cash shortfall exists, determine the need for temporary borrowing.

The DLS recommends maintaining a cash flow budget to forecast investment opportunities or borrowing needs. Major revenue sources, like property taxes and state aid, are generally received in large, lump sums at specific points in the fiscal year and do not necessary coincide with expense patterns, which often results in cash surpluses or shortfalls during certain periods of the year. The GFOA also recommends cash flow forecasting as a best practice. When used as a cash management guide, it can lead to the optimized use of funds as well as insure sufficient liquidity.

**Policy Guideline:** The Treasurer/Collector will maintain a detailed monthly cash flow document which combined with historical data going back several years will assist the Treasurer/Collector in identifying possible investment opportunities during the Fiscal Year and beyond.

**References:**

- *Use of Cash Flow Forecasts in Treasury Operations*, GFOA Best Practice, February 2011

## 11. PROCUREMENT AND PURCHASING

**Background:** The Commonwealth of Massachusetts establishes municipal purchasing regulations under M.G.L. Chapter 30B, 149, 30 Section 39M. The State Inspector General's office has oversight of public purchasing laws and has published a comprehensive guide to procurement requirements.

**Policy Guideline:** The Town will follow the guidance contained in the Inspector General's "The Chapter 30B Manual: Procuring Supplies, Services and Real Property" and "Designing and Constructing Public Facilities Manual" in order to comply with the requirements of M.G.L. Chapter 30B, 149, and 30 Section 39M. To supplement this guidance, the Town's Purchasing Agent will maintain a concise manual on purchasing procedures for department heads or others involved in Town purchasing or procurement.

**References:**

- *Town of Danvers Procurement Policies and Procedures*
- *Chapter 30B Manual*, MA Office of the Inspector General
- *Designing and Constructing Public Facilities Manual*, MA Office of the Inspector General

## 12. TREASURER INVESTMENT POLICIES

**Investment**

**Background:** A local government's investment policy establishes guidelines and responsibilities in accordance with state law for managing and investing municipal funds. The GASB recommends the disclosure of key policies affecting cash deposits and other long-term investments to ensure they are managed prudently or are not subject to extraordinary risks. When assessing municipalities for credit quality, rating agencies look for investment management policies that address selection of financial institutions for services and transactions, risk assessment, investment objectives, investment maturities and volatility, portfolio diversification, safekeeping and custody, and investment performance reporting, benchmarking, and disclosure.

The Town has a long-standing Treasurer's Policy on Banking and Investment.

**Policy Guidelines:** The Treasurer/Collector is responsible for developing and maintaining the policies for investing Town funds and will make all decisions regarding their management. The Treasurer/Collector will invest Town funds in a manner that meets daily operating cash flow requirements and conforms to state statutes governing public funds, while adhering to generally accepted diversification, collateralization, and the prudent investment principles of safety, liquidity, and yield. The Treasurer/Collector will also regularly monitor statutory changes governing investments and offer any policy amendments. The Treasurer/Collector will submit a report of investments on a regular basis to the Town Manager and Board of Selectmen.

References:

- M.G.L. Ch. 40, §5; M.G.L. Ch. 44, §54, §SSA, §558; and M.G.L. c. 448, §7
- *Town of Danvers Policy on Banking and General Fund Investments*

**Post-Issuance Tax Compliance**

**Background:** Post-issuance compliance procedures are designed to provide for the effective management of a municipality's post bond or note issuance compliance program for tax-exempt and other tax-benefited bonds in a manner consistent with state and federal laws applicable to such obligations.

**Policy Guideline:** The Treasurer/Collector should review post-issuance compliance procedures annually and implement revisions as deemed appropriate in consultation with bond counsel and Financial Advisor.

## APPENDIX: GLOSSARY OF TERMS

**Available Funds:** Balances in the various fund types that represent non-recurring revenue sources. As a matter of sound practice, they are frequently appropriated to meet unforeseen expenses, for capital expenditures or other onetime costs. Examples of available funds include free cash, stabilization funds, overlay surplus, water surplus, and enterprise net assets unrestricted (formerly retained earnings).

