



*Massachusetts*  
*Collectors and Treasurers*  
*Association*

# **TREASURER'S MANUAL**

Revised 2017

# Chapter 1

## Overview and Legal Basis of Municipal Finance in Massachusetts

### Legal Foundation of Municipal Finance

The development of the powers and duties of Massachusetts cities and towns has evolved since colonial times. The Massachusetts General Laws set out the legal foundation of municipal finance, but new statutes, court decisions, agency regulations, and guidelines are constantly changing. Knowledge of where to find the statutes and regulations, and keeping up with changes is of great importance for all treasurers. More detail can be found on the Division of Local Services publication “A Guide to Financial Management for Town Officials” [www.mass.gov/dor/docs/dls/publ/misc/town.pdf](http://www.mass.gov/dor/docs/dls/publ/misc/town.pdf).

### Sources of Legal Information

The Division of Local Services (DLS) of the State Department of Revenue (DOR) has statutory responsibilities regarding the assessment and collection of property and other local taxes, municipal budgets and debt, and municipal accounting and other financial practices. The Bureau of Municipal Finance Law serves as the legal bureau of the DLS and is available to municipal treasurers for legal advice and assistance. (See Bulletin 2006-02B titled Bureau of Municipal Finance Law online at [www.mass.gov/dls](http://www.mass.gov/dls).) Treasurers can call to speak to one of the assigned “attorneys of the day” at 617-626-2400 or email a question to [DLSLAW@dor.state.ma.us](mailto:DLSLAW@dor.state.ma.us). In an email request, a treasurer needs to include name, community, position, telephone number, and best time to reach you in case follow up is needed.

The DLS has a website ([www.mass.gov/dls](http://www.mass.gov/dls)) which is invaluable to municipal treasurers looking for legal information pertinent to their jobs. There are quick links from the DLS home page to a local officials directory, bulletins on new laws, regulations, procedures, and seminars and workshops being offered by the DLS, Informational Guideline Releases (IGR’s) which explain new laws and related regulations, copies of the newsletter, “City and Town”, copies of the Cherry Sheet which gives information regarding the state budget, state aid and assessments to individual municipalities, and other important information. Treasurers should subscribe to the online service for these important publications as they are no longer mailed to local officials. This can be done online or by contacting the DLS at 617-626-2353. There is no charge for this online service. (See DLS Bulletin 2003-09B titled Dissemination of DLS Information by Email online.)

Each year, one of the DLS bulletins contains a summary of the prior year’s changes in municipal finance law. These bulletins are available at the DLS website quick links, cited above. Copies of the General Laws and Session Laws are available at the State

House Bookstore, located in Room 116 of the State House, or at [www.malegislature.gov](http://www.malegislature.gov).

The DLS has also published a volume entitled “Laws Relating to Municipal Finance and Taxation”, which provides municipal officials with most of the statutes relative to city and town government. Multiple copies are mailed to each municipality when the volume is updated –usually every three years. Contact the DLS legal department if there is not a volume in your office.

The DOR website ([www.mass.gov/DOR](http://www.mass.gov/DOR)) has a number of publications which may be helpful to treasurers. They may be downloaded or saved to one’s computer. Among the titles are the following: Bureau of Accounts State House Note Program Forms; Cherry Sheet Manual; Developing a Capital Improvement Program: A manual for Massachusetts communities; Guide to Financial Management for Town Officials; Technical Assistance—A brochure detailing the DLS financial management assistance/consulting available to Massachusetts local governments.

State law may also be researched by using the website, [www.malegislature.gov](http://www.malegislature.gov). Current legislation and adopted statutes are available at this site.

### **Massachusetts Collectors and Treasurers Association (MCTA) Website**

The website of the MCTA, [www.masscta.com](http://www.masscta.com), has links to many other important websites including the following:

- Department of Revenue
- Division of Local Services
- Ethics Commission
- Legislation, including pending laws, hearings, description of gov’t
- State and Local Employers
- State Treasurer
- Social Security
- Mass Division of Employment and Training
- Public Records Division
- Registry of Deeds (Secretary of State)

MCTA’s website also has the address, telephone number, and email address of the Association, which is available to all members for aid and assistance. In 2017, they were as follows: address: 510 King Street, Littleton, MA 01460; telephone: (978) 952-6644; fax: (978) 952-6655; email: [MassCTA@gmail.com](mailto:MassCTA@gmail.com)

### **Proposition 2½**

An example of a far reaching statute affecting the municipalities of the Commonwealth was an initiative petition resulting in a statewide referendum termed Proposition 2½ (Ch.

59 §21C) which was passed by the voters in 1980. It limits the amount of money a community can levy, i.e., raise through real and personal property taxes. At the DOR

website ([www.mass.gov/DOR](http://www.mass.gov/DOR)), there is a list of publications, including two very helpful bulletins on Proposition 2 ½ , titled Levy Limits: A Primer on Proposition 2 ½ and Proposition 2 ½ Ballot Questions, Requirements, and Procedures.

Proposition 2 ½ provided for two, distinct limitations. First, a community cannot levy more than 2.5 percent of the total full and fair cash value of all taxable real and personal property in the community. This constraint is generally called the community's "levy ceiling." Second, a community's levy can only increase by a prescribed amount, discussed below, from year to year. This second constraint is generally called the community's "levy limit."

Proposition 2½ directs the Department of Revenue to annually adjust each community's levy limit by applying two statutory increases: (1) an automatic increase of 2.5 percent over the prior fiscal year's levy, and (2) a "new growth" increase, based on the value of new construction in the community, including additions to and alterations of real property, that did not result from property revaluation.

Proposition 2½ also provides communities with local procedures whereby they can increase their tax levies above their levy limits. These procedures require voter approval at a referendum election. They include overrides, on the one hand, and debt exclusions and capital outlay exclusions, on the other. An override increases a community's levy limit for the current fiscal year and becomes part of the base for calculating future years' levy limits. Exclusions provide communities with a means to raise additional taxes to fund capital projects. Unlike overrides, though, exclusions do not become part of the tax base; therefore, they do not result in permanent increases in the tax levy.

Furthermore, specific statutory provisions allow special exclusions, permitting communities, for certain limited capital purposes, to assess taxes above the levy limit or ceiling. The amount of a special exclusion is only added to the levy limit or ceiling for a temporary period of time, and does not become part of the base upon which the levy limit is calculated for future years. One such special debt exclusion permits a community to add water and sewer project debt service costs to its levy limit or levy ceiling for the life of the debt, as long as it reduces water and sewer rates by the same amount. Another special exclusion permits a community to assist homeowners to repair or replace faulty septic systems, remove underground fuel storage tanks or remove dangerous levels of lead paint in order to meet public health and safety code requirements.

Proposition 2½ also permits communities, by referendum vote, to reduce their levy limits by passing an underride. An underride reduces the base upon which levy limits are calculated for future years, thereby resulting in a permanent decrease in the levy limit of a community.

## **Municipal Powers and Duties**

With its enactment in 1966 of the Home Rule Amendment to the Massachusetts Constitution (Article 89 as reported in Article 2 of the Articles of Amendment), the

Legislature granted broad home rule powers to both cities and towns. Pursuant to the Home Rule Amendment, municipalities may now exercise any power or function that the Legislature has the power to confer, through the adoption, amendment, or repeal of local ordinances or bylaws. The Home Rule Amendment contains important exceptions and qualifiers, which limit the legislative power of cities and towns. These are set out in Article II §7, which states:

Nothing in this article shall be deemed to grant to any city or town the power to (1) regulate elections other than those prescribed by sections three and four; (2) to levy, assess and collect taxes; (3) to borrow money or pledge the credit of the city or town; (4) to dispose of park land; (5) to enact private or civil law governing civil relationships except as an incident to an exercise of an independent municipal power; or (6) to define and provide for the punishment of a felony or to impose imprisonment as a punishment for any violation of law.

Furthermore, the Home-Rule Amendment prohibits a municipality from exercising any power that is (a) denied to it by its own charter, or (b) reserved to the state under the Constitution. Also, the exercise of a municipality's powers must be consistent both with the Constitution and with all general and special laws enacted by the Legislature.

The Legislature has conferred upon cities and towns the power or duty to:

1. Acquire any land, easement, or right on the territory within its boundaries for any public purpose. (40:14) The acquisition may be made by the means of an outright purchase, by an eminent domain taking, by gift, or by tax title. (60:64-69)
2. Sue or be sued. A municipality may be a party to litigation and appear either as a plaintiff or a defendant in Massachusetts courts and in the courts of any other state. (40:2)
3. Contract for goods, materials, or services in the exercise of their corporate powers.
4. Appropriate or set aside funds for any particular purpose. As a general rule, no municipal department may incur a liability in excess of an appropriation. (44:31) It follows that a city or town department may not ordinarily enter into a contract without first obtaining a sufficient appropriation.
5. Assess and collect taxes on real and personal property situated within their respective boundaries. They may collect a motor vehicle excise, assessed to owners for the privilege of registration, as well as certain license and user fees.
6. Impose a local option excise tax upon the transient rental of rooms in hotels, motels, and lodging houses. (64G: 3A;.) They may impose a similar local option excise upon jet aircraft fuel (64J). Another local option excise tax may be accepted for meals tax (64L:2)
7. Incur debt by borrowing for specified purposes within specified debt limits and time periods. Such debt, once authorized, may be issued using notes (generally short-term) or bonds (long-term). (44:4, 6A, 7, 8)

8. Adequately provide for the education of school-age children. Municipalities must ensure a sufficient number of schools to teach all children who legally wish to attend. In those municipalities that have at least 500 families, a high school will generally have to be staffed, maintained, and equipped.
9. Exercise police powers for the preservation of the public peace, order, health, morality, and welfare. (See McQuillan, *Municipal Corporations*, §24.01, pp. 417-419. 3rd ed., 1980.) Police powers may be exercised utilizing a variety of methods, including the enactment of regulations, ordinances and bylaws and the issuance of licenses and permits.

Local governments have the right to elect a Charter Commission which is charged with drafting a Home Rule Charter. After its adoption by the voters in a general election, a Home Rule Charter gives a community the right to make many changes in its governmental structure, such as adding a town or city manager position to take on functions formerly held by the Selectmen or Mayor. The Town Manager/Administrator may be the Chief Executive Officer, Chief Financial Officer, Chief Administrative Officer, and/or Chief Procurement Officer. A Home Rule Charter can be used to change elected boards or commissions to appointed bodies, change elected officials to appointed officials, and assign new functions to various positions or boards, committees, and commissions.

## **The Structure of City Government**

### **Mayor and City Council**

The mayor generally serves as the chief executive officer in a city. However, the extent of the power and responsibility of the mayor differs widely from city to city, depending on the specific form of government adopted by a particular city. For example, under a Plan A form of government, mayors serve as full-time administrators with extensive power; conversely, under a Plan E form of government, mayors serve as ceremonial heads and possess little more authority than a city councilor.

A city council or board of aldermen possesses legislative authority, pursuant to Ch. 43 §72, to enact ordinances and adopt resolutions; however, their actions frequently require the concurrence of the mayor in order to take effect. The council is the appropriating body of a city, but it can ordinarily act only to accept, reduce or reject outright the recommended appropriations submitted by the mayor. The council cannot increase those recommendations. (44:32)

Notwithstanding, the city council, on the recommendation of the school committee, may, by a 2/3 vote, increase the appropriation for the school budget or the regional school district assessment over the amount requested by the mayor. However, any increase under this provision does not permit the city to exceed its Proposition 2½ levy limit.

The mayor has 120 days to submit the annual budget to the council. The council can act on its own initiative if the mayor does not act within the 120-day period. (IGR 86-202, pp. 1-19 through 1-20) The council may also enact municipal ordinances; such ordinances,

however, may have to be approved by the mayor, either under provisions of the General Laws, such as Ch. 43 §125, or by terms of the city charter. The acceptance and revocation of acceptance of local option legislation is likewise the prerogative of the city council, with the mayor's approval where required by charter or other provisions of law. (4:4, 4A, 4B)

## **The Structure of Town Government**

### **Selectmen (41:20-23C)**

The selectmen serve as a town's chief executive body. They have overall responsibility for the general operations of town government. They constitute the primary, non-school appointing authority for a town. In addition, the selectmen may enter into contracts on behalf of the municipality.

Generally, the board contains three or five members. In the smallest towns, the board of selectmen may supervise almost all town operations. In larger towns, however, the board primarily develops administrative policies and leaves general administration to a professional manager.

The selectmen's responsibilities are very broad. They sort out the various positions of different departments and boards to determine the best overall course of action for the town.

They coordinate the roles of all players in the financial management process and promote a team approach for addressing the fiscal issues of the town. Selectmen should participate in the budget process, directly reviewing budget requests and having input at all levels of the process. They should provide leadership in the development of a capital improvement program and a risk management policy (i.e. insurance). Throughout the fiscal year, the selectmen (in conjunction with the finance committee), should monitor the financial performance of the town. Finally, selectmen should assume an active role in any issue or policy that has broad implication for the financial condition of the town, including such issues as tax classification, free cash policy, use of stabilization fund, financial reporting and the audit process.

Selectmen possess responsibility for the appointment and supervision of town employees, but they may delegate this authority. Selectmen are required to set the amounts of the performance bonds for those municipal officers required to be bonded, provided that these amounts are not less than the amounts established by the Commissioner of Revenue. In addition, no bills chargeable to the appropriations of a town can be paid unless they are drawn upon a warrant prepared by the accountant and approved by a majority of the selectmen. (41:56) This authority can be delegated to a Town Manager/Administrator. No bonds or notes may be issued by a town unless they have been signed by a majority of the members of the board. (44:16) All town property not expressly under the control of some other officer or board is under the authority of the selectmen. (40:3) The selectmen also serve as a town's licensing board. [See Randall and Franklin, 18 Massachusetts Practice § 135 (4th ed.).]

The selectmen have the sole power to place a Proposition 2½ override or exclusion question on the ballot for voter consideration. Override or exclusion questions may not be placed on the ballot by vote of town meeting or through use of a local initiative process. Unless a local initiative process is provided by law, the selectmen also have the sole power to place an override question on the ballot.

(If a local initiative process is available in a community, the people, as well as the selectmen, may place an override question on the ballot by using the initiative process.)

## **Town Meeting**

Town meeting possesses the legislative authority of a town. A town meeting may only be called pursuant to a warrant, a document that notifies the inhabitants of the time, place and subject matter of the meeting. The warrant is normally issued by the selectmen; however, the voters of a town may petition a meeting. (39:10) Each town must hold an annual town meeting in February, March, April, or May. (39:9) Town meeting may be delayed by a vote of the selectmen, but all business must be completed on or before June 30<sup>th</sup>. That portion of the town meeting providing for the election or certification of officers and ballot questions may not be delayed. (See IGR 86-202 in the Addendum for more information.) A town may also hold as many additional special town meetings as necessary to consider and conduct town business. Town meetings are open, with all registered voters eligible to participate, unless a community has adopted a representative town meeting form of government pursuant to Ch. 43A §2.

Town meeting is responsible for all appropriations (40:5) and for the enactment of all bylaws. (43B: 13) It acts on behalf of the town to accept local option statutes, unless a statute specifies another mode of acceptance. (4:4) Town meeting may authorize the selectmen to sell town land (40:3) or to act as water and sewer commissioners, assessors, etc. (41:21) The town meeting also decides whether to establish certain town boards (such as trust fund commissioners under 41:45).

## **Other Municipal Officers**

### **Assessors**

The General Laws provide for one, three, five, seven, or nine assessors to serve in each city and for one, three, or five to serve in each town. Assessors may be elected or appointed; the mode of selection depends on provisions of the local charter or bylaw. (41:24)

An assessor's term in office continues for one or more years. Under no circumstances may an assessor serve as a tax collector or deputy tax collector (41:24) The Commissioner of Revenue serves in a general supervisory and oversight capacity over municipal assessors. (58:1-7)

Massachusetts cities and towns finance themselves with an "ad valorem" [\[2\]](#) property tax system, under which each taxpayer contributes toward the maintenance of municipal government an amount in proportion to the value of his or her property.



The duties of the board of assessors include (a) assigning value to real and personal property, utilizing state-authorized mass appraisal techniques, for the purposes of apportioning the property tax, (b) ensuring that these values correlate with full and fair cash value standards and (c) complying with the Commissioner of Revenue's recertification requirements of property valuation every three years.

Assessors must maintain information concerning each parcel of property in the community. This information is typically recorded on property record cards. This information includes the area of the parcel, a description of any structures located there, including their quality and condition, the address of the property and/or its owner, and details about the deed or probate record of ownership of the parcel.

Assessors must exercise particular care in obtaining accurate, legal identification of property ownership since effective collection and enforcement of taxes levied on property depend on that correctness.

Other responsibilities of the assessors include:

1. Reviewing and responding to taxpayer abatement and exemption applications. (59:5 & 59)

Assessors have the authority to grant abatements and exemptions to taxpayers. A taxpayer who feels his or her property has been overvalued or disproportionately assessed may file an application for abatement. If the assessors agree with the taxpayer, they may grant an abatement, and the taxpayer will receive a reduction in the amount of the tax owed. Taxpayers unhappy with a decision of the assessors may appeal that decision to the Appellate Tax Board (ATB).

Exemption from taxation is a statutory privilege conferred on various categories of persons or property. Some of the most frequent recipients of exemptions are religious or charitable organizations, disabled veterans, elderly persons, surviving spouses and blind persons.

All abatements and exemptions are funded from an account called the overlay reserve for abatements and exemptions. The assessors annually establish the amount to set aside in this special account prior to setting the tax rate. This amount should correspond with their estimation of the aggregate of:

- (a) abatement and exemption costs expected for the year and
- (b) property taxes anticipated not to be collected that year. The Department of Revenue must authorize this amount as part of the tax rate approval process. (59:23)

2. Determining actual tax rates, which must comply with Proposition 2½ and result in an assessment sufficient to finance the budget. The tax rate approval is usually delegated to the Director of Accounts. The approval is the legal basis for the Assessors to commit the taxes to the Collector, which is required for the Collector to issue tax bills. (59:23)
3. Preparing a tax list and warrant in a form approved by the Commissioner of Revenue. (59:54)

4. Committing the tax list and warrant to the tax collector and, in a community with one or more tax-levying districts, committing a separate tax list and warrant to each district. (59:53)
5. Applying to the Department of Revenue for the “new construction” adjustment to the levy limit under Proposition 2½. (59:21C(f))

Assessors must establish and maintain public trust and confidence in the valuation process. They can expand that trust and confidence by being ever sensitive to their accessibility by taxpayers.

The property tax is usually the largest revenue source of a municipality. Hence, the assessors, with their key responsibility in overseeing real and personal property valuations, play a crucial role in the financial wellbeing of the community. Any delay or error in the valuation or tax billing process may result in the necessity of borrowing, with related costs, or in a misallocation of the tax burden. Interest costs divert funds the town could otherwise spend on goods and services. Moreover, late tax bills result in a significant decrease in investment earnings since they delay the deposit of revenues in interest-bearing bank accounts. Lastly, errors in assessed ownership preclude collection enforcement and add additional cost outlays for legal fees, particularly costs for title examinations, renunciations, re-takings and advertising.

## **Collectors**

Municipalities may adopt charter provisions or enact ordinances or bylaws relating to the appointment and term of office of the tax collector. In the absence of such local regulations, however, a town must elect one or more collectors for a term of one or more years. (41:1) The collector must annually obtain a performance bond, in an amount set by the selectmen, but not less than the minimum amount established by the Commissioner of Revenue. (60:13)

The collector’s primary function entails the collection of taxes, motor vehicle excises, betterments and special assessments in accordance with the commitment list and warrant prepared by the assessors. In a community that accepts Ch. 41 §38A, the tax collector has the further responsibility to collect some or all other monies due to the municipality, such as water and sewer, utility, trash, user fees and charges for certain permits and licenses.

The General Laws detail the manner in which the collector is to proceed in enforcing the collection of all committed taxes. Upon receiving the tax list or commitment and warrant from the assessors, the collector must send a tax bill to each assessed property owner. The bill must be in a form approved by the Commissioner of Revenue. An Affidavit of Mailing should be notarized to provide prima face evidence that the bills were mailed on a certain date. Once a week, or more often, the collector must pay over to the treasurer all money received from the payment of taxes and interest during the preceding week (or lesser period). (60:2)

A tax collector must establish and maintain an effective and reliable record-keeping system. All money received should be deposited as quickly as is reasonably possible.

If payment is not received by the collector within the statutory period, a demand for payment must be sent to the taxpayer before collection enforcement procedures may be initiated. Such collection enforcement procedures include:

1. A collector may issue a warrant to a deputy collector requiring him to collect the unpaid taxes (real estate, personal property, motor vehicle, ...)
2. The perfection of a tax taking for real estate taxes only. A tax taking perfects the lien that arises automatically upon the commitment of a tax on real estate. Upon the taking, title vests in the city or town, subject to the taxpayer's right of redemption or until such time as that right has been foreclosed. (60:53-57)
3. The institution of a civil suit. Collectors generally resort to this procedure, when a tax taking cannot be made. (60:35) A suit must be brought within six years of the due date of the tax.

Tax collectors should work aggressively to collect all bills committed to them. Clearly, uncollected revenues may substantially impact a town's financial position in an unfavorable manner.

### **City Auditors/Town Accountants**

In cities, the charter generally sets out procedures for the appointment of the city auditor. In towns that have established the position of town accountant, the office of town auditor may be abolished. Town accountants cannot hold any office that involves the receipt or disbursement of money, except for the office of town clerk. (41:55)

A critical responsibility of the city auditor (41:52) and the town accountant (41:56) relates to the payment of bills and payrolls, which must be examined for legality and the requisite oaths and approvals. Should any claim be deemed fraudulent, unlawful, or excessive, payment authorization may be withheld. In such instances, a statement must be filed with the city or town treasurer, outlining the reasons for the refusal. Alternatively, if all is in order, the auditor or accountant must draw a warrant upon the treasury for payment.

The town accountant must maintain (a) a complete set of municipal books, including each specific appropriation, with the amounts and purposes of each expenditure from each appropriation (b) a detailed record of the town debt, including borrowing purposes, rates of interest, due dates, and payment provisions and (c) all town contracts. (41:57) In cities, the city clerk maintains municipal contracts. (41:17)

The town accountant must inform town officers at regular intervals of unexpended balances in their appropriations. (41:58) Immediately upon the close of the calendar year, the accountant must prepare statements detailing the preceding fiscal year's appropriations and expenditures, appropriations for the current fiscal year, and expenditures incurred during its first six months, as well as estimated expenditures for the second six months and estimates for the ensuing fiscal year. By August 1<sup>st</sup>, the city auditor, town accountant, or treasurer must furnish the assessors with a written report of the money received, other than from taxes,

loans, and trust funds, for the preceding fiscal year. (41:54A)

### **Town Auditors**

The powers of town auditors are more limited than those of town accountants or city auditors. They have a purely auditing function, rather than an auditing and control function, examining transactions after the fact rather than approving or disapproving them as they occur.

Town auditors cannot disallow the payment of bills as illegal, fraudulent, or excessive; also, town auditors possess no role in the budgetary process comparable to the accountant's role under Ch. 41 §§59-60. The principal duty of town auditors is to examine the books of all town officers and boards that handle money or have charge of appropriations. Town auditors must file an annual report of the result of their audit, verify cash balances, and reconcile bank balances. They must also audit certain public trusts and certify annually the source and total of town receipts other than taxes, loans, and trust income. A town may have several town auditors.

### **City and Town Clerks**

A city or town clerk possesses as an essential function the maintenance of the official records of the municipality. Because clerks receive money for such functions as issuing licenses and certifying copies of official documents, they must obtain an annual performance bond, in an amount set by the mayor or selectmen, but not less than the minimum amount established by the Commissioner of Revenue. (41:13, 13A)

Clerks record town meeting votes, administer oaths of office, and keep an index of those instruments entered in the clerk's office that are required by law to be recorded (e.g., records of births and deaths, business names, and security agreements between private parties). (41:15)

Clerks must also keep a record of all appropriations and certify them to the auditor or accountant, if any, otherwise to the treasurer, as well as to the assessors for use in setting the tax rate. City clerks must certify appropriations to the treasurer in any case. The certification must give details of the appropriations, identifying the provisions the appropriating authority made for funding the expenditure, if specified in the appropriation order or vote. (41:15A)

Whenever a city, town, or district votes to authorize the use of debt, the city, town, or district clerk must furnish a copy of the vote to the Director of the Bureau of Accounts within 48 hours after the vote becomes effective. (44:28)

All contracts made by a city officer on behalf of the city must be filed with the city clerk as well as with the city auditor. Such contracts are public records and must be indexed. (41:17)

Additional duties of the clerk include:

- Notifying the secretary of state of local acceptance of statutes. (4:5)
- Supervising the state census, if appointed to do so by the mayor or

selectmen. (9:7)

- Making regulations concerning (a) the handling of ballot boxes and (b) the counting and returning of votes. (50:7)
- Acting as custodian of the municipality's public records. (66:6,7)

## **Finance Committee**

Every town with an equalized valuation exceeding one million dollars must, and any other town may, legislate the mandatory election or appointment of a finance committee (also called an advisory, appropriation, or prudential committee). The terms of committee members may not exceed three years, although the size and composition of its membership may vary.

In all cases, the finance committee has the responsibility to consider all municipal finance questions for the purpose of making a report to town meeting. Furthermore, unless a provision of a town's bylaw gives the responsibility to the selectmen, the finance committee must present a budget at the annual town meeting. Even if that ultimate responsibility lies with the selectmen, the finance committee possesses an important role in budget preparation. The committee should review estimates provided by the various municipal departments and formulate them into spending recommendations for inclusion in the town meeting warrant.

Furthermore, the finance committee has the power to approve transfers from the reserve fund, a contingency fund usually appropriated as part of the annual budget, to departmental budgets for extraordinary or unforeseen occurrences. (40:6)

The finance committee is the official fiscal watchdog for a town. Finance committees were established to permit a representative group of taxpayers to conduct a thorough review of municipal finance questions on behalf of all citizens.

## **Districts**

A district is an area comprising all or a portion of one or more municipalities, having fixed borders, and organized for the purpose of carrying out some governmental function, such as providing fire protection, water, education, electricity, common sewers, water pollution abatement or refuse disposal. In Massachusetts, districts fall into one of two basic types, either tax-levying districts, which levy taxes directly upon individual citizens and taxpayers, or assessment districts, which assess charges and costs upon cities and towns, either directly or through the Cherry Sheet. Fire and water districts generally levy taxes directly. Regional school and regional transportation districts, on the other hand, generally assess member cities and towns, either directly, as in the case of regional schools, or through the Cherry Sheet, as in the case of regional transportation authorities.

Tax-levying districts ordinarily rely upon the assessors and collectors of the municipality or municipalities in which they are located to assess and collect district taxes and other charges. Both tax-levying and assessment districts generally have their own treasurer to handle and manage district funds.

## **District Treasurers**

Treasurers of tax-levying districts possess the essential powers and duties of town treasurers, holding responsibility for the custody, management, and investment of district funds. (44:53, 55) Nothing in the General Laws, however, explicitly makes all provisions pertaining to city and town treasurers applicable to district treasurers. Therefore, unless a district's enabling legislation otherwise provides, the district treasurer may not, for example, appoint an assistant treasurer since Ch. 41 §39A, which authorizes such appointments in cities and towns, fails to mention districts. Similarly, the statutory authorization for city and town treasurers to make deductions for employees' deferred compensation and individual retirement accounts (44:67, 67A) does not extend to district treasurers. Conversely, Ch. 41 §121 expressly makes district treasurers subject to the bonding requirements and the exculpatory provisions relating to a loss of certain investments set out for municipal treasurers by Ch. 41 §35 and Ch. 44 §55A, respectively.

The sections in Ch. 44 relating to temporary and long-term borrowing are as applicable to districts as they are to towns. The Ch. 44 provisions relating to revenue and grant anticipation notes can be found in §§4 and 6A, and information on the issuance and form of notes and bonds, in §§16-20; state house notes are discussed in §§23-28.

Districts possess the authority of cities and towns to incur long-term debt (44:7, 8), but only if they are authorized by law to spend money for the purposes for which the debt is to be incurred. (44:9) A district's enabling act generally sets out the purposes for which the district may expend money.

## **Optional Forms of Municipal Administration**

A community that desires to establish a consolidated department of municipal finance may do so by accepting the provisions of Ch. 43C §11. Such a consolidated department may include the offices of assessors, collector, accountant, auditor or comptroller, and treasurer.

The consolidated municipal finance department must have an appointed director serving ex officio as the accountant, auditor, comptroller, treasurer, collector or treasurer/collector of the community. The bylaw or ordinance must specify the scope and structure of the department. All other personnel necessary to staff the department must be appointed by the director, subject to approval by the selectman or mayor, unless some other provision is made in the municipal charter.

Chapter 43C also permits a municipality to establish two other consolidated departments, one consolidating persons and departments involved in community development activities, and the other consolidating those performing municipal inspections.

## **(Role of) Department Heads**

A department head's ultimate role or mission is to strive to provide to the community the highest level of service possible from the available resources of the municipal budget. Usually, department heads prepare their own individual budgets. These budgets must be created within the broad framework and guidelines of the charter and the rules or

procedures established by the finance committee, selectmen, and/or manager. Department heads should participate actively in the budget review process. Following budget approval, department heads have direct legal obligations to spend within the allocated amount of their respective budgets.

Department heads also should play a major role in their respective municipality's capital planning process by identifying the capital needs of their particular departments. In addition, they should carefully provide for proper care and maintenance of capital items under their control, endeavoring to extend the useful life of those items as much as possible.

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<sup>[1]</sup>160 Mass 102

<sup>[2]</sup>L. ad valorem means according to the value

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## **Chapter 2**

# **Duties and Responsibilities of the Treasurer**

### **Overview**

- The main functions of the municipal treasurer are prescribed in various chapters and sections of State Law. As described in Chapter 1 of this manual, and in the Appendix, treasurers have many resources to research these laws. The main areas of the treasurer's responsibility have separate chapters in this manual devoted solely to these topics. They are: Chapter 5: Tax Title (60:50,54,61,62,63,76,77,79,80)
- Chapter 6: Trust Funds (44:53A)
- Chapter 7: Payroll and Employee Benefits (149:178B)
- Chapter 8: Retirement (Ch 32)
- Chapter 9: Borrowing and Debt Service (44:4,6,6A,7,8)

Chapter 11: Cash management (41:35) and Investment of Municipal Funds (44:54-55A & B; 29:38A) The remaining chapters provide detail concerning the execution of these main treasurer's duties and responsibilities as follows:

- Chapter 1: Legal Basis for and Overview of Municipal Finance in Massachusetts
- Chapter 3: Operations of the Treasurer's Office
- Chapter 4: Reconciliation of Cash
- Chapter 10: Financing Capital Improvements
- Chapter 12: Procuring Banking Services

### **Responsibilities of and Functions Carried Out by the Treasurer**

Following is a brief description of the various treasurers' responsibilities, intended as an overview and introduction.

The treasurer must take custody of all monies belonging to the city or town and must scrupulously account for those monies. (41:35) In this accounting, the treasurer must utilize and maintain a cash book, containing a breakdown of all receipts, disbursements, and cash balances.

The treasurer must determine the cash needs of a municipality and ensure that sufficient liquid assets are available to pay current obligations. All money not required to be kept liquid for purposes of distribution must be invested by the treasurer in such a manner as to require the payment of interest on the money at the highest possible rate reasonably available, taking account of safety, liquidity and yield. (44:55B)

## **Duties and Responsibilities of the Treasurer**

The treasurer's responsibilities also include a major role in the issuance of municipal debt. Issuing debt requires, initially, an affirmative vote by the municipality's legislative authority, the city council or town meeting. Temporary loans require a majority vote and longer-term borrowing, a two-thirds vote. (44:4, 6, 6A, 7) Debt instruments must be signed by the treasurer and countersigned by the mayor, in a city, unless the charter otherwise provides; in a town, the bonds must be countersigned by a majority of the selectmen. Upon the authorization of long-term debt, the treasurer should prepare for the sale by working with the community's financial advisor, bond counsel and other local officials. The treasurer should negotiate borrowings, prepare the necessary documents and notes, and report to the Director of Accounts on all debt issued. (44:16, 23, 24, 28) Town treasurers must report to the town accountant, or to the finance committee, in the absence of a town accountant, the amount of debt and interest due in the next fiscal year at the time they submit their budget estimates. (41:59)

Only the treasurer may pay out public money. Even then, the treasurer may only make payments upon the signature of the board or officer duly authorized to approve the payment of bills. In cities, it is the auditor, or officer invested with similar duties, who must approve all bills and payrolls before the treasurer may pay them. In towns, it is the town accountant and a majority of the board of selectmen who must give the approval. In some towns, approval responsibility has been given to the town manager, instead of to the selectmen. (41:52, 56) In the case of payrolls, the department head, or designee, must attest to their accuracy before the treasurer may make payment. (41:41)

The treasurer possesses a number of specific responsibilities relating to payment of and accounting for salaries and wages. These include:

- Receiving, accounting for, and disbursing all payroll and personnel deduction amounts (taxes, retirement, insurance, annuities, etc.).
- Maintaining all payroll and personnel records and acting as liaison between employees and the retirement board, insurance vendors, etc. (149:178B; 175:138A)
- Acting as custodian and administrator, if so appointed, of the unemployment compensation program. (40:5E)
- Assuring compliance with the General Laws and with state and federal regulations pertaining to labor and industry standards and to retirement and insurance benefits.
- Monitoring conformity with local personnel bylaws, union contracts, and civil service regulations.

In cities and towns, which maintain a separate retirement system, the treasurer must also serve as the treasurer of that retirement system. [32:23(2)]

The treasurer must maintain custody of stabilization funds, pension reserve funds, trust funds, enterprise funds, investments, and all other funds of the town not specifically allocated to other agencies by general law or special act. (40:5B, 5D; 41:46; 44:53; 44:53F<sup>1/2</sup>)

Generally, the treasurer serves as custodian of various financial documents, such as insurance policies, fidelity bonds of other town officials, and deeds to all municipal property acquired by deed.

## **Duties and Responsibilities of the Treasurer**

[The town accountant serves as the custody of contracts in towns and must also maintain a register of sureties on bonds (41:57); in cities, the clerk serves as the custodian of contracts. (41:17)]

The treasurer should regularly advise administrative officers, finance committees, and others concerning the financial condition of the city or town, providing factual information upon which appropriating and budgeting decisions may be made.

The treasurer should diligently maintain tax title accounts, conduct sales of land of low value, in proper circumstances, and prepare documents required to petition for foreclosure, when appropriate. (60:50, 61, 62, 63, 76, 77, 79, 80)

Ultimately, the treasurer bears responsibility for the closing and reconciliation of all books and accounts in the treasurer's office, including the cash book, warrants (including vendor, payroll, and special warrants), bank accounts (checking accounts, trust funds, and bond and coupon accounts), insurance programs, retirement funds, debt records, and tax title accounts.

The treasurer should regularly and carefully prepare all obligatory reports, including (a) cash reconciliations (b) reports to the accountant of all receipts and balances; reports of payroll deductions (i.e., federal withholding, state withholding, retirement funds, group insurance, credit union, union dues, etc.) (c) an annual report, which includes a statement of receipts and disbursements, a statement of debt, and, in the absence of trust commissioners, a report of trust funds, and (d) reports required to be submitted to the Bureau of Accounts, including an annual filing on or before June 30<sup>th</sup> of the quarterly report of reconciliation of treasurer's cash. See Division of Local Services website, [www.mass.gov/dls](http://www.mass.gov/dls).)