**Betterments** *("Special* Assessments"): Whenever part of a community benefits from a public improvement, or betterment *(e. g.,* water, sewer, sidewalks, etc.), special property taxes may be assessed to the property owners of that area to reimburse the governmental entity for all, or part, of the costs it incurred in completing the project. Each property parcel receiving the benefit is assessed a proportionate share of the cost which may be paid in full, or apportioned over a period of up to 20 years. In this case, one year's apportionment along with one year's committed interest computed from October 1 to October 1 is added to the tax bill until the betterment is paid.

**Block Grant:** A Block Grant is a Federal grant of money awarded by formula under very general guidelines that allow grantees broad latitude in spending activities. Recipients are normally state or local governments.

**Bond:** a means to raise money through the issuance of debt. A bond issuer/borrower promises in writing to repay a specified sum of money, alternately referred to as face value, par value or bond principal, to the buyer of the bond on a specified future date (maturity date), together with periodic interest at a specified rate. The term of a bond is always greater than one year.

**Bond and Interest Schedule Record** *("Bond Register"):* The permanent and complete record maintained by a treasurer for each bond issue. It shows the amount of interest and principal coming due each date and all other pertinent information concerning the bond issue.

**Bond Anticipation Note** ("BAN"): Short-term debt instrument used to generate cash for initial project costs and with the expectation that the debt will be replaced later by permanent bonding. Typically issued for a term of less than one year, BANs may be re-issued for up to five years, provided principal repayment begins after two years (MGL Ch. 44§17). Principal payments on school related BANs may be deferred up to seven years (increased in 2002 from five years) if the community has an approved project on the Massachusetts School Building Authority (MSBA) priority list. BANs are full faith and credit obligations.

**Bond Authorization:** The action of town meeting or a city council authorizing the executive branch to raise money through the sale of bonds in a specific amount and for a specific purpose. Once authorized, issuance is by the treasurer upon the signature of the mayor, or selectmen. (See Bond Issue)

***Bond Buyer.*** A daily trade paper containing current and historical information of interest to the municipal bond business.

**Bond Counsel:** An attorney or law firm engaged to review and submit an opinion on the legal aspects of a municipal bond or note issue.

**Bond Issue:** The actual sale of the entire, or a portion of, the bond amount authorized by town meeting.

**Bond Rating** (Municipal): A credit rating assigned to a municipality to help investors assess the future ability, legal obligation, and willingness of the municipality (bond issuer) to make timely debt service payments. Stated otherwise, a rating helps prospective investors determine the level of risk associated with a given fixed-income investment. Rating agencies, such as Moody's and Standard and Poor's, use rating systems, which designate a letter or a combination of letters and numerals where AAA is the highest rating and C1 is a very low rating.

**Bonds Authorized and Unissued:** Balance of a bond authorization not yet sold. Upon completion or abandonment of a project, any remaining balance of authorized and unissued bonds may not be used for other purposes, but must be rescinded by town meeting or the city council to be removed from community's books.

**Capital Assets:** All tangible property used in the operation of government, which is not easily converted into cash, and has an initial useful live extending beyond a single financial reporting period. Capital assets include land and land improvements; infrastructure such as roads, bridges, water and sewer lines; easements; buildings and building improvements; vehicles, machinery and equipment. Communities typically define capital assets in terms of a minimum useful life and a minimum initial cost. (See Fixed Asset)

**Capital Budget:** An appropriation or spending plan that uses borrowing or direct outlay for capital or fixed asset improvements. Among other information, a capital budget should identify the method of financing each recommended expenditure, i.e., tax levy, and identify those items that were not recommended. (See Capital Asset, Fixed Asset)

**Capital Improvements Program:** A blueprint for planning a community's capital expenditures that comprises an annual capital budget and a five-year capital program. It coordinates community planning, fiscal capacity and physical development. While all of the community's needs should be identified in the program, there is a set of criteria that prioritizes the expenditures.

**Capital Outlay:** The exchange of one asset (cash) for another (capital asset), with no ultimate effect on net assets. Also known as "pay as you go," it is the appropriation and use of available cash to fund a capital improvement, as opposed to incurring debt to cover the cost.