A treasurer who also serves as the accounting officer for a community must submit the prescribed statement of financial position, or "balance sheet," dated as of the close of business on June 30<sup>th</sup>. The Bureau of Accounts will not certify a community's free cash until after this report has been submitted. (See IGR 86-104, titled Free Cash in the Addendum of this manual for more information on free cash.)

Other responsibilities of the treasurer include the general care of equipment and internal systems, the general management of department personnel, communication with rating services, and acting as remitting agent (for federal and state withholding taxes, retirement programs, hospitalization plans, teachers' annuities, insurance plans, credit unions, United Way, savings banks, labor unions, deferred compensation, and IRAs). See the "Treasurer Records Retention Schedule" for information on disposition of public records. It is located on the website, [www.mass.gov](http://www.mass.gov) under Secretary of Commonwealth (located in alphabetical list of agencies) and in the Addendum of this manual.

## **Miscellaneous Statutory Provisions Applying to Treasurers**

### **Term of Office: Elected**

In the absence of a special act, charter provision or bylaw otherwise providing, a town at its annual election must elect a treasurer for one or more years. (41:1) The treasurer must swear to faithfully perform the duties of the office. (41:107)

## **Duties and Responsibilities of the Treasurer**

### **Term of Office: Appointed**

A town which elects its treasurer under the provisions of Ch. 41 §1 may convert the treasurer's position to appointed by a majority vote of an annual or special town meeting, together with acceptance by the voters at the annual town elections. Subsequently, the board of selectmen appoints the treasurer for a term not to exceed three years. (41:1B)

### **Salary and Compensation**

Town meeting annually fixes the salary and compensation of all elected officials, including elected treasurers. (41:108) For appointed officials, communities may establish salary plans by ordinance or bylaw to classify jobs and set the maximum and minimum salaries for each classification. (41:108A)

In cities and towns which accept Ch. 41 §108P, a treasurer who completes the necessary training and receives certification as a Massachusetts Municipal Treasurer is entitled to receive additional compensation in the amount of 10% of the annual salary, up to a maximum of \$1000.

### **Vacancy in Office**

**Cities** — If a city treasurer's office becomes vacant, or if the treasurer, due to disability or absence, is unable to perform the duties of the office, the mayor, without confirmation by the city council, must appoint a temporary treasurer to perform those duties thereof until another is duly elected or appointed or the treasurer who was disabled or absent resumes those duties; however, no such temporary treasurer may be appointed for a period exceeding sixty days. A temporary treasurer must obtain a performance bond within ten days of appointment. (41:61A)

**Towns** — If a town treasurer's office becomes vacant, or if the treasurer, due to disability or absence, is unable to perform the duties of the office, a majority of the selectmen may, in writing, appoint a temporary treasurer to perform those duties until another is duly elected or appointed or the treasurer who was disabled or absent resumes those duties. A temporary treasurer must obtain a performance bond within ten days of appointment. (41:40)

If a vacancy occurs in the office of town treasurer because of failure to elect a treasurer or the elected person does not accept the office or for any other reason, the town may at any town meeting elect a person to the office. (41:10)

### **Liability of the Treasurer**

A municipal or district treasurer who, in good faith and in the exercise of due care, deposits public money in the Massachusetts Municipal Depository Trust or in a Massachusetts-organized savings bank, trust company or FDIC banking company is not personally liable to the city, town or district for any loss resulting from the closing up of such depository or from the liquidation of its affairs. (44:55A)

A municipality may provide counsel for a municipal treasurer who is sued and whose property is attached if the mayor and council, in cities, or the selectmen, in towns, believe that the suit arose out of actions in which the treasurer performed in good faith, without negligence, and believing the actions were in municipality's interest. In such circumstances, the mayor and council, or the

## **Duties and Responsibilities of the Treasurer**

selectmen, may dissolve an attachment by filing certificates in accordance with legal requirements. (41:43A.) Treasurers may also be eligible for indemnification, including their legal costs, under Ch. 258 § 9 & 13.

### **Bonding of Treasurer**

A treasurer must obtain a performance bond, in an amount set by the selectmen, but not less than the minimum amount established by the Commissioner of Revenue through the publication and distribution of a Bond Amount Schedule. This schedule lists ranges of amounts of money handled and the corresponding minimum bond amounts required. See the Bond Amount Schedule and instructions in the Addendum of this Manual. The bond, also known as a surety bond is purchased from an insurance company and a copy is filed with the Town or City Clerk's office. The performance bond is payable to a municipality and is intended to cover any malfeasance or fraud on the part of the municipal treasurer. It does not protect the treasurer against suit or accusation.

Annually, municipal treasurers must calculate the approximate amount of money from all sources they will handle during the year, determine the range in which that amount occurs, and obtain a bond in at least the minimum amount for that range. If the chief executive officer of the municipality has set a higher amount, the treasurer must obtain a bond in that higher amount.

If the treasurer is not bonded within ten days of election or appointment, the selectmen or mayor and aldermen shall declare the office vacant. Chapter 41, Section 35 of the General Laws regulates the Treasurer's responsibilities in providing for this bond for the faithful performance of his (her) duties. It may be found at the [mass.gov/legislature/general\\_laws](http://mass.gov/legislature/general_laws) website.

## **Assistant, Temporary, and District Treasurers, and Acting Collector-Treasurers**

### **Assistant Treasurer**

With the approval of the selectmen or mayor, the treasurer may appoint, in writing, an assistant treasurer. (41:39A) Unless a temporary treasurer is appointed, the assistant treasurer may, in the absence of the treasurer, perform the treasurer's duties. In performing those duties, the assistant treasurer shall have the powers and be subject to the requirements and penalties applicable to the treasurer. An assistant treasurer must obtain a performance bond within ten days of appointment. The commissioner's minimum bond amount for an assistant treasurer is 25% of the amount established for the treasurer. (41:39A)

An assistant treasurer appointed under G.L. Ch. 41 §39A is an officer with an indefinite term of office, and no reappointment is required until the assistant resigns, retires or is otherwise removed from office. Removal would probably require joint action by the treasurer and the selectmen (or mayor).

### **Treasurers Acting as Collector of Taxes**

A town may vote to authorize its treasurer to act as collector of taxes. (41:1) A treasurer authorized to act as a tax collector may exercise all the powers of a tax collector, including the appointment of deputy tax collectors. (41:37; 60:92)

## **Duties and Responsibilities of the Treasurer**

### **District Treasurer**

See Chapter 1 for an explanation of the duties of a district treasurer.

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## **Chapter 3**

# **Operations**

This chapter discusses operational procedures and reporting requirements imposed upon municipal treasurers to ensure their proper accounting for all municipal monies in their care.

### **Cash Receipt and Disbursement Records**

The treasurer must maintain a number of journals and other materials to account for municipal monies turned over to the treasurer's office, including a cash book and bank ledger, together with records of municipal debt, tax title accounts, trust funds, and payroll and vendor accounts. In addition, the treasurer must preserve materials containing back-up authentication for entries in these books and records. The Treasurer must interface with the Town Accountant or City Auditor to provide information properly coded and organized for the Accountant's records in order that the municipality is prepared for its annual audit.

### **Accounting Standards and Audits**

The Bureau of Accounts strongly recommends annual audits of a municipality's financial statements by an independent CPA firm. Annual audits are required, however, if a community has expended a certain level of federal funds. Audited financial statements are very important to a municipality as they measure its financial health and its ability to repay debt. Qualified opinions or disclaimers from outside auditors affect a municipality's bond rating, its ability to borrow, and the covenant with existing bond holders.

The Massachusetts Bureau of Accounts oversees the financial management of the 351 Massachusetts cities and towns. It reviews and approves the audit reports of these local governmental units, as well as those of authorities and other governmental units. The Governmental Accounting Standards Board (GASB) is the authoritative standard setting body on how to prepare financial statements in conformance with Generally Accepted Accounting Standards (GAAP). In 1999, GASB's standard # 34 was issued, requiring a new set of standards for all governmental audits. It was important that all municipalities conform to these accounting standards in order for their financial statements to be consistent with those of other governmental units across the country. The Bureau of Accounts issued "A Practical Guide for Implementation of Governmental Accounting Standards Board Statement # 34 for Massachusetts Local Governments". This guide was written by a consultant, Powers and Sullivan, CPA's. It may be found on the website, [mass.gov/bureau of accounts/accountants](http://mass.gov/bureau%20of%20accounts/accountants). In July, 2003, The Bureau also issued a publication titled "Uniform Massachusetts Accounting System", which updated the Bureau's recommended accounting system and Uniform Chart of Accounts to make compliance with GASB 34 easier. This document may also be found at the same website.

## The Cash Book

Municipal treasurers must “annually render a true account of all [their] receipts and disbursements and a report of their official acts.” 41:35: This statutory provision necessitates treasurers' use of a cash book. The cash book provides a control that enables treasurers to reconcile the cash on hand with bank statements and with the general ledger. A cash book may vary in form to suit a particular community's needs, and is generally made up of computerized records

The cash book should contain the dates and amounts of all receipts and deposits. A list of payments by warrant is also necessary information for the cash book.

Following is a brief description of the contents of a cash book:

1. Cash Receipts
  - a. Beginning balance — reconciled balance brought forward from the previous month.
  - b. Date — usually the date of receipt. Sometimes, as in the case of the direct deposit of state receipts, the entry in the cash book will be a day or two after the date of receipt in the bank account. Use both the date of entry and the date of receipt in this instance.
  - c. Sources — primary sources of revenue are taxation and state receipts. For accurate accounting and reporting, the source must be clearly identified. If a receipt is not immediately identifiable, record and deposit it, and then follow up on it.
  - d. Amount of receipt.
  - e. Subtotal amount.
  - f. Amount of deposit — when deposits to more than one bank are made, each bank should be identified.
  - g. Total of monthly cash receipts.
2. Cash Disbursements
  - a. Date of warrant.
  - b. Warrant number.
  - c. Type of warrant — this will vary with each community. Some have only one weekly warrant that includes all expenditures; others have separate warrants for payrolls, revenue sharing, investments, community development, etc. If separate cash books are maintained by fund, the treasurer should record the warrant in the cash book where receipts are recorded.
  - d. Check series used on warrant.
  - e. Amount of warrant.
  - f. Total of monthly warrants.

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3. **Cash Reconciliation** (Refer also to chapter 4 on reconciliation.)
  - a. Bring forward the month's beginning balance.
  - b. Add to this amount the total receipts for the current month.
  - c. Deduct the total warrants paid during the month.
  - d. Reconcile bank statements with check register balance. (Refer to information on check registers in this chapter.)
  - e. List all banks, account numbers, types of accounts, reconciled cash balances, and cash on hand. Cash on hand consists of receipts recorded in the cash book in the current month but not yet deposited to the bank. The total of this list should equal the total cash book balance and the general ledger cash balance.

## Cash Receipts

Various municipal officers and departments turn over money to the treasurer. The following list identifies some of these officers and departments and includes an explanation of the particular receipts acquired from each source.

1. **Tax Collector:** The tax collector makes turnovers to the treasurer using a *Schedule of Payments to the Treasurer*, forwarding a copy to the accountant or auditor, who compares it with the *Schedule of Treasurer's Receipts*. Real and personal property taxes.

Semiannual System: Under the semiannual system, real and personal property taxes are due in 2 installments, depending on the date of mailing of the tax bills. For the first installment, if the bills are mailed on or before October 1<sup>st</sup>, that payment is due on November 1<sup>st</sup>. If, on the other hand, the bills are mailed after October 1<sup>st</sup>, the first installment is due on the 30<sup>th</sup> day following the date of mailing. For the second installment, if the bills are mailed on or before April 1<sup>st</sup>, that payment is due on May 1<sup>st</sup>, but if the bills are mailed after April 1<sup>st</sup>, the second installment is due on the 30<sup>th</sup> day following the date of mailing.

Quarterly System: A municipality may make real and personal property taxes due in 4 installments by accepting Ch. 59 §57C. Under this system, the first two installments are due on August 1<sup>st</sup> and November 1<sup>st</sup>, respectively, so long as the bill, called a preliminary bill, is mailed on or before July 1<sup>st</sup>. Sending a bill after July 1<sup>st</sup> requires approval of the Commissioner of Revenue, a condition of which is the submission to the Commissioner of a *pro forma* recap sheet. A late-mailed bill is due in 2 installments, the first 30 days after mailing, and the 2<sup>nd</sup> on November 1<sup>st</sup>.

The second two installments are due on February 1<sup>st</sup> and May 1<sup>st</sup> respectively, so long as the bill, called an actual bill, is mailed by December 31<sup>st</sup>. The actual bill can only be issued after the establishment of the tax rate for the fiscal year.

If the actual bill cannot be mailed by December 31, an additional preliminary bill may be issued upon approval of the Commissioner. This third quarter bill is due on February 1<sup>st</sup>, or 30 days after the date of mailing, whichever is later. The actual tax bill issued upon the establishment of the tax rate is then due on May 1<sup>st</sup>, or 30 days after the date of mailing the bill, whichever is later.

- a. Interest on delinquent real estate and personal property taxes.

Delinquent property taxes accrue interest at 14% under both the semiannual and the quarterly systems; Under both systems interest accrues from the respective due date.

- b. Abatements resulting in overpayment of tax.

A taxpayer who receives a tax abatement that results in an overpayment of the tax is eligible for a refund in the amount of (a) the overpayment, (b) interest paid on the overpayment and (c) interest at 8% *per annum* on the overpayment, calculated from the due date or the payment date, whichever is later. (59:69) The treasurer cannot issue a refund in an amount less than one dollar. (59:58A)

- c. Motor vehicle excises.

The Registry of Motor Vehicles annually calculates the value of all registered motor vehicles for the purpose of excise assessment, enters billing information on computer tapes, and mails the tapes, with commitments, to the cities and towns for their use in producing motor vehicle excise bills. Because of the volume and variety of types of vehicles, the Registry is unable to provide billing information for all vehicles at the same time. Rather, the billing tapes, with commitments, are prepared and distributed in batches subsequent to January 1. The first batch, usually mailed out in early January of each year, is comprised of passenger motor vehicles which were registered as of the preceding January 1. Billing information and commitments for other types of vehicles and all vehicles registered after January 1 are sent in later batches. Excise bills are due on or before the 30<sup>th</sup> day after the date of mailing. If a motor vehicle excise is not timely paid, interest accrues on any unpaid amount at 12% *per annum* from the date the payment was due until the date it is paid.

- d. Boat excises.

Municipalities are required to assess an excise upon any person who owns a boat on July 1<sup>st</sup> and moors, docks or principally situates that boat for the summer season in the city or town. The excise is due on or before the 60<sup>th</sup> day following the mailing of the bill. If a boat excise is not timely paid, interest accrues on any unpaid amount at the rate of 12% *per annum* from the date the payment was due until the date it is paid. In addition, the boat owner must pay a penalty in the amount of \$20 or 20% of the amount of the excise due, whichever is greater.

Any municipality that collects a boat excise must establish a Waterways Improvement and Maintenance Fund under Ch. 40 §5G and credit 50% of all boat excise revenue received to the fund. [60B §2(i)]

- e. Betterments (Special assessments).

Whenever a specific area of a city or town benefits from a public improvement, or betterment (e.g., water, sewer, sidewalks, etc.), the municipality may assess special property taxes upon the property owners of that area to reimburse the governmental entity for all, or part, of its costs in constructing the improvement (80:13). 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. If

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apportioned, each year's amount, together with one year's committed interest, computed from October 1<sup>st</sup> to October 1<sup>st</sup>, is added to the tax bill until the betterment has been paid. A community can set an alternative interest rate at ANY percentage up to 2%, rather than charge the current fixed rate of 2% above the financed rate. Under the semiannual system, betterments and other special assessments are billed to the first half real estate bills. Under the quarterly system, the assessors may commit betterments and other special assessments with the preliminary tax. If paid annually, communities can structure the installment payments to be equal or equal to the number of real estate payments (i.e. quarterly (4))

- f. Water, sewer use, and electric light.

A community which makes its tax collector a city or town collector by voting to accept Ch. 41 §38A may extend its collector's authority to the collection of "all accounts due the city or town...." In such communities, the collector collects utility payments and should turn those payments over to the treasurer on a daily basis.

- g. Miscellaneous receipts.

Miscellaneous receipts, such as demand charges amount set by municipality), cemetery receipts, ambulance service fees, certificates of municipal liens (60:23), etc. should be turned over to the treasurer at least weekly.

### 2. **Municipal Departmental Receipts.**

Departments turning over money to the treasurer should utilize a *Schedule of Departmental Payments to Treasurer*. The heading of this schedule also should have the municipality's name, and the name of the department originating the schedule. The actual schedule lists each payment, stating from whom it originated, the source of the funds, and the amount. This design of this schedule originated with the Department of Revenue as *Form 9 & 10*, and was typed. It is now normally done as a computer spreadsheet which contains the information required. One copy of this form should be transmitted to the accountant or auditor, a second to the treasurer, and the third retained by the department. The bottom of the accountant's copy of the schedule contains the signature of the responsible official in the originating department as well as the date and amount being remitted. The bottom of the Treasurer's schedule is a tear-off sheet which is signed by the treasurer or designee and returned to the originating department as a receipt.

- a. Water, Sewer, and Municipal Light Departments.

In any municipality with a separate department to handle the billing and collecting of water, sewer, and electric light receivables, the treasurer should insist that the department, at least weekly, and preferably daily, (a) pay over all monies collected to the treasurer or (b) deposit those monies into a designated bank account, sending a copy of the deposit slip to the treasurer. In either case, the department should utilize a *Schedule of Payments to the Treasurer*. The treasurer should ensure that all persons responsible for such collections are properly bonded. Notwithstanding the fact that the General Laws only set out requirements that collectors, treasurers, clerks and assistants be bonded, all other employees handling money should also be bonded, either individually or under a blanket employee fidelity policy.

b. Fees.

A number of municipal officials who perform local inspections collect fees for their services. These include building, electrical, gas and plumbing inspectors, along with the sealer of weights and measures. Other officials collect fees for licenses issued by municipal department, including licenses for street openings, marriage and death certificates and alcoholic beverages pouring licenses. The school department collects monies for tickets to athletic events, for school lunches and through student activity fees. The treasurer should insist that all of these monies are turned over to the treasurer at least weekly.

c. User Fees.