**Capital Outlay Expenditure Exclusion**: A temporary increase in the tax levy to fund a capital project or make a capital acquisition. Exclusions require two-thirds vote of the selectmen or city council (sometimes with the mayor's approval) and a majority vote in a community-wide referendum. The exclusion is added to the tax levy only during the year in which the project is being funded and may increase the tax levy above the levy ceiling

**Chapter 90 Highway Funds:** State funds derived from periodic transportation bond authorizations and apportioned to communities for highway projects based on a formula under the provisions of MGL Ch. 90 §34. The Chapter 90 formula comprises three variables: local road mileage (58.33 percent) as certified by the Massachusetts Highway Department (MHD), local employment level (20.83 percent) derived the Department of Employment and Training (DET), and population estimates (20.83 percent) from the US Census Bureau. Local highway projects are approved in advance. Later, on the submission of certified expenditure reports to MHD, communities receive cost reimbursements to the limit of the grant.

**Contingent Appropriation**: An appropriation that authorizes spending for a particular purpose only if subsequently approved in a voter referendum. Under MGL Ch. 59 §21C (m), towns may make appropriations from the tax levy, available funds or borrowing, contingent upon the subsequent passage of a Proposition *2 1/2* override or exclusion question for the same purpose. If initially approved at an annual town meeting, voter approval of the contingent appropriation must occur by September 15. Otherwise, the referendum vote must occur within 90 days after the town meeting dissolves. The question may be placed before the voters at more than one election, but if not approved by the applicable deadline, the appropriation is null and void. If contingent appropriations are funded through property taxes, DOR cannot approve the tax rate until the related override or exclusion question is resolved or the deadline passes, whichever occurs first.

**Debt Authorization:** Formal approval by a two- thirds vote of town meeting or city council to incur debt, in accordance with procedures stated in MGL Ch. 44 §§1, 2, 3, 4a, 6-15.

**Debt Burden:** The amount of debt carried by an issuer usually expressed as a measure of value (i.e., debt as a percentage of assessed value, debt per capita, etc.). Sometimes debt burden refers to debt service costs as a percentage of the total annual budget.

**Debt Exclusion:** An action taken by a community through a referendum vote to raise the funds necessary to pay debt service costs for a particular project from the property tax levy, but outside the limits under Proposition *2 1/2.* By approving a debt exclusion, a community calculates its annual levy limit under Proposition *2 1/2,* then adds the excluded debt service cost. The amount is added to the levy limit for the life of the debt only and may increase the levy above the levy ceiling.

**Debt Limit:** The maximum amount of debt that a municipality may authorize for qualified purposes under state law. Under MGL Ch. 44 §10, debt limits are set at 5 percent of EQV. By petition to the Municipal Finance Oversight Board, cities and towns can receive approval to increase their debt limit to 1O percent of EQV.

**Debt Policy:** Part of an overall capital financing policy that provides evidence of a commitment to meet infrastructure needs through a planned program of future financing. Debt policies should be submitted to elected officials for consideration and approval.

**Debt Service:** The repayment cost, usually stated in annual terms and based on an amortization schedule, of the principal and interest on any particular bond issue.

**Enterprise Fund:** An enterprise fund, authorized by MGL Ch. 44 §53F1/2, is a separate accounting and financial reporting mechanism for municipal services for which a fee is charged in exchange for goods or services. It allows a community to demonstrate to the public the portion of total costs of a service that is recovered through user charges and the portion that is subsidized by the tax levy, if any. With an enterprise fund, all costs of service delivery—direct, indirect, and capital costs--are identified. This allows the community to recover total service costs through user fees if it chooses. Enterprise accounting also enables communities to reserve the "surplus" or net assets unrestricted generated by the operation of the enterprise rather than closing it out to the general fund at year-end. Services that may be treated as enterprises include, but are not limited to, water, sewer, hospital, and airport services. See DOR IGROB-101

**Free Cash** (Also *"Budgetary Fund Balance"):* Remaining, unrestricted funds from operations of the previous fiscal year including unexpended free cash from the previous year, actual receipts in excess of revenue estimates shown on the tax recapitulation sheet, and unspent amounts in budget line-items. Unpaid property taxes and certain deficits reduce the amount that can be certified as free cash. The calculation of free cash is based on the balance sheet as of June 30, which is submitted by the community's auditor, accountant or comptroller. Important: free cash is not available for appropriation until certified by the Director of Accounts.