Two local acceptance statutes permit municipalities to earmark user fees for particular services to support the costs of the departments providing those services.

Offset Receipts (44:53) — This local option provision permits estimated receipts of a particular department to be earmarked for use of the department and appropriated to offset its annual operating budget. The statute limits the amount of offset receipts appropriated to no more than the actual receipts collected for the prior fiscal year. The Director of Accounts must approve use of a higher amount before appropriation. Actual collections greater than the amount appropriated close to the general fund at year-end. If actual collections are less, the deficit must be raised in the next year's tax rate.

Revolving Funds (44:53½) — This local option provision permits a community to raise revenues from a specific service and to use those revenues without appropriation to support the service. The statute specifies that each fund must be re-authorized each year at annual town meeting or by city council action, and that a limit on the total amount that may be spent from each fund must be established at that time. The aggregate of all revolving funds may not exceed 10% of the amount raised by taxation by the city or town in the most recent fiscal year, and no more than 1% of the amount raised by taxation may be administered by a single fund. Wages or salaries for full-time employees may be paid from the revolving fund only if the fund is also charged for all associated fringe benefits.

d. Insurance Reimbursements.

Sums not in excess of \$150,000 ~~\$20,000~~ recovered under the terms of fire or physical damage insurance policies or received in restitution for damage done to municipal property may be used by the officer or department having control of the property for its restoration or replacement without specific appropriation.

3. **State and Federal Agencies:** The following list identifies some of the monies provided to cities and towns by state and federal agencies. The treasurer must notify the accountant or auditor upon the receipt of these monies.

**Commonwealth**

a. Cherry Sheet receipts.

## Operations

The Cherry Sheet is the official notification to cities, towns and regional school districts of the next fiscal year's state aid and assessments. The name derives from the cherry colored paper on which the notices were originally printed. Cherry Sheet aid distributions are based on formulas and reimbursements that provide funds for costs incurred during a prior period for certain programs or services. The State Treasurer must monthly ~~annually~~ distribute Cherry Sheet payments to cities and towns on or before the last day of the month ~~on or before September 30<sup>th</sup>, December 31<sup>st</sup>, March 31<sup>st</sup> and June 30<sup>th</sup>~~. (58:18A) The State Treasurer disburses these monies electronically, providing with each distribution a cover letter that indicates what funds (e.g., Ch. 70, Lottery, Highway Fund) will be made available, less monthly ~~quarterly~~ assessments. The Town Treasurer should include a copy of this letter with the *Schedule of Treasurer's Receipts*, sent to the accountant or auditor for record keeping purposes.

No complete Cherry Sheet distribution may be made in any fiscal year to a city or town that has not submitted its prior fiscal year's Schedule A to the Department of Revenue. In addition, no Cherry Sheet distribution may be made to a regional school district that has not submitted its prior year's annual financial reports, as prescribed by the Director of Accounts, to the Department of Revenue. All withheld aid is distributed to the appropriate municipality and school district once the requisite reports have been submitted and accepted by the Division of Local Services. (58:18F) Sometimes partial cherry sheet payments are made.

b. Other state receipts.

The state distributes to local communities some monies that do not appear on the Cherry Sheet. These monies include court fines and restitutions (280:2), hotel/motel excise distributions (64G:3A) and Chapter 90 Highway Funds (58:18B).

c. Grants.

The state awards grants at various times throughout the year, depending on when a community qualifies for a particular program. Although the General Laws require all copies of grants and contracts to be on file in the accountant's or auditor's office, the treasurer should obtain copies of grants to be aware of their requirements in order better to comply with these requirements.

The treasurer must credit all interest earned on grant funds to the general fund unless some specific provision of the grant or of general or special law otherwise provides. (44:53) Certain grants received from the Massachusetts Department of Public Works provide an example of an instance in which a special law expressly provides that interest earned on grant funds becomes part of the grant.

#### 4. Managing State Receipts

Treasurers should arrange to have grants and other state payments to their respective municipalities sent directly to their depository banks or to the Massachusetts Depository Trust for deposit into the municipality's designated account. Further, treasurers should direct their depositories to give them notice as soon as possible after receiving such payments to enable them to quickly invest these monies for maximum earnings.



5. **Loan Proceeds:**

When the treasurer issues debt and the bank credits the loan proceeds, together with accrued interest and any premium, to the municipality's general fund, the treasurer should separately identify the proceeds, interest and premium when reporting to the accountant or auditor on the *Schedule of Treasurer's Receipts*. Bond premium, net of issuance costs, must be used to reduce the amount borrowed, or placed in a special fund for appropriation to capital projects.

6. **Investments:**

- a. Matured Investment. Whenever an investment, such as a certificate of deposit or a Treasury bill, matures, the treasurer must record it as a cash receipt. The treasurer should record the name of the bank in which the money was held, the type of investment that matured, its date of maturity, and the amount of the matured investment. It is insufficient for the treasurer to simply advise the bank to roll the investment over without performing a cash entry; doing so would result in an imbalance in the accountant or auditor's ledger.
- b. Interest. Upon receiving notice of interest earned on various investments throughout the year, the treasurer should record this interest earning as a cash receipt in the cash book, noting the type of investment yielding the interest and the name of the bank holding the investment.

7. **Tax Titles:**

- a. Whenever a property owner redeems a tax title, the treasurer should record the redemption in the cash book, noting the amount of the redemption and specifying a breakdown of the interest and any other associated costs.
- b. Whenever a tax possession property is sold, the treasurer should record the sale in the cash book. The entry should state the amount of tax, interest and charges outstanding on the property at the time of sale, as set out in the accountant or auditor's books (the book value), and the net amount of the gain or loss on the sale.

8. **Miscellaneous Receipts:**

Treasurers receive money from a variety of other sources throughout the year, including refunds from vendors, rental payments for use of municipally-owned property, other than school buildings health insurance payments from retired municipal employees, and insurance recoveries from fire or physical damage policies. The treasurer may keep the revenue in revolving accounts and use the revenue to maintain the buildings without appropriation. The balance of the account will be transferred to the General Fund at year end. The treasurer should clearly identify the source of all receipts when recording them in the cash book.

## **Operations**

### **Disbursements**

The treasurer possesses sole responsibility to pay the bills of a city or town and must make such payments in strict accordance with the General Laws. This responsibility is set out in Ch. 41 §35, which states, “[The treasurer) shall receive and take charge of all money belonging to the town, and pay over and account for the same according to the order of the town or its authorized officers. No other person shall pay any bill of any department.”

Ch. 41 § 52 & 56 detail the mandatory procedures for submitting, approving, and paying bills. Section 56 states, in pertinent part:

The selectmen and all boards, committees, heads of departments and officers authorized to expend money shall approve and transmit to the town accountant as often as once each week ~~once each month~~ all bills, drafts, orders and pay rolls chargeable to the respective appropriations of which they have the expenditure. Such approval shall be given only after an examination to determine that the charges are correct and that the goods, materials or services charged for were ordered and that such goods and materials were delivered and that the services were actually rendered to or for the town as the case may be.... The town accountant shall examine all such bills, drafts, orders and pay rolls, and, if found correct and approved as herein provided, shall draw a warrant upon the treasury for the payment of the same, and the treasurer shall pay no money from the treasury except upon such warrant approved by the selectmen.... The treasurer shall not pay any claim or bill disallowed by the town accountant As being fraudulent, unlawful, or excessive The DOR has consistently held that an expenditure is “excessive” when the appropriation is exhausted. So far as apt this section shall apply to cities.

This statute delineates several steps involved in the payment process. This process incorporates a check and balance system between the treasurer and other city or town officials. Fundamental to the process is the preparation of a warrant by the accountant or auditor. The warrant is a list of the bills to be paid and communicates authority to the treasurer to pay the bills and payrolls listed by carrying the authorized signatures. The accountant or auditor examines the legitimacy of the bills provided by officers and departments of the municipality and may disallow and refuse to approve for payment any claim deemed to be fraudulent, unlawful or excessive. The accountant or auditor then prepares a warrant, placing on that warrant all of the bills which examination has determined should properly be paid. The accountant or auditor then submits the warrant to the selectmen or city council for approval. In municipalities which have adopted a charter, the Town Manager or Town Administrator may be designated to sign the warrant. Autonomous boards such as School Committees, some Water and Sewer Commissions, and Municipal Light Boards are allowed to designate one person, with a designated backup, to must approve their warrants, which are separate from the municipal warrant. Upon signing a warrant, the selectmen, city council, or other paying authority transmits it to the treasurer for payment. The most common warrants, discussed below, are vendor warrants and payroll warrants. A number of special types of warrants, however, are used with less frequency.

### **Vendor Warrants**

Some variations exist in check preparation among the various cities and towns. Generally, the treasurer’s office prepares the checks to be signed and issued. In some communities, however, the accountant or auditor prepares the checks, utilizing a computer system to print the checks at the

same time the warrant is printed. Certainly, if the accountant or auditor prepares the checks, the treasurer should carefully verify the information on them, as ultimate liability rests with the treasurer, the person statutorily responsible for the issuance of checks.

In any case, the treasurer's office should carefully maintain a check register to record all disbursements and should regularly reconcile this register with bank balances. Whether a check is written for individual vouchers or batched to the vendors using consolidated checks, the treasurer must maintain a clear record that discloses for each check the payee, the payment amount, the warrant and voucher numbers, the payment date, and the check number.

For effective cash management purposes, the treasurer should fix the timing of disbursements in such a way as to pay out money from the treasury at the last possible moment. Of course, the treasurer must, at the same time, make payments timely in order to treat vendors fairly and equitably. Wire transfer payments of Fed Funds which go directly into the payee's account for debt service, health insurance premiums, large contractor payments, etc. allow a treasurer to pay bills on the due date. Paying on the due date allows the treasurer to keep funds invested as long as possible. The accountant or auditor needs to mark such large items as No Check vouchers in the check register, so that a check will not be produced. The treasurer and accountant or auditor should work cooperatively with all major municipal departments to effectively schedule warrant payments in a way that enhances good cash management. Such factors as vendor discounts, invoice processing policies, vendor mandates, and payment delivery procedures can substantially affect payment dates.

### **Payroll Warrants**

No material difference exists between processing a payroll warrant and a vendor warrant. In both cases, the treasurer must create a record that discloses the payee, the amount paid, the voucher numbers, the accounts charged, and the gross amount disbursed. In processing a payroll, however, the treasurer must be vigilant in ensuring compliance with all federal and state withholding forms and requirements. Chapter 7 provides a very detailed discussion of issues and legal requirements involved in making payrolls.

### **Special Warrants**

A treasurer may utilize a special warrant or separate warrants to authorize payment from certain restricted funds, such as:

1. Enterprise funds (water, sewer and electric departments).
2. Trust funds, including stabilization and conservation funds.
3. Retirement funds.
4. Capital projects funds.
5. State or federal grants funds.
6. Agency funds.

Under the UMAS (Uniform Municipal Accounting System promulgated by the Bureau of Accounts and described in their website, [www.mass.gov](http://www.mass.gov)) accounting system used by Town Accountants and

## Operations

City Auditors however, these fund disbursements are usually included on the vendor or payroll warrant, but designated by the fund number pertaining to the particular fund.

## Supporting Documentation for Cash Book

Treasurers should retain all documentation that relates to particular receipts in a file or loose-leaf book, indexing this material to the cash book. This documentation is of especial importance in the case of receipts from federal and state agencies and certain miscellaneous sources. Some types of documentation include:

1. *Schedule of Turnovers to the Treasurer* (Information on original Bureau of Accounts forms, AD Form 7 or AD Form 9 & 10). Municipal departments that collect revenues must use replicas of these forms in making turn overs. The treasurer should verify the amounts listed on a turn over form and return a receipted copy to the department.
2. Check stubs. The treasurer should maintain reconciled bank statements, outstanding check lists, and canceled (and voided) checks, either in numerical sequence or on compact disks using check imaging.
3. Letters of transmittal.
4. Deposit slips. Deposit slips disclose in detail amounts deposited and provide a trail to the total deposit and individual recorded receipts in the cash book. The detail on a deposit slip may consist of an actual listing of payees with the amount of the check to each payee. In larger communities, the detail may consist of an adding machine tape that verifies the deposit total. Such tapes, and the bank verified deposit slips themselves should be stapled to the corresponding *Schedules of Departmental Receipts*.
5. Warrants. The treasurer should retain all warrants separately.
6. Receipt books. Receipt books are generally bound and contain pre-numbered receipts. The treasurer may utilize a receipt book to record miscellaneous receipts collected over the counter for which no other documentation existed to explain the receipt. Documentation is essential for a good audit trail, not only for the treasurer, but also for anyone who might audit a community. A poor audit trail in any department could be very costly to a municipality when an audit is performed because of the additional time required to verify transactions and perform the audit work. It also opens suspicion of mismanagement of funds, or outright fraud.

## Classification Book or Worksheet

Some treasurers keep a classification book or worksheet that will provide a detailed breakdown of amounts posted to the cash book. The book or worksheet is maintained daily or at least weekly. Preserving these records can be helpful in completing reports such as the *Schedule of Treasurer's Receipts* and the annual reports. A treasurer must determine whether the extra effort and bookkeeping is worth the effort of an extra paper trail. If the cash book documents and related computer print outs are sufficient, an extra worksheet or classification book is not necessary.

## Required Reports: Reporting from the Cash Book

All of the reports that the treasurer must make, either to internal departments or to external agencies, can be prepared from the cash book. These reports include:

1. Schedule of Treasurer's Receipts. The treasurer must complete and transmit this report weekly in large communities and monthly in smaller ones to the accountant or auditor, using AD Form 11LL or a spreadsheet containing the following information for each receipt: the payer, the payment amount and the reason for the payment. Receipts of the same type, such as real estate taxes for a particular fiscal year, should be combined and reported as one amount. Some receipts, however, such as grant and Cherry Sheet receipts, should not be summarized. The accountant or auditor can best advise the treasurer about how to report a particular item. Generally, the more detailed a report, the better.
2. Quarterly Reconciliation of Treasurer's Cash. The treasurer, with the assistance of the accountant or auditor, must complete this report within 45 days of the close of each calendar quarter. The reports are to be kept in the Treasurer's office, with the exception of the June report, which must be submitted to the Division of Local Services, Bureau of Accounts (DLS). The format of this report can be found on the DLS website, [www.mass.gov/dls](http://www.mass.gov/dls). The accounting officer must complete part two or three of the report. Reconciling at least monthly with the accountant or auditor will make preparing the *Quarterly Report of Reconciliation* much easier.

## Bank Ledger (Master Check Register)

Municipalities using multiple banks and a variety of banking services may find a bank ledger to be helpful in keeping track of daily balances and in reconciling total cash each month, although a computerized spreadsheet may be even easier.

A bank ledger is a multiple column spread sheet with a separate column for each bank account. Total daily deposits, warrants paid, transfers in and out, miscellaneous debits and credits, investments, and interest should be posted in the appropriate columns. The bank ledger should agree with the cash book since both records reflect deposits, net of total warrants paid. Reconciled bank statements that reflect outstanding checks, deposits in transit, and other timing adjustments should also agree with both records. A bank ledger provides a particularly good trail in municipalities that transmit and receive frequent wire transfers of funds.

## The Check Register

A check register lists checks paid in numerical sequence, identifying for each check the payee, date drawn, and amount paid. A separate check register should be maintained for each checking account. Check registers may be produced as part of an electronic data processing (EDP) of warrants.

The check register is the primary record for preparing the outstanding check list necessary to reconcile bank statements at the end of each month. The check register may also serve as a control for the use of checks since they are accounted for in numerical sequence.

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### **Investment Policy and Log**

Treasurers should develop an investment policy, which explains investment strategy and specific goals within the state laws restricting investments and the degree to which investment goals were met. Auditors find investment policy documents to be extremely helpful. The Mass Collectors and Treasurers Association (MCTA) developed a model investment policy, which is available through the MCTA office.

An investment log is a multiple column form or computerized spreadsheet disclosing for each investment such information as the date of purchase, amount paid, name of the bank or custodian, and the date and value at maturity. It is a valuable aid for the treasurer in keeping track of fixed-term investments and in computing investment income.

### **Preparing for an Audit**

All municipal finance officers must understand their respective roles in preparation for and in the course of an audit conducted by an independent public accounting firm. Communication and cooperation between municipal officers and the audit team are essential for the effective and efficient performance and timely completion of the audit.

In preparing for an audit, a treasurer should assemble several documents for the auditors to review during their work, including:

- An organization chart of the treasurer's office, with a copy of job descriptions and office procedures.
- A listing of all bank accounts held in the name of the municipality, including addresses, and names of contacts.
- Auditors may require Treasurer's office to prepare a confirmation letter requesting verification for balances as of a certain date (usually June 30<sup>th</sup> of the FY being audited) which are to be sent to all banks. This confirmation letter must be signed by the Treasurer and given to the Auditors to mail; Confirmations are then sent directly to the Auditors.
- A reconciliation of all bank statements.
- Copies of June 30th bank statements.
- A detailed listing of all investments, with the name of each custodian, as of the end of the prior fiscal year.
- A reconciliation of outstanding receivables.
- Listing of debt payments for Fiscal Year being audited, and outstanding debt
- A reconciliation of Treasurer's cash to Accountant or Auditor's records
- A formally adopted investment policy
- An explanation of procedures for student activity accounts.

The treasurer should be prepared to discuss with the auditors, at their request, these and any other documents relating to the financial activities of the treasurer's office.

### **Internal Control Review**

Normally, auditors initiate an audit of a municipality's finances with a review the municipality's internal control. A municipality's internal control consist of its plan of organization, together with all of the coordinate methods and measures adopted by it to safeguard its assets, check the accuracy and reliability of its accounting data, promote operational efficiency, and encourage adherence to prescribed fiscal policies.

An internal control review encompasses four phases:

1. Documentation of the internal control system.
2. Preliminary review of the system.
3. Test of the system to ensure that financial transactions comply with it.
4. Final evaluation of the system.

#### Documentation.

During the documentation phase of the internal control review, the auditors develop work papers to obtain a basic understanding of the treasury system. They learn how the treasurer performs the duties of the office.

The work papers may consist of any combination of flow charts, written narratives, copies of sample forms and reports. To develop the work papers, the auditors may need organization charts, job descriptions, procedure manuals and other documents. The auditors may also conduct interviews with employees involved in billing and collecting taxes, making daily deposits and performing monthly reconciliations. The treasurer may find the documentation materials developed by the auditor to be useful to the future performance of the duties of the office. Accordingly, the treasurer should request copies of these materials.

#### Preliminary Review.

After completing the documentation phase, the auditors will commence a preliminary review or evaluation of the municipality's internal control. They will ascertain whether the system contains sufficient safeguards. If they conclude the system is safe, the amount of auditing work necessary will be greatly reduced. Conversely, if they conclude otherwise, the amount of that work will be greatly expanded.

A distinct segregation of functions and duties constitutes a key element of internal control. If different individuals perform key functions, the auditors will anticipate a decreased likelihood of a problem's going undetected. For example, if a department head were to place persons on the payroll, submit the weekly time sheets and distribute checks to employees, that department head would be in a position to place a fictitious employee on the payroll and then retain and cash fraudulent checks.

## **Operations**

While conducting the preliminary review, the auditors will begin to compile comments for the management letter. The treasurer should not hesitate to request the auditor to give comments on the internal control system. Hearing the comments right away will permit the treasurer to initiate corrective action during the audit. In this way, the management letter might include the statement, “The town official responsible has begun to implement, or has taken corrective action.”

### Compliance Testing.

If the auditors conclude that they can rely on the internal control system, they must next ensure that the system is actually being used. This step is called “compliance testing.” It involves taking samples of transactions (normally a statistical sample) and reviewing the documents that were involved in these transactions (i.e., warrants, invoices, canceled checks, and time and attendance records). The auditors will check to see that warrants have been signed, that invoices are mathematically accurate and that purchase orders were properly approved. The auditors will also review postings in ledgers, cash books and journals. In addition, they will review the minutes of town meetings to attest that financial articles were properly recorded.

### Final Evaluation.

Once the auditors have completed compliance testing, they will perform a final evaluation. This evaluation will determine whether the procedures of the system are being followed. Of course, the audit fee will relate directly to the number of hours required to perform the audit. Accordingly, audit costs are substantially reduced if a municipality has adequate internal control procedures and follows those procedures.

## **Substantive or Validation Tests**

After the internal control review, the auditors will develop an audit program to perform substantive or validation tests. These tests will entail verifying bank account balances, reviewing legal documents, performing various analyses, and requesting management and legal representation letters. To comply with generally accepted auditing standards, the auditors will put the audit program in writing and make it a part of their working papers.

Substantive or validation testing involves reconciling a document prepared by an external organization with the town’s records to ensure the accuracy of those records. One normal substantive test is reconciling the town’s cash account with a bank statement sent directly to the auditor from the bank.

The auditor may also request a standard written confirmation with the bank statement. On such a confirmation, the bank would enumerate all town bank accounts, their account numbers, and their balances on the audit date. Such a confirmation helps the auditor to be confident that all banking accounts at particular banks have been taken into account.

Auditors frequently prepare, in addition, a list of individuals and firms that the municipality's records of receivables indicate owe money to the town on the audit date. Subsequently, they send a statement to those individuals and firms, asking them to verify the amount they owe. After they



receive these statements back, they can investigate any discrepancies, thereby ascertaining the authenticity of the municipality's records.

Other substantive tests may include an analysis of investments, insurance policies, and contracts. The auditors may also review various records for the period after the audit date to determine whether transactions after the audit period that should have been recorded during that period were properly executed.

The treasurer's involvement with the audit decreases substantially after completion of this testing. At this point, the audit firm deals primarily with the municipality's executive's officers. Notwithstanding, the treasurer may be asked for assistance at any time.

All in all, since the treasurer's operations constitute a major focus of a financial audit, the treasurer must always prepare in advance by being careful to maintain up-to-date and accurate records of all financial transactions.

### **Procedures for Handling Unclaimed Checks**

Ch. 200A §9A makes available to cities and towns a more advantageous procedure for handling unclaimed checks than the escheat provisions applicable to other holders of unclaimed funds, whereby they must turn over such checks to the state. Indeed, if the treasurer complies with the procedures set out in this statute, instead of having to turn the checks over to the state, the municipality can retain them.

The §9A procedures require the treasurer to declare, in writing, an intention to retain the unclaimed checks and to file that declaration with the municipal clerk. The treasurer must then give notice to the apparent owner of each check. For an uncashed check issued by the municipality in the amount of \$10 or more, the treasurer must mail notice to the apparent owner, explaining how that person may solicit the money. For an uncashed check issued by the municipality in the amount of \$100 or more, the treasurer must cause a notice of the check to be published.

The owner of an unclaimed check has 1 year from the date of notice to file a claim for that check. If no claim is filed, the treasurer may credit the unclaimed check to the general fund of the municipality.

If, on the other hand, a claim is filed, the treasurer possesses the sole right to determine the claim and must send written notice of the determination to the claimant. Within 20 days of this notice, the claimant may apply for a hearing and redetermination of the claim. After an appropriate hearing, the treasurer must make a final determination within 30 days after the hearing. A claimant adversely affected by the treasurer's decision may appeal within 20 days of receiving notice to the district, municipal, or superior court. If the court rules in favor of the claimant, the treasurer must pay over the amount of the check, with interest at the rate one-twelfth of 1% per month, from the date the claimant first made the claim.

## **Operations**

### **Collecting Unpaid Checks from State**

Unpaid checks can also be found money for municipalities. When a check has been made out to a municipality and has not been turned over to the municipal treasurer, it may remain uncashed. It is eventually turned over to the State as an unpaid check and held by the State Treasurer in an unpaid check fund. Should out dated checks turn up (usually left in a file drawer or cabinet), the treasurer should contact the State Treasurer's office to see if it is in the State's unpaid check fund. The State Treasurer also posts notices of unpaid checks in the fund, and periodically sends notices to municipalities, apprising them of unpaid checks being held. For information, and a claim form, Treasurers should use the website [www.mass.gov/dor](http://www.mass.gov/dor) and "Unpaid check fund claim form" in the Quick links listed. Another source is the State Treasurer's website at [mass.gov/treasurer](http://mass.gov/treasurer).

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## **Chapter 4**

# **Reconciliation**

### **Reconciliation of Cash**

One of a municipal treasurer's primary functions is to conscientiously manage the municipality's cash. Such management requires prompt and frequent cash reconciliations. The proper frequency of such reconciliations in any particular municipality depends largely on the number and types of bank accounts held by that municipality. At a minimum, however, the treasurer should reconcile the bank accounts, the cash book and the general ledger at least monthly.

A treasurer may choose from a variety of available methods to reconcile a bank account, ranging from performing a manual reconciliation to utilizing a comprehensive reconciliation service offered by a vendor. In a community that issues 300 or more checks per month, the treasurer would be wise to utilize a comprehensive reconciliation service. In such a case, the treasurer would only have to provide the vendor with a list of all checks issued in order to receive in return complete reconciliation reports. Communities issuing fewer checks generally do not require a full reconciliation service; however, they can generally benefit from some other, more limited, reconciliation assistance. With advancing technology, additional new programs and materials frequently become available. Treasurers should strive to be aware of these advancements. The treasurer must, however, weigh the cost for any particular program or service against the benefit anticipated to be derived by the community.

To perform a cash reconciliation, a treasurer must coordinate and balance three, separate categories of financial records:

1. The statements for all municipal bank accounts under the treasurer's control.
2. The treasurer's cash book.
3. The accountant's or auditor's ledger(s).

### **Reconciliation Chronology**

The treasurer should calculate the aggregate amount of cash on deposit in municipal bank accounts and balance this total with the cash book prior to undertaking a reconciliation of these records to the accountant's or auditor's ledger(s).

## Reconciliation of Bank Statement

The ensuing list relates a series of steps a treasurer should take upon receiving a bank statement. The treasurer should:

4. Compare bank charges with debit memos, and bank credits with deposit tickets and credit memos.
5. Check off the cancelled checks that appear on a previous bank reconciliation sheet.
6. Check off in the checkbook or register the cancelled checks issued since the last reconciliation. (Generally, a treasurer makes a check mark to denote those checks paid by the bank and an "O" to denote the check(s) still outstanding.)

In the process of reviewing checks, the treasurer should heed all voided checks. Any check replaced with a new check must be removed from the outstanding list to prevent double counting. Conversely, any check not replaced must be added back to the accountant's or auditor's books as cash.

7. Calculate the aggregate amount of all outstanding checks. In performing this calculation, the treasurer should subtract the amount of the checks paid by the bank since the previous statement from the amount of the checks outstanding at the time of the issuance of that statement.
8. Subtract the current total of outstanding checks from the figure shown on the bank statement as the current balance. The resultant number should equal the treasurer's balance for that account.
9. Undertake the following additional steps if the bank statement disagrees with the treasurer's balance:
  - Add to the bank balance any deposits that were made at the end of the subject month that will not appear until the issuance of the subsequent month's bank statement.
  - Add or subtract any other debits or credits that were posted to the account and included with the statement. Interest earned by a bank account should be recorded in the cash book in the same period that the bank recorded it.
  - Add or subtract any other adjustments the treasurer has recorded that were not shown on the statement.
  - Carefully check the bank's work, making a comparison of the bank's computer listing of checks it paid with the individual cancelled checks. The treasurer might discover that the bank (a) charged the treasurer's account for a check it paid but failed to include the cancelled check with the statement, (b) paid an amount slightly different from the

## Reconciliation

amount specified on the check or (c) erroneously charged the account for someone else's check.

10. Undertake the following further steps if, after making the appropriate adjustments, the statement continues to differ from the treasurer's balance:
  - Subtract from the bank's figure any deposits that were outstanding as of the end of the preceding month.
  - Subtract redeposits of "bounced" checks.
  - Review deposit slips and verify transfers from other depositories to ensure proper credit for additions to the beginning bank balance. Add any deposits that were made but not credited.
  - Add or subtract for any other adjustments. The bank may have treated something as a deposit that the treasurer did not, and vice versa. The treasurer may have voided a check and returned it to cash, or may have returned "tailings" (uncashed checks returned to general fund—See Chapter 3) to cash as a receipt.
11. Undertake the following supplementary steps to check disbursements if, after reconciling receipts, the statement continues to disagree with the treasurer's balance:
  - Add the amount of each cancelled check returned by the bank, warrant by warrant. For each warrant, the treasurer should add to the warrant total the aggregate amount of the outstanding checks for the warrant. This figure should agree with the total warrant amount, after the warrant total has been adjusted for any non-check items.
  - Upon discovering that a particular warrant contains an error, carefully recheck the outstanding checks for that warrant.

## Preliminary Work for Preparing a Reconciliation Worksheet

The following list itemizes various steps a treasurer should take prior to making entries on a reconciliation worksheet. The treasurer should:

1. List payments of checks, by bank, either individually or in groups, on the date they were charged against the balance in the bank account, verifying that each check, whether reported individually or as part of a list, is recorded on the particular statement.
2. Verify paid, direct deposit checks with a detailed list of payments, ensuring that the amount on the list agrees with the amount recorded on the bank statement. (Direct deposit in this instance means a check transferred from the treasurer's depository to the employee's account, which may be in the same or in another depository.)
3. Ascertain that other bank charges (stop payment orders, transfers to other depositories, etc.) are accompanied by bank or municipal authorizations.

4. Review deposit slips and verify transfers from other depositories to ensure proper credit for additions to the beginning bank balance. For deposits made but not included, the treasurer should add the aggregate of these deposits to the ending bank balance as listed on the bank statement.
5. Determine the aggregate amount of outstanding checks. The treasurer should begin by comparing the amounts of all returned checks with the amounts listed in the checkbook or register. The treasurer should include the numbers of any voided checks with the numbers of the checks returned with the bank statement in order that missing check numbers may identify uncashed checks. The treasurer should then prepare an outstanding list, adding up the amounts for which the missing checks were written. Some of these missing checks may have been written in previous months but remain uncashed at the time of reconciliation. In totaling the amount of all missing checks, the treasurer should, in the case of a small number of such checks, list them on the back of the bank statement; for a large number, the treasurer should itemize the checks on a standard check register form and attach it to the bank statement. The treasurer should retain all applicable information as a proof of reconciliation and in the establishment of an audit trail.
6. List the ending balance of the bank account as recorded on the current bank statement.
7. Subtract the total of outstanding checks from the total ending balance listed on the bank statement. The result should agree with the balance in the treasurer's checkbook or register.

### Utilizing a Reconciliation Spreadsheet

Treasurers will find an electronic spread sheet to be of substantial assistance in performing reconciliations. Such a spreadsheet should include the following: beginning and ending bank balances for all accounts including investments, deposits into accounts, interest earned, payments made out of accounts, other charges made against account such as bounced check fees, transfers into and out of the account, outstanding checks, and deposits in transit. Space should be left for special adjustments or special transactions not included in the standard categories.

The effort will aid the treasurer in discerning reconciliation problems that result from the timing of transactions between banks. The process will enable the treasurer to verify that:

1. Deposits made to all banks during the period balance with the total of all deposit receipts.
2. Payments for each bank statement balance with warrants paid during the period covered by that statement.



## Reconciliation

3. Any transfer from a bank balances with a transfer to some other bank.

## Reconciling the Worksheet

4. The worksheet enumerates transfers in and out of checking accounts to enable the treasurer to trace transferred monies from bank to bank. If the total amount of transfers in does not equal the total amount of transfers out, the treasurer should carefully check each transfer.
5. If the total amount of deposits, together with the amount of cash on hand, does not equal the total amount of cash book receipts, the treasurer should review deposit slips and other documentation in order to discover the reason for the discrepancy. Imbalances frequently result from timing difficulties. Furthermore, if a community makes book entries for payroll deductions but does not actually redeposit these monies, the payroll deductions must be added to deposits in order for them to agree with the cash book.
6. In order to ensure that payments agree with warrants, taking outstanding checks into account, the treasurer should perform the following calculation:
  - Add together all payments.
  - Add to the sum obtained the aggregate amount of all checks remaining outstanding at the end of the month.
  - Subtract from this sum the aggregate amount of outstanding checks at the beginning of the month.

Upon discovering that payments and warrants do not agree, the treasurer should determine whether (1) any payments occurred during the subject period that were not on warrants or (2) any checks cleared the bank but were on the first warrant of the following month.

## Reconciling the Cashbook to the Ledger

After reconciling bank statements to the treasurer's cash book, that cash book total should be reconciled to the accountant's or auditor's ledger. If these records do not agree, the treasurer should undertake the following procedures to reconcile them:

1. The treasurer should verify that transfers between trust (or other non-operating accounts) have been entered in both the treasurer's and the accountant's or auditor's books.
2. Also, the treasurer should compare the total amount of monies actually received with the amount recorded in the ledger(s) for the month. If these amounts do not agree, the treasurer should verify that the *Treasurer's Schedule of Receipts* (end-of-month report to accountant or auditor) agrees

by detailed amount and classification with the cash book. If not, the treasurer has made a reporting error and must correct that error.

3. In addition, the treasurer should compare the total amount of the warrants paid during the month with the total warrant amount recorded in the accountant/auditor's ledger(s) for the same period. The last warrant paid should be the last warrant recorded. Otherwise, a timing problem probably accounts for the discrepancy.

The accountant's or auditor's cash accounts in the ledger should reflect only those cash transactions provided by the treasurer. Therefore, undertaking the above steps should resolve any discrepancies between the cashbook and the ledger. If they do not, the treasurer and accountant or auditor should go through each entry to the ledger until they ascertain the reason for any variance.

### **Unclaimed Checks**

The treasurer should deal with uncashed checks utilizing the procedure set out in Ch. 200A §9A. See Chapter 3 for a detailed explanation of this process.

### **Record Retention**

Treasurers should retain bank statements, together with all accompanying information, including returned checks, in accordance with the record retention requirements of the Secretary of State. (See website at [www.mass.gov](http://www.mass.gov) and look under list of agencies for Secretary of State and in Addendum in this manual.)

## Reconciliation

<b>Reconciliation .....</b>	<b>0</b>
Reconciliation of Cash.....	0
Reconciliation Chronology s.....	0
Reconciliation of Bank Statement.....	1
Preliminary Work for Preparing a Reconciliation Worksheet .....	2
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reconciliation .....	1	spreadsheet .....	4
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### **Chapter 5**

## **Tax Titles and Foreclosures**

When a taxpayer becomes delinquent in paying real estate taxes or other local charges that constitute liens on real estate, the municipality has statutory authority to take title to the taxpayer's property and, subsequently, to undertake proceedings to foreclose the owner's right to redeem that property from tax title.

Ch 60 §54, provides in pertinent part:

Title to...land...taken [for nonpayment of taxes] shall...vest in the town, subject to the right of redemption. Such title shall, until redemption or until the right of redemption is foreclosed..., be held as security for the repayment of said taxes with all intervening costs, terms imposed for redemption and charges with interest....

It is common for tax collectors and treasurers to use legal counsel specializing in tax title and foreclosure law to assure that all steps in the process of taking title or foreclosing are precisely followed.

### **Tax Title Process**

The tax collector may not initiate a taking on any particular parcel of real property until at least 14 days have elapsed following the mailing to the property owner of a demand for the overdue taxes and charges. In order to commence the taking process, the collector must prepare a notice of taking for each parcel to be taken. At least 14 days before the date of the taking, the collector must publish the notice in a local newspaper and must post copies of that notice in 2 or more public places (e.g. Library, Town Hall). At the designated date and time the collector must go to the designated place and announce the taking on behalf of the city or town. The designated place could be the collector's office

Subsequent to an announcement of taking, the collector must prepare an Instrument of Taking (State Tax Form 301) for each parcel. Optionally, and if the budget permits the collector may hire the tax title attorney to review the Instrument of Taking documents and ensure all current and subsequent owners or listed and that no bankruptcies are pending. The fee for these services can be added to the Tax Title account and recovered upon redemption. The collector must record and/or register these documents at the appropriate registry of deeds within 60 days of the date of taking or the taking would be invalid and must be redone.