**General Obligation Bonds:** Bonds issued by a municipality for purposes allowed by statute that are backed by the full faith and credit of its taxing authority.

**Levy Limit:** A levy limit is one of two types of levy (tax) restrictions imposed by MGL Ch. 59 §21C (Proposition 2 1/2.). It states that the real and personal property taxes imposed by a city or town may only grow each year by 2 1/2 percent of the prior year's levy limit, plus new growth and any overrides or exclusions. The levy limit can exceed the levy ceiling only if the community passes a capital expenditure exclusion, debt exclusion, or special exclusion. (See Levy Ceiling)

**Massachusetts School Building Authority** ("MSBA"): Administers the state program that reimburses cities, towns, and regional school districts varying percentages of their school construction costs depending on the wealth of the community or district and the category of reimbursement. Projects that received their first reimbursement payment prior to July 26, 2004 will continue to get annual state payments to offset the related annual debt service. Thereafter, cities, towns, and regional school districts will receive a lump sum amount representing the state's share of the eligible project costs... (See DOR IGR 06-101)

**New Growth:** The additional tax revenue generated by new construction, renovations and other increases in the property tax base during a calendar year. It does not include value increases caused by normal market forces or by revaluations.

**Non-Recurring Revenue Source:** A one-time source of money available to a city or town. By its nature, a non-recurring revenue source cannot be relied upon in future years. Therefore, such funds should not be used for operating or other expenses that continue from year-to-year (See Recurring Revenue Source)

**Principal:** The face amount of a bond, exclusive of accrued interest.

**Receipts Reserved for Appropriation:** Proceeds that are earmarked by law and placed in separate accounts for appropriation for particular purposes. For example, parking meter proceeds may be appropriated to offset certain expenses for parking meters and the regulation of parking and other traffic activities.

**Sale of Cemetery Lots Fund:** A fund established to account for proceeds of the sale of cemetery lots. The proceeds may only be appropriated to pay for the cost of the land, its care and improvement or the enlargement of the cemetery under provisions of MGL Ch. 114 §15.

**Sale of Real Estate Fund: A** fund established to account for the proceeds of the sale of municipal real estate other than proceeds acquired through tax title foreclosure. MGL Ch. 44 §63 states that such proceeds shall be applied first to the retirement of debt on the property sold. In the absence of such debt, funds may generally be used for purposes for which the city or town is authorized to borrow for a period of five years or more.

**Short-Term Debt:** Outstanding balance, at any given time, on amounts borrowed with a maturity date of

12 months or less.

**Special Exclusion:** For a few limited capital purposes, a community may exceed its levy limit or levy ceiling without voter approval. Presently, there are two special expenditure exclusions: 1) water and sewer project debt service costs which reduce the water and sewer rates by the same amount; and 2) a program to assist homeowners to repair or replace faulty septic systems, remove underground fuel storage tanks, or remove dangerous levels of lead paint to meet public health and safety code requirements. In the second special exclusion, homeowners repay the municipality for the cost plus interest apportioned over a period of time, not to exceed 20 years.

**Special Revenue Fund:** Funds, established by statute only, containing revenues that are earmarked for and restricted to expenditures for specific purposes. Special revenue funds include receipts reserved for appropriation, revolving funds, grants from governmental entities, and gifts from private individuals or organizations.

**Stabilization Fund: A** fund designed to accumulate amounts for capital and other future spending purposes, although it may be appropriated for any lawful purpose (MGL Ch. 40 §58). Communities may establish one or more stabilization funds for different purposes and may appropriate into them in any year an amount not to exceed ten percent of the prior year's tax levy. Any interest shall be added to and become a part of the funds. A two-thirds vote of town meeting or city council is required to establish, amend the purpose of, or appropriate money from a stabilization fund. A majority vote of town meeting is required to appropriate money into a stabilization fund.