Upon the completion of a taking process, the collector must transmit to the treasurer a list of the recorded takings. (State Tax Form 346,) The list must detail for each property the name(s) of the delinquent taxpayer(s), a brief description of the property, the years for which the property was taken and the amount of the unpaid taxes and other liens at the time of the taking. Upon receiving this list, the treasurer becomes responsible to collect the delinquencies.

The treasurer must set up a separate Tax Title Account (State Tax Form 410) for each parcel of real estate included in a list of recorded takings. (Each Tax Title Account must contain the following information:

- Name and address of person assessed.
- Name(s) of subsequent owner(s).
- Date of taking.
- Legal description and location of property.
- Book and page of the recording of the Instrument of Taking or, in the case of registered land, certificate and document number.
- Unpaid tax amount for the year(s) for which the property was taken.
- Other additional costs, such as betterments, utility charges, district taxes etc.
- Collector's interest to the date of taking.
- Collector's fees and charges, as outlined in Ch. 60 §15.
- Subsequently certified taxes.

Upon setting up a new Tax Title Account, the treasurer should promptly notify the delinquent taxpayer, as well as the current owner of the subject property, if different from that taxpayer, to give notice that the property is in tax title and to inquire whether either party wishes to redeem the property. A current owner may have purchased the property subsequent to the tax year in question and may not know of the delinquent status. The notice may prove particularly helpful in such a circumstance.

### **Maintaining Records on Tax Title Accounts**

The treasurer's tax title duties also include taking custody of all tax deeds and instruments of taking and maintaining records on all properties in tax title. Collaborating with the collector and the assessors facilitates the record collection and preservation process.

Proper maintenance of tax title records will permit an accurate determination of the amounts necessary for redemption and will establish a legal basis for a petition for foreclosure of the right of redemption with the Land Court. Electronic record keeping is most helpful to the treasurer. There are programs available, or they can be developed in house. The tax title account sheets should be kept in a uniform manner, either by delinquent's name, by street location or parcel id. If time and resources permit, the treasurer should cross-index the accounts alphabetically by location. With some computer software, a treasurer can maintain account sheets in map and parcel order, a system which assessors favor. In any case, treasurers should not keep account sheets chronologically. A

treasurer using a chronological filing system, upon receiving an inquiry, would have to examine account sheets for multiple dates of taking.

The treasurer should retain on file a copy of each instrument of taking, attaching a copy of the newspaper clipping containing the advertisement to the tax title sheet. A copy of the assessors map and field card may also be helpful.

Further, the treasurer should determine whether any mortgages exist on tax title property by performing research at the registry of deeds, if the collector has not already done so. Generally, the register of deeds can provide online computer access to registry records, facilitating the treasurer's research. Law firms providing tax title expertise normally have staff available to research this information as well. Upon discovering the existence of a mortgage, the treasurer should notify the mortgagee of the tax title status and about foreclosure proceedings. Since a municipality possesses a priority lien on unpaid taxes, a mortgage holder has a substantial interest in redeeming a tax title on mortgaged property.

The treasurer should also know the identity of local developers and other persons who own multiple properties, particularly multi-unit buildings. Frequently, such properties become subject to tax titles. A treasurer who is diligent and aggressive in communicating with the owners of such properties can often facilitate tax title payments.

In addition, the treasurer should know the identity of surveyors who are active in the area. A surveyor may be able to assist the treasurer in identifying the owner of properties listed as "owner unknown" in the assessors' records. For example, if a surveyor surveys a land parcel adjacent to owner unknown property in tax title, the survey results might disclose the tax title property's owner. If the treasurer has cultivated the surveyor's acquaintance, the surveyor may communicate the ownership information to the treasurer, and to the collector and assessors, as well.

## **Redeeming a Tax Title with Installment Payments**

Any person with an ownership interest in a tax title property can redeem that property with the treasurer at any time up until a petition to foreclose has been filed in the Land Court by paying all of the outstanding taxes, interest and other charges due on the property. (60:62) Such a person may also redeem the property by making installment payments to the treasurer. (60:62) Chapter 354 of the General Laws of 2006 amended this statute. Effective February 7, 2007, Ch 60:62 as amended gives treasurers greater flexibility in working out reasonable payment plans with delinquent taxpayers. Prior to this change, a delinquent taxpayer had to pay at least 25 % of the full amount needed to redeem the tax title and then pay out the remainder within a one year extension. The amendment eliminates any minimum partial payment and allows a treasurer to extend by two years the period within which foreclosure proceedings cannot be initiated. As part of the payment plan a treasurer may insist that the taxpayer remain current with new tax bills as they are issued. The payment plan schedule should be realistic for the taxpayer and provide a payoff in a reasonable time period. Failure to pay new tax bills or the tax title payments in full and on time would place the taxpayer in a default status and subject to foreclosure in land court.

## **Assignment of Tax Title**

Although the Commissioner of Revenue recommends against the procedure, Ch. 60 §52 permits a municipal treasurer to assign a tax title to the highest bidder after a public auction, provided that the sum paid for an assignment is not less than the amount necessary for redemption. There are publishing, posting, and notification requirements for an assignment similar to a tax taking. See Ch 60 §52 for details. Surplus proceeds from an assignment are general revenue of the municipality. The assignee does not acquire any right to possession of, or receive any rent or income from, the tax title property. The assignee is entitled to collect only 6.5% interest, not the 16% owed to a municipality under G.L. Ch. 60 §62. Subsequent years' taxes for the property must still be assessed and billed to the owner of record, not the assignee. If these taxes are not paid the collector will end up executing another tax taking on the property. An assignee selling property after acquiring title through a Land Court foreclosure does not have to pay any surplus proceeds to persons who could have redeemed the property before foreclosure.

### **Bulk Assignments**

Ch. 60 §52 authorizes collectors and treasurers to make bulk assignments of their delinquent property tax receivables. This power supplements a collector's power to make tax sales under Ch. 60 §§40 -50 and a treasurer's power to make assignments of tax titles under Ch. 60 §52. The power to make bulk assignments applies to delinquent personal property taxes as well as to real estate taxes. In the case of real estate taxes, the assignment must include non-tax obligations, such as water and sewer charges, that have been added to the tax and are secured by the tax lien. (See IGR 97-201 in Addendum or at DLS website, [www.mass.gov/dls](http://www.mass.gov/dls)).

### **Land Ownership Records**

Massachusetts maintains two concurrent systems for determining real estate title. The oldest and most common is the abstract system. The abstract of a parcel of real property is made up of all of the deeds and other instruments which relate to that parcel that have been recorded in the registry of deeds for the district in which the land lies. To determine the ownership of a particular parcel, a title examiner must review the abstract of the property, tracing the ownership from person to person and from deed to deed over the years. All deeds for recorded land are identified by the book and page number in which the deed is recorded at the appropriate registry of deeds.

The concomitant title system in the Commonwealth is the registered land system. Land becomes registered when the Land Court issues a decree certifying that the person(s) named on the Certificate of Title hold(s) ownership rights to the land and that the land is free of any encumbrances not listed on the certificate. Once a parcel of land has been registered, all subsequent instruments affecting that land must be filed with the registered land section of the registry of deeds and must be noted on the appropriate Certificate of Title in order to be effective.

### **Foreclosures in the Land Court**

The Massachusetts Land Court has exclusive, original jurisdiction over the registration



of title to real property and over all matters and disputes concerning such title subsequent to registration. The court also exercises exclusive original jurisdiction over the foreclosure and redemption of real estate tax liens.

The offices of the Land Court are located at 24 New Chardon Street in Boston, MA 02114-4703. The justices of the Land Court usually sit at these premises. Where circumstances warrant, however, the court holds sessions in other locations within the state.

#### When a Foreclosure Petition May Be Brought

A municipal treasurer can bring a petition in the Land Court to foreclose an owner's right to redeem a property from tax title. The foreclosure process constitutes a very effective payment enforcement tool available to treasurers. Through utilizing this tool, a treasurer can either induce a delinquent taxpayer to redeem a tax title by paying the necessary tax and charges or to forfeit title to the property by action of the Land Court.

Chapter 60:65 applies to tax title foreclosure. It states in part that "Except as provided in section sixty-two, whoever then holds the title to land acquired by a sale or taking for taxes may bring a petition in the land court for the foreclosure of all rights of redemptions of said land either after six months from the sale or taking, or in the case of a city or town, at any time following the sale or taking if the buildings thereon have been found to be abandoned property pursuant to section eight-one A, or there has been a certification pursuant to section 81 B that the redemption amount as determined pursuant to section 62 exceeds the assessed value of the parcel."

#### Procuring Legal Assistance

Treasurers undertaking foreclosure proceedings in Land Court should consider engaging the services of a law firm with experience in tax title foreclosures. Land Court cases do not proceed automatically. They require constant monitoring in order to be successful.

#### Funding Tax Title Foreclosures

Ch. 60 §50B directs that every community include in its annual budget the necessary monies to pay for tax title foreclosure proceedings. This appropriation should be in the amount estimated by the treasurer; however, it must be at least \$80 for each tax title ripe for foreclosure held by the community involving property having a current assessed valuation greater than \$100,000.00.

The statute contains, in addition, a default provision, which provides that "[i]f in any year the amount so estimated [by the treasurer] is not included in the budget as finally passed, the treasurer shall certify in writing to the assessors such portion of the amount estimated...as has not been provided and the assessors shall raise in the assessment for such year the amount certified to them by the treasurer and thereupon said amount shall be added to the treasurer's appropriation...."

Pursuant to this default provision, the Department of Revenue's tax rate approval process incorporates the automatic inclusion of monies for tax title purposes among "other amounts to be raised" as distinct from amounts appropriated by municipality.

In 1999, in a Bulletin entitled, "Budgeting for Expense of Tax Titles and Foreclosures," the Division of Local Services clarified what particular amounts may be raised without appropriation pursuant to these default provisions of Ch.

60 §50B. The bulletin identified these amounts as "out-of-pocket expenses" such as:

- Filing and recording fees, including examiner's costs required by the Land Court.
- Advertising and publishing costs.
- Certified mailing costs.

Other expenses, such as the following, cannot be raised pursuant to these provisions and must be appropriated:

- Staff expenses of the collector and treasurer.
- Staff expenses of the city solicitor or town counsel.
- Outside counsel fees.
- Costs for consultants or for service bureaus retained for record keeping.
- Custodial costs and costs for maintaining or insuring property.
- Costs of selling property after foreclosure.

On July 1, 2015 MGL Ch 60 §15B became effective allowing cities and towns to establish a tax title collection revolving funds account to pay for expenses related to tax takings and foreclosures. IGR 16-101 states "The purpose is to provide tax collectors and treasurers with funds to secure the municipality's liens for delinquent real estate tax receivables and to foreclose tax titles after reasonable efforts to work with taxpayers on payment of amounts outstanding." It is a local acceptance statute. It is established by (a) by-law; (b) ordinance; or (c) vote of the legislative body. In general, the charges, costs, and fees associated with a tax taking and foreclosure go into the revolving funds. The collector's and treasurer's interest goes to the general fund. Interest on these funds also goes to the general fund. The funds can be used on the expenses of tax takings and foreclosure up to the amount in the fund without further appropriation. The officer in charge of the fund must report annually to the Board of Selectmen, mayor, manager, or chief administrative or executive officer. The municipality may revoke the fund. See MGL Ch 60 §15B and IGR 16-101 for details.

### **Petition to Foreclose**

To initiate foreclosure proceedings at the Land Court, the treasurer (or the tax title attorney for the municipality) must prepare and file a Petition to Foreclose. All of the documents necessary for such a filing are available at the offices of the Land Court. In filling out a petition, the treasurer (or tax title attorney) must enter the date of taking, the date and the book and page of the recording of the Instrument of Taking, the assessed value of the property, the description that appears in the Instrument of Taking, and the names and addresses of all persons with any ownership interest in the property. The treasurer must, under oath, sign both the petition and a duplicate. (See Land Court Form LCP-5)

## **Filing at Land Court**

The treasurer (or tax title attorney) must file the foreclosure petition at the Land Court office in Boston. The Land Court clerks are very knowledgeable and can answer questions about the filing procedure. Upon filing a petition, a treasurer (or tax title attorney) must file a Notice of Filing Petition in the local registry of deeds. (Land Court Form LCN-2).

## **Filing Fees**

At the time of filing a petition, the treasurer (or tax title attorney) must make a deposit to the Land Court. Subsequently, the court will draw against this deposit for the costs of the following:

1. A Land Court examiner's services to trace title at the registry of deeds and to provide the court with a list of the names and addresses of all parties with an interest in the property.
2. Making copies of the judgment.
3. Preparing and issuing a memo to the assistant recorder.
4. Mailing certified mail notices.
5. Issuing a motion to withdraw, a motion to vacate or a dismissal.

The Land Court will refund any unexpended balance of the deposit at the conclusion of a case. During the progress of a case, the court may request additional deposits to cover increased costs for title examiner's services, publications, or mailing of notices.

## **Land Court Examiner**

At the commencement of a case at the Land Court, the court will appoint a title examiner who will (a) prepare a mini-title abstract that traces ownership from a period beginning 20 to 25 years prior to the tax taking and (b) submit a written report that sets forth the names and addresses of all parties with an interest in the property, "whether as equity owners, mortgagees, lienors, attaching creditors or otherwise." (60:66)

If the report fails to contain the addresses of all of these parties, the Land Court will contact the treasurer (or tax title attorney), requesting the missing information. The court will not proceed further until it receives this information.

## **Notification by the Land Court: to Interested Parties**

The Land Court, upon receiving the examiner's report, must give notice, by certified mail, to all interested parties of the pending of the foreclosure petition. The notice must declare the case number, the property location and the date and time by which an appearance must be entered and an answer filed. Moreover, the notice must "contain a statement that unless the party notified shall appear and answer within the time fixed, a default will be recorded, the petition taken as confessed, and the right of redemption forever barred." (60:66)

If a notice is returned to the court as undeliverable, the court will transmit this notice to the treasurer, requesting the treasurer (or tax title attorney) to further research the subject

owner's address and to forward any corrected address information to the court. Once the treasurer provides an updated address, the court will send a notice to this new address, containing the same information as the original but with a new return date.

Alternatively, a deputy sheriff may be engaged to serve a citation if certified mail fails to reach an interested party.

If, notwithstanding follow-up efforts, a municipality is unable to discover the address of an owner of tax title property, that municipality must so notify the Land Court in writing, including in its notice documentation of its diligent search to discover the address. If the Land Court finds the municipality's explanation to be satisfactory, it will cause notice of the foreclosure petition to be published in a local newspaper and will send a copy of this notice to all other parties with an interest in the property, assessing the additional notification costs to the municipality.

### **Filing an Appearance or Objection (60:68)**

A person claiming an interest in tax title property who wishes to redeem that property must file an answer with the Land Court. In this answer, the person must (a) describe the derivation of the ownership interest and (b) either file a written affidavit of objection to the foreclosure petition, stating the specific facts and grounds upon which the objection is based, or make an offer to redeem the property from tax title.

After that, subject to preliminary motions filed by the parties, the Land Court will assign the case for a hearing. At the hearing, the treasurer (or tax title attorney) will make known to the court the full amount due on the tax title, including all interest, using the interest rate shown on Form 410. The property owner will either (a) offer reasons why the court should refuse to enter a foreclosure degree or (b) offer to pay the amount due. The judge will then either continue the case to a future date or enter a finding, setting out the amount currently due, with the per diem percentage of interest accruing on that amount, and the deadline, generally not less than three months, by which the payment must be made.

### **If Payment is Made**

If the property owner pays the total amount due, including the Land Court costs, the treasurer must issue an Instrument of Redemption (State Tax Form 441) and record or register that document at the registry of deeds. The treasurer (or tax title attorney) must also file a motion with the Land Court to withdraw the foreclosure petition.) The treasurer should also file the redeemed tax title account in the inactive file with the book and page number of the Instrument of Redemption. Finally, the treasurer should issue a Notice of Final Disposition of Tax Title Account (State Tax Form 486) to the collector, accountant and assessor.

### **Partial Payments**

While Ch. 60 §62, discussed above, permits installment payments of the outstanding taxes and charges on a tax title property, the statute specifies that such payments may only be made, unless the Land Court otherwise approves, “prior to the filing of a petition for foreclosure.” (Emphasis supplied.) As a practical matter, however, the court often urges a treasurer to accept installment payments, in which case it continues the case for a

specified period of time to permit the taxpayer to pay installments until the total amount of the redemption costs has been paid.

### **If Payment is Not Made**

If an owner fails to make payment on or before the due date specified by the Land Court, then the treasurer (or tax title attorney) may file a motion for a foreclosure decree, alleging that the terms of the finding have not been met. The court must hold a hearing on the motion, at which time court will permit the owner to offer an explanation about why the payment has not been made. The taxpayer may pledge to make the payment in the future. At the hearing, the judge must either allow the motion for a foreclosure decree or continue its consideration to a future date. If the hearing is continued, similar procedures will take place at the continued hearing or subsequent continued hearing(s) until the case is withdrawn, as a result of redemption, or the court allows the motion for a foreclosure decree. (60:69)

### **Non-Contested Cases**

If the owner of tax title property, after having received proper notice of a foreclosure petition, fails to file an answer within the prescribed time period or otherwise to contest the case, the treasurer, in order for the court to issue a foreclosure decree, must first file 2 other documents:

- An Affidavit as to Military Service, stating that no parties in the case are away in military service, using Land Court Forms LCA-3 or LCA-4.
- A motion for general default using Land Court Form LC-M-1. Following its receipt of these forms, the court will take under consideration the issuance of a foreclosure decree.

### **The Issuing of a Foreclosure Decree**

If the court allows a motion for a foreclosure decree, it will first consider all other aspects of the case; if it finds them in order, it will then issue the decree, sending an attested copy to the treasurer (or tax title attorney) for recording or registering at the registry of deeds.

Upon the issuance of the decree, title to the property vests in the municipality. At this point, the treasurer should notify, in writing, all interested municipal departments, including the collector, assessors, auditor or accountant and mayor or selectmen. (See State Tax Form 486). All of the outstanding taxes should be certified to the tax title account before the decree is entered. If not, then the collector must certify the taxes to the tax possession account. Be sure to include any betterments that may exist on the property.

The property should be removed from the tax rolls and no further taxes assessed unless the property is redeemed or sold. If taxes are assessed in error they are to be certified to the tax possession account.

### **Redemption of Tax Titles Which Have Been Foreclosed**

Should any interested party request to redeem a tax title that has been foreclosed, the

treasurer must refuse. A treasurer cannot accept payment or issue an Instrument of Redemption. Rather, the treasurer should direct the person to the custodian, department or body which then has control over the disposition of municipal property. If that custodian, department or body indicates to the treasurer, in writing, that it has no objection to the redemption, the treasurer (or tax title attorney) may petition the Land Court to have the foreclosure decree vacated upon payment of the full amount of taxes and charges due.

Ch. 60 §69A permits a party with a legal interest in a parcel of foreclosed property to petition the Land Court to vacate the decree during the 1-year period following the entry of the final decree. In a case in which the treasurer has certified that the redemption fee exceeds the value of the property, the statute limits the filing of a petition to vacate to the 90-day period following the entry. This abbreviated time period permits a municipality to more quickly dispose of such property without having to be concerned that a former owner might file a petition to vacate.

It is usually not advisable to have a decree vacated until after payment has been received in full and the check, if any, has cleared. As with a regular redemption, once payment has been received, a petition to vacate the decree filed, and the case withdrawn, the treasurer must prepare and record or register an Instrument of Redemption.

### **If the Request for Redemption is Denied**

Should the custodian, department or body deny a party's request for redemption, the party may, within one year of the date of the decree, file with the Land Court a petition to vacate. The court will hold a hearing on the petition and, if the delinquent taxpayer can pay all monies due and the municipality has not conveyed the property to a third person, will generally grant the petition.

Upon the entry of a decree of foreclosure or the denial of a petition to vacate a decree of foreclosure, an interested party may appeal to the Massachusetts

### **Appeals Court.**

A treasurer should obtain counsel to handle cases allowed by that court.

### **Recovery of Costs and Fees**

A treasurer (or tax title attorney) may file a motion with the Land Court to allow adding up to \$500.00 in attorney's fees to the tax title account. (60:65) The party redeeming tax title property is liable for all court costs. The amount of these costs can be obtained from the court's accounting department.

Furthermore, if the value of a foreclosed property does not cover the taxes, charges, fees, and interest due to the municipality, the municipality may bring a civil suit against the assessed owner for the deficiency. See Boston v. Gordon.

### **Tax Possessions**

The mayor in cities and the selectmen in towns may appoint a custodian to manage property acquired through the foreclosure of tax titles. Specifically, the custodian “shall have the care, custody, management and control of all property heretofore or hereafter so acquired by said city or town. The custodian shall serve during the pleasure of the mayor or selectmen and shall receive as his compensation, if any, a sum fixed by the mayor or by the selectmen.” (60:77B) The treasurer is often appointed as the custodian, especially in smaller towns.

When a municipality acquires a property through land court foreclosure, land of low value foreclosure or deed in lieu of foreclosure the custodian of tax possessions should secure the property immediately. First notify the fire, police, and building departments. Second, physically secure the property by changing the locks on any buildings. If there are buildings add the property to appropriate insurance policy to protect against damage. These expenses should be tracked and included should the foreclosed property be redeemed.

The custodian has authority to sell tax possession property at public auction. However, at least 14 days before a tax possession sale, the municipality must notify, by certified mail, the person who was the owner of record of the property prior to its acquisition by the community. The municipality must also post notice in two or more, public places at least 14 days prior to the sale. The notice must include a description of the property; the date, time and place of sale; and the terms and conditions of that sale. (60:77B)

The custodian may reject any and all bids at such sale if, in his or her opinion, none of the bids represent the market value of the property. The custodian may also adjourn the sale. Upon the consummation of a sale, the treasurer must execute and deliver all instruments necessary to transfer title after payment has been made.

### **Pro Rata/Pro Forma Taxes**

If property belonging to a municipality is sold, the board or officer executing the deed must receive a pro-rated payment in lieu of taxes for the current fiscal year before the deed can be delivered. (44:63A) The payment is calculated by multiplying the tax rate for the fiscal year of the sale by the sale price. For example, if a property were to sell for \$100,000.00 on December 15<sup>th</sup> and the tax rate were \$25.00, the in lieu of tax payment would be calculated as follows:

$$\text{Sale Price} \times \text{Tax Rate} \times \text{Days Remaining in FY} \div \text{Days in FY} = \text{Tax Due}$$

$$\text{For example: } \$100,000.00 \times .025 \times 197 \div 365 = \$1,349.32$$

If the property is sold between January 2<sup>nd</sup> and June 30<sup>th</sup>, the municipality should receive an additional payment in lieu of taxes for the next succeeding fiscal year. This pro-forma tax is calculated by multiplying the sales price by the tax rate. The pro-rata/pro-forma taxes must be received before delivery of the deed. The deed should recite compliance with Ch. 44 §63A.

### **Leasing of Tax Possession Property**

A custodian who believes that selling a tax possession property would not be practicable may lease the property for a period not exceeding 3 years, subject to the approval of the mayor or selectmen.

## **Persons Not Eligible to Purchase Tax Possession Property**

Real property that has been acquired through foreclosure may not be sold to persons convicted of certain crimes, such as arson or fire insurance fraud, or to certain tax delinquents. (60:77B) A prospective grantee must swear under the pains and penalties of perjury that neither he or she, nor any other person who would gain equity in the property, has ever been convicted of arson or fire insurance fraud or is currently a tax delinquent. (See IGR 87-217 at website [www.mass.gov/dls](http://www.mass.gov/dls) and in the Addendum of this manual)The deed for a tax possession property must contain a recitation that such affidavits have been received by the custodian or other person signing the deed.

## **Foreclosure Procedures for Land of Low Value**

A treasurer can expedite the disposal of tax title land of low value through utilizing the procedures set out in Ch. 60 §§79-80C. A treasurer cannot initiate these procedures until after the expiration of at least 90 days from the date of taking.

To utilize this process for any particular parcel, the treasurer must first obtain a certification by the Commissioner of Revenue that the parcel qualifies as low value land.

The Department of Revenue has promulgated 2 state tax forms for use by municipal treasurers in obtaining low value certification. These forms are: (1) State Tax Form 452, an Affidavit to Foreclose Tax Title Land of Low Value and (2) State Tax Form 452A, Statement Relative to Tax Title. The treasurer must submit a separate statement (Form 452A) for each parcel for which low value certification is sought. Each submission, whether or not the submission includes one or multiple statements, must be accompanied with an affidavit (Form 452).

The front side of a Form 452A must be filled out by the treasurer. The information on the front side relates primarily to the details of the tax taking of the subject parcel. The Commissioner will not issue an affidavit certifying property to be low value land if any of the information relating to the taking indicates that this process may not have strictly conformed with statutory requirements. The information provided by the treasurer must be complete and accurate; otherwise, the Commissioner will return the form to the treasurer for completion or correction.

The back side of Form 452A must be filled out by the assessors. The information on the back side relates primarily to the valuation of the subject parcel. The Commissioner will not issue an affidavit certifying property to be low value land if in the assessors' opinion the value of that property exceeds the statutory maximum. The information provided by the assessors must be complete and accurate; otherwise, the Commissioner will return the form to the treasurer for completion or correction by the assessors.

If the Commissioner determines that a parcel (a) is of insufficient value to cover all delinquent taxes, interest, charges and prospective foreclosure costs, (b) that the parcel does not exceed the current year's limit for being categorized as land of low value (See IGR 06-208 in Addendum or current year's corresponding IGR at the website of DLS, [www.mass.gov/dls](http://www.mass.gov/dls) and look under "IGR") This dollar value increases every January 1<sup>st</sup>,



beginning January 1, 2003, by the percentage increase of the Consumer Price Index for Urban Consumers prepared by the Bureau of Labor Statistics of the U.S. Department of Labor for the previous calendar year and (c) that the property has been properly taken, the Commissioner must transmit to the treasurer a written affidavit of this determination. The treasurer must record this affidavit in the registry of deeds for the district wherein the land lies. Once an affidavit in which the Commissioner has certified particular parcels as low value land has been recorded, the treasurer, pursuant to Ch. 60 §79, "may sell those] parcels..., severally or together, at a public auction to the highest bidder," without any city council or town meeting involvement.

That portion of the proceeds of a land of low value sale which constitutes the aggregate of the taxes, interest and charges and expenses of the sale must be deposited in the general fund, pursuant to G.L. Ch. 44 §53, where it becomes available for city council or town meeting appropriation for any lawful purpose. Any surplus, pursuant to Ch. 60 §79, must be deposited by the treasurer in a separate account "to be paid to the person entitled thereto if demanded within five years." If no demand is made, the surplus inures to the municipality's general fund for subsequent appropriation for any lawful purpose.

The treasurer must receive the Commissioner's affidavit that a parcel qualifies as low value land in order to utilize the expedited, land of low value process for the disposal of that parcel. If a parcel does not so qualify, the treasurer must utilize the regular tax foreclosure process, discussed above, for its disposal.

The land of low value process and forms are located on the DOR Gateway website under the "Misc Forms" tab. The DOR has published a guide for applying for land of low value affidavit:

<http://www.mass.gov/dor/docs/dls/mflb/applyingforlandoflowvalueaffidavit.pdf>

and a tip sheet to help make the process easier:

<http://www.mass.gov/dor/docs/dls/it/lovgatewaytips.pdf>

## **Collection Procedures, Tax Titles and Foreclosures**

To minimize the necessity of taking property into tax title and subsequently pursuing foreclosure proceedings, municipalities might undertake some or all of the various actions discussed below:

### **Subdivision Rules and Regulations**

Through its planning board, a municipality could include language in its subdivision rules and regulations specifying that prior to the release of any lots in a subdivision, the planning board will require the submission of percolation test results for all lots in the subdivision, not just for lots subject to a particular request. The language might further provide that any lot within the subdivision that failed a percolation test will be joined with a buildable lot that has passed a percolation test. Moreover, the planning board might also develop its rules and regulation in such a way as to optimize the likelihood that lots will be laid out in a manner that will decrease the occurrence of tax delinquencies. For example,

these rules and regulations could require applicants, at the time of presenting their applications, to include the percolation test results for all of the lots in their subdivision plans, thereby assisting the board's ability to ensure that all the lots are buildable and, therefore, less likely to become tax delinquent. The rules might further establish that, at the time of the release of the initial lot in a subdivision, any other lot that does not comply with state and local percolation standards must be combined with an adjacent, buildable lot. These kinds of planning board provisions would, in particular, permit municipalities to avoid future tax title problems in subdivisions where part of the land is wet or unbuildable and likely, therefore, to be eventually abandoned.

### **Suspension, Denial or Revocation of Local Licenses and Permits**

Through the acceptance of Ch. 40 §57 and the adoption of a by-law or ordinance in accordance with its provisions, municipal licensing authorities may deny, revoke or suspend the licenses or permits of persons and businesses that have outstanding taxes or charges. The bylaw or ordinance should denote if there is any minimum grace period before licenses or permits would be denied, revoked, or suspended. The statute specifically excludes licenses and permits for open burning, dog licenses, fishing, hunting, and marriage among others. This statute is particularly effective in collecting tax delinquencies of commercial enterprises.

### **Withholding for delinquent taxes**

Ch. 60 §93 allows the treasurer to withhold money due to the taxpayer from the municipality for delinquent taxes, other assessments, or other charges committed to the collector. So if a taxpayer is owed a motor vehicle refund but has a Tax Title account, the refund can be applied to the Tax Title account. A receipt and an explanation should be sent to the taxpayer with the remainder or the refund, if any.

### **Intermunicipal Agreements**

A municipality might enter into an intermunicipal agreement with another governmental entity to utilize the license or permit suspension, denial or revocation provisions of Ch. 40 §57. Such intermunicipal agreements are permitted under the provisions of Ch. 40 §4A, which state in pertinent part:

The chief executive officer of a city or town, or a board committee or officer otherwise authorized by law to execute a contract in the name of a governmental entity, as hereinafter defined, may enter on behalf of such unit into an agreement with one or more other governmental units to perform jointly or for such other unit or units any service, activities or undertakings which any of the contracting units is authorized by law to perform, if such an agreement is authorized by the parties thereto, in a city by the city council with the approval of the mayor, and in a town or district by the town or district meeting.

### **Bank or Mortgage Companies**

There are two approaches that can be taken with Banks or Mortgage Companies that hold the mortgage on delinquent properties.

1. Contact the Bank or Mortgage Company and inform them of the delinquent real estate taxes. Not all mortgages come with an escrow account. Not all mortgage servicers pay water/sewer and other charges liened to real estate taxes. Therefore, they may not know about the delinquent taxes and may have much to loose if the property is foreclosed upon.
2. A municipality might utilize the provisions of Ch. 59 §§12A & 12B, which permit cities and towns to levy taxes upon mortgagee banks for real property on which those banks hold mortgages if the equity owners of those properties are delinquent. The assessments may be up to the face amounts of the mortgages, or the fair cash values of the properties, whichever is less. The statute encourages banks to create tax escrows for commercial properties.

### **Collection by Suit**

A municipality may collect a delinquent tax or charge by bringing a lawsuit against the person assessed the tax or charge, within 6 years of the due date, pursuant to the provisions of Ch. 60 §35. A suit filed in a superior court normally takes about 3 months. Once a municipality wins a judgment, it can set up a sheriff's sale to auction off delinquent property. The statute is very effective for mortgaged property. The municipality can also use this statute to collect rental income on commercial property. The jurisdiction of small claims court with respect to municipal claims is detailed in Ch. 218 §21.

### **Collection from Descendants Estates**

If a property tax bill is issued before the owner's death, the executor or administrator should pay the tax; the collector, however, must commence an action within 12 months of that owner's death or lose the community's right to recover the obligation. (197:9) If the bill is issued after the owner's death, the bill should be addressed to the owner's estate. The executor or administrator becomes personally liable for any non-payment up to 6 years after the owner's death.

### **Use of Credit Bureau**

A municipality might consider using the provisions of Ch. 93 to report tax liens to a credit bureau as a means to collect delinquent taxes.

### **Deed(s) in Lieu of Foreclosure**

Pursuant to, G.L. Ch. 60 §77C, cities and towns, as an alternative to tax taking and foreclosure, may accept a deed from all persons with an interest in certain properties on which there are outstanding taxes and charges. Only municipal liens can exist on such properties, and the municipal legislative body must vote to accept the deed. Once the accepted deed has been recorded, the property should be treated as a tax possession. The grantors are permanently barred from reacquiring the parcel from the municipality. (See Ch. 60 §77C.; see also Certification of Assessed Valuation and Redemption Amount, State Tax form 60:81B

## **Tax Title Collection Policies and Procedures**

The treasurer and collector should jointly develop and maintain detailed, tax collection policies and procedures to facilitate the timely collection of delinquent property taxes in the most effective manner. These policies and procedures might include some or all of the following:

### **Policies**

1. Demands can be issued the day after the due date and should be issued on or shortly after that date.
2. If the services of a deputy collector are to be used for real estate taxes, warrants can be issued the day after the demand due date and should be issued on or shortly after that date.
3. The Tax Taking can be executed soon after a demand is issued and must be done before 3 ½ years after the end of the fiscal year for which the taxes were assessed. However, there are costs associated with the taking, so you may not want to execute a taking as soon as legally possible. Decide when tax takings are going to occur and execute them around the same time every year.
4. The municipality will contact mortgagees and inform them of the delinquent taxes and their intentions to utilize the provisions of Ch. 59 §§12, 12A & 12B in the case of delinquent taxes on mortgaged properties.
1. The municipality will report tax delinquents to a credit bureau in cases in which the outstanding tax amount exceeds some threshold amount established by the community.
2. The municipality will report to the credit bureau any tax lien that it obtained through a court proceeding.
3. In appropriate cases, the collector will bring a lawsuit against a tax delinquent, pursuant to the provisions of Ch. 60 §35.
4. The treasurer will seek an attachment on any rental income that is paid on commercial tax title property.
5. The treasurer will initiate foreclosure proceedings 6 months after tax taking for properties which have a value greater than the land of low value threshold, no issues with the tax taking, and do not have a current payment plan in place.
6. In fitting situations, the treasurer will communicate with bankruptcy trustees to seek dismissal of proceedings or relief from a stay of foreclosure actions.

### **Procedures:**

- The tax collector will send a copy of the municipality's tax collection policy to each delinquent taxpayer prior to advertising a property for tax taking.
- Twenty-one days after a tax title is filed at the registry of deeds, the treasurer will notify the property owner, in writing, and will request full payment of all delinquent taxes, interest, and charges within 14 days. (60:61)
- If the owner does not make full payment or sign an installment payment agreement (and the municipality has accepted the provisions of Ch. 40,

§57), the treasurer will transmit the owner's name to all departments,

boards, and committees that issue licenses or permits and, if that owner has any application license or permit in effect or pending, will request the pertinent department, board or committee to deny, suspend or revoke that license or permit pursuant to the statute.

- The treasurer will ascertain whether or not a mortgage exists on tax title property. If so, the treasurer will assess the mortgagee under the provisions of Ch. 59 §§12, 12A & 12B.

### **Certification of Subsequent Taxes to Tax Title Accounts (60:61)**

For all parcels of real estate taken into tax title for nonpayment of taxes in prior year(s) and not redeemed, the collector must certify to the treasurer all unpaid taxes and assessments, together with any costs and interest accrued, in each subsequent year, using State Tax Form 347. A delinquent taxpayer may tender payments on current taxes without penalty until the due date. The collector should make the certification prior to September 1<sup>st</sup> of the year following that of its assessment, preparing Form 347 in triplicate.

The treasurer must return a certified copy of Form 347 to the collector, retain the original for the treasurer's records and forward the remaining copy to the accounting officer.

Upon the accounting officer's receiving a certified copy of Form 347 from the treasurer, that officer will credit the collector for the amount certified to the tax title account as if the tax had been actually paid. The collector must then post the amount shown on the certificate to the applicable account in the tax title column in the commitment book, thereby clearing this account for the tax year.

Upon a taxpayer's redeeming a tax title, the treasurer must issue a Certificate of Redemption and notify the collector. The collector must note the redemption in the commitment book and on the tax title record and remove the record from the active tax title file, noting on the record the name of the person who made the redemption, the date and the redemption amount.

### **Disputed Tax Title Accounts**

If any claim is made that a tax title is improper or invalid, the treasurer should refer the complainant to assessors and the tax collector. The treasurer has no authority to disclaim a tax title. Only the collector possesses this authority. (60:84)

### **Tax Title Redemption**

Any person with an interest in a property in tax title can redeem that property with the treasurer at any time up until a petition to foreclose has been filed in the Land Court. If a person elects to redeem a tax title, the treasurer must perform the following actions:

- Compute the amount due. This amount is the aggregate of the tax title account balance, including fees, charges and other costs. The interest must be calculated each year separately, at the rate specified in Ch. 60 §62, from the date of taking or subsequent certification to the date of payment.
- Collect the amount computed as the full amount due, plus the cost of recording an Instrument of Redemption, and record the payment in the cash receipts book.
- File an Instrument of Redemption at the appropriate registry of deeds. (See State Tax Form 441)
- File the redeemed tax title account in the inactive file with the book and page number of the Instrument of Redemption.
- Issue a Notice of Final Disposition of Tax Title Account to the collector, accountant and assessors. (See State Tax Form 486) Most tax title records are permanent records, pursuant to the Secretary of State's retention schedule for records of municipal treasurers.

## **Abatement of Tax Titles**

Cities and towns that accept a local option statute, Ch. 58 §8C, may enter into agreements with developers of affordable housing for the payment of outstanding property taxes, including the abatement of an amount that makes developing the site economically feasible. A municipality that accepts the statute must first adopt an implementation by-law or ordinance. Abatements must be approved by the Commissioner of Revenue and are limited to 75% of the amount of outstanding real estate taxes and 100% of the accrued interest and collection costs. (See IGR 02-206, titled Tax Agreements for Affordable Housing Developers-- Options for Tax Title Foreclosure, in the Addendum to this manual or at the Division of Local Services website [www.mass.gov/dls](http://www.mass.gov/dls))

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## Chapter 6

# Trust Funds, Grants and Other Special Funds

### Gifts and Trust Funds

#### GASB 34

The Governmental Accounting Standards Board Statement 34 (GASB 34) made significant changes to trust funds. The titles of fund types changed and the accounting for them has been modified. Non-expendable and expendable trust funds have been reclassified. Current categories include:

**Special Revenue Funds** — Funds where earnings must be used for governmental purposes, such as Health Claims Trust, Stabilization Fund, Retirement Fund, Law Enforcement Trust Fund, Conservation Trust Fund, and Unemployment Fund, etc.

**Permanent Funds** (Non-expendable ) — Where income only can be expended, but original principal is restricted and cannot be violated, such as scholarship, library, cemetery, and miscellaneous funds.

**Private Purpose Funds** (Fully expendable) — All other funds where principal and income benefit individuals, private organizations, and other governments, such as cemetery, library, scholarship, and miscellaneous funds.

#### Gifts to a Municipality

Municipal officers and departments may accept gifts or grants of money from governmental or charitable entities, private corporations and/or individuals.

Gifts or grants to school departments must be accepted under the provisions of Ch. 71 §37A; gifts for educational purposes may be expended with the approval of the school committee. Gifts to other municipal departments must be accepted under the provisions of Ch. 44 §53A. Gifts for any purpose other than educational may be expended with the approval of a mayor and council in cities, and selectmen in towns.

Gifts are generally shortlived. The specie is usually expended as soon as funds accrue in amount sufficient to accomplish the purpose intended. Interest accruing on a gift or grant account normally remains with the general fund and becomes part of the gift or grant only if the donor or grantor expressly so provided in writing at the time of making the gift or grant.

#### Trust Funds vs. Gifts

An outright gift to a municipality involves the direct transfer of all interest in the gift property to the city or town at the time of making the gift. A gift in trust, on the other hand, entails an *ongoing* gift to support a specified purpose, program or activity of the municipality.

## Trust Funds, Grants and Other Special Funds

A person making a gift to a city or town generally places some limit on the expenditure of the principal of the gift, perhaps limiting expenditure to the interest, alone.

A person bestowing a gift *in trust* may make an *inter vivos* gift, making the gift effective during the donor's lifetime. Alternatively, the person may bestow a testamentary gift, giving the money as a bequest in a will and making the gift effective after his or her death. Whether a gift in trust is made as a testamentary or *inter vivos* gift, the person making the gift generally will, in writing, (a) specify the purpose(s) for which the monies may be expended and (b) define the powers and duties of the trustee.

The treasurer should deposit all monies given in trust to a city or town in separate fiduciary accounts and should administer them in a trustee capacity in accordance with the written directions of the donor.

### Distinguishing between Trust Funds and Gifts

A trust may be either express or implied. An express trust, which is the standard administered by a municipality, is created by specific provisions in a deed, will, or other writing. An implied trust is one where the intent of the parties, although not made explicit, may be inferred from the nature of the transaction or relationship of the parties.

If a donor's written directions make clear an intent to establish an ongoing fund to support a specified program or activity, then the gift should be treated as a trust. A donor who restricts expenditures to interest accruing on the gift clearly manifests such an intent.

Donors, however, do not always make their intent so clear. Treasurers, accordingly, must exercise care in ascertaining a donor's intent. In the case of significant donations, treasurers should request assistance from the municipality's legal counsel.

A gift, which could be either money or some other tangible property, is generally intended for a specific purpose and not intended to be perpetual. Only donations not intended to establish ongoing objectives, but designated to be expended within a limited period of time should be treated as gifts pursuant to Ch. 44 § 53A.

### A Municipality's Authority to Hold Trust Funds

Massachusetts law expressly permits cities and towns to accept gifts and bequests in trust for such purposes as supporting schools, war memorials, libraries, cemeteries, charities, and scholarships. For example:

- A town “may hold real and personal estate in trust for the support of schools....” (40:3)<sup>[1]</sup>
- A town may “receive, hold, and manage any...[real or personal property] or gift for the establishment of...[war] memorials... and for the establishment or maintenance of any [library] reading room....” (40:3)<sup>[2]</sup>
- “A town in which cemetery commissioners are chosen may receive bequests for maintaining cemeteries or cemetery lots....” (114:25)

## Trust Funds, Grants and Other Special Funds

- “A town may establish and maintain public libraries for its inhabitants ...and may receive, hold and manage any gift, bequest or devise therefore.” (78:7)
- A board or officer of a city or town “may accept grants or gifts of funds from the federal government, a charitable foundation, a private corporation, or an individual, ...the commonwealth, a county or municipality [for educational or other specified purposes]. (44:53A)

## Defining Key Terms

In managing trust funds, a treasurer will encounter numerous legal terms relating to trusts. The following, including definitions from *Black's Law Dictionary*, 7<sup>th</sup>. Ed., will assist in interpreting the meaning of these terms:

- **Bequest** Property, (usually personal property other than money) disposed of in a will.
- **Beneficiary** One designated to receive something as a result of a legal arrangement.
- **Custodian** One who exercises a fiduciary responsibility to guard and care for property absent a trustee's right to dispose of it.
- **Devise** Property, (usually real property) disposed of in a will.
- **Donation** A gift.
- **Donative Trust** A trust requiring no payment of consideration by a beneficiary.
- **Donee** One to whom a gift is made.
- **Donor** One who gives something without receiving consideration from the transfer.
- **Gift** The act of voluntarily transferring property to another without consideration.
- **Settlor** A person who makes a settlement of property; esp., one who sets up a trust.
- **Testamentary** Pertaining to a will or testament.
- **Trust** A fiduciary relationship regarding property and subjecting the person with title to the property to equitable duties to deal with it for another's benefit.
- **Trustee** One who, having legal title to property, holds it in trust for the benefit of another and owes a fiduciary duty to that beneficiary.
- **Trust Fund** The property held in trust by a trustee.

## The Doctrine of Cy Pres

If a treasurer determines that the designated purpose of a trust fund is no longer feasible, the treasurer should consult with the municipality's legal counsel about invoking the *cy pres* doctrine.

## **Trust Funds, Grants and Other Special Funds**

Under this doctrine, if a trust's purpose cannot be accomplished because circumstances have changed after the trust was created or for any other reason, a court may alter specific provisions of the trust, so long as the alteration enables attainment of the general objective of the person who created it.

### **Administration of Trust Funds**

The General Laws of Massachusetts include a number of provisions governing the administration of trust funds and assigning administrative responsibility to several parties. For example:

#### **Board of Commissioners of Trust Funds**

“Any city or town, except Boston, may create a board of commissioners of trust funds, consisting of three persons who shall have the management of all trust funds given or bequeathed for the benefit of the town or the inhabitants thereof, unless the donor in making the gift or bequest shall otherwise provide. In cities the commissioners shall be appointed by the mayor and confirmed by the council. In towns they shall be elected in the same manner as other town officers.” (41:45)

“The said board of commissioners shall, so far as consistent with the terms of the trusts, manage and control the same, and distribute the income in accordance with the terms of the respective trusts. The board shall keep a record of its doings, and at the close of each financial year shall make a report to the town, showing the total amount of the funds, and their investments, receipts and disbursements on account of the same, setting forth in detail the sources of the receipts and the purposes of the expenditures.” (41:47)

When a town has more than 5,000 residents and has not created a board of commissioners of trust funds, authority over trust funds rests with the town meeting.

#### **The Board of Selectmen as Trust Fund Commissioners**

“If a town having less than five thousand inhabitants votes to accept this section, the board of selectmen of such town shall thereafter have all the powers and duties of commissioners of trust funds, as provided in sections forty-five and forty-seven, until such time as the number of inhabitants of said town shall exceed five thousand.” (41:45A)

#### **Role of the Treasurer**

“The town treasurer shall be the custodian of all funds and securities of such trust funds, shall invest and reinvest them and expend therefrom monies as directed by the commissioners. The treasurer shall furnish a bond satisfactory to them for the faithful performance of his duties.” (41:46)

The treasurer's bond “shall cover the duties of the treasurer with respect to trust funds...which are in his custody by virtue of his office, and any such funds, for the purposes of said bond, shall be deemed to be public funds.” (41:35)

#### **The Treasurer and the Trust Fund Commissioners**

Although the treasurer is the “custodian” of trust funds (41:46), the treasurer must “invest and reinvest them *as directed by the [trust fund] commissioners.*” (Emphasis supplied.)

## **Trust Funds, Grants and Other Special Funds**

Notwithstanding, Ch. 44 §54 sets out rules and provisions controlling the investment of trust funds. The treasurer should advise the commissioners about the requirements of this statute and should timely notify them of any investment instruction which would contravene it. The treasurer should always be willing to share his or her financial expertise with the trust fund commissioners.

### **Cemetery Commissioners and Perpetual Care Funds**

A town with cemetery commissioners may receive gifts for maintenance of cemeteries and cemetery lots. These gifts must be turned over to the treasurer and maintained in a “perpetual care fund,” separate from other accounts of the town. The treasurer must invest perpetual care monies in accordance with the specific instructions of the donors. If the donors gave no investment instructions, the treasurer must invest the monies as directed by the cemetery commissioners. (114:25)

### **Library Trustees and Gifts to Libraries**

A town that appropriates money for the support of a free public library must elect a board of library trustees. (78:10) The library trustees may accept gifts of money and property for the library's use. Such monies must be turned over to the treasurer for deposit in a separate account. These monies must be administered by the library trustees “in accordance with the provisions of [the] gift....” (78:11)

### **Municipal Trust Funds when the Principal is not in the Custody of the Community**

If a gift of money is made, not to a municipality, but to some person or entity in trust for the benefit of the municipality, the municipality may accept the gift, pursuant to its terms, and use the proceeds for the intended purpose(s).

## **Investment of Trust Funds in the Custody of the Treasurer**

Unless otherwise provided or directed by the donor, trust funds must (a) be placed at interest in savings banks or trust companies, (b) invested in a combined investment fund, such as the Massachusetts Municipal Depository Trust (29:38A), or (c) invested in bonds or notes which are legal investments for savings banks. (44:54) Cities or towns with a fund aggregate in excess of \$250,000 may also invest such funds in securities which are legal for the investment of funds of savings banks, provided that (a) not more than 15% of such trust monies shall be invested in bank or insurance company stocks and (b) not more than 1½% of such monies shall be invested in the stock of any one bank or insurance company.

The Massachusetts Legal List, maintained by the Commissioner of Banks, sets out a list of legal investments for savings banks. The Legal List is published every year and is available at the State House Book Store. Unfortunately Chapter 44 § 54 has not been updated to reflect the fact that the term “securities which are legal for the investment of funds of savings banks” is archaic and the Legal List is very limited. Many of the banks and investment companies in Massachusetts provide trust fund investment services. Investment options available range from simple money market accounts to active investment management of stock and bond portfolios consisting of Legal List investments.

### Suggested Trust Fund Policies

Trust fund commissioners should meet with the local treasurer to draw up a general policy statement that clearly establishes policies and principles for the management, control, and custody of trust funds. Following are example elements of a sound policy statement:

1. All trust funds and gifts shall be held, administered, and invested in accordance with wills, testaments, or other documents, stating the terms of the respective gifts and bequests.
2. All trust funds and gifts shall be held, administered, and invested in strict accordance with all of the various General Laws governing such funds.
3. A permanent file shall be established and maintained which contains copies of all wills and other documents that elucidate the terms of any gift made to the municipality or trust established for the municipality's benefit.
4. Original stock and bond certificates shall be kept in a safe deposit box.
5. Trust funds and gift monies may be pooled for the purpose of investment, so long as the principal, interest, and expenditures are clearly accounted for separately.
6. Unless otherwise specified by the donor, all income received should be segregated in a separate income account on a regular basis. If so provided in the trust instrument, earned interest shall be added to, and become part of, the income available for appropriation or expenditure.
7. Trust fund commissioners shall review investments at least annually and report to the treasurer, in writing, any changes involving reinvestment of funds. When possible under the terms of relevant wills, the treasurer shall combine and consolidate principal sums and income received for like purposes.
8. A report of gift and trust funds shall be prepared annually. The report shall: (a) contain a summary of all funds, (b) identify the type of each investment, and c) include a schedule of balances and income. This schedule should state the balances forward and break down (a) all bequests and gifts received, (b) all transfers and expenditures made, and (c) all balances at the end of the period for which the report is made.
9. The treasurer shall apprise trust fund commissioners of changes in the general laws relating to trust funds. The treasurer shall also make sure that trust funds have been properly accepted.

### Special Revenue Funds

Where funds are restricted and earnings must be used for governmental purposes, they are classified as special revenue funds. The following list enumerates and discusses some of the additional, special funds expressly permitted by Massachusetts' law. The treasurer is the custodian of these funds and may invest these special funds in combination with other trust funds so long as the governing statute expressly permits. The accountant, however, must maintain and separately record entries for each individual fund.

## **Trust Funds, Grants and Other Special Funds**

### **Stabilization Fund**

Under Chapter 40 §5B, a community may establish one or more stabilization funds for different purposes by a two-thirds vote of its legislative body. It may amend the purposes of those funds at a later time in the same manner. Appropriations into ~~and from the funds require a two-thirds vote of the legislative body.~~

In addition, under Ch. 59 §21C, a city or town that has a Proposition 2 1/2 override approved by its voters for the purpose of making appropriations to any stabilization fund must now allocate or dedicate the additional levy capacity resulting from that override to the same purpose in subsequent years. Ordinarily money from an override is only earmarked for the stated purpose in the fiscal year in which the override is effective. Voters may, however, approve a change in the purpose for which the additional levy capacity can be used in future years.

Any stabilization fund pre-existing the change in the law in 2003 should continue to be treated as a reserve for any lawful purpose, ie. a “general” stabilization fund. A city, town, or district can reallocate or earmark all or part of its balance to any new stabilization fund or funds by a vote to transfer money.

The treasurer, as custodian may invest fund monies in national, savings, or cooperative banks. Massachusetts trust companies, federal savings and loan associations located in Massachusetts, or legal investments for savings banks in Massachusetts. Ch 40 §5B which authorizes stabilization funds does not expressly allow fund monies to be deposited into the Massachusetts Municipal Depository Trust (MMDT); however, the legislation establishing the MMDT (29:38A) was drafted sufficiently broadly to permit investment of stabilization funds into the trust.

cIt cannot be put into the general fund. The treasurer may pool monies from all stabilization funds for investment purposes, but the accounting officer must account for them separately in the general ledger and allocate earnings proportionally to each fund.

Annual appropriations to all stabilization funds are not limited, and there is no cap to how much a community can have in the funds.

### **Pension Reserve Fund**

In 1988, the State Legislature finally recognized that it was imperative to fund the unfunded pension liability which was rapidly growing and threatening state and municipal bond ratings throughout the state. The future financial stability of the Commonwealth and its cities and towns was at stake. A forty year plan was put into place whereby bi-annual actuarial studies of the retirement systems, with off year updates were required. Based on these studies and funding schedules derived from them, governmental entities were required each year to remit to their Retirement Board the appropriate sum needed to meet projections to fully fund the retirement program by 2028. Retirement Boards are charged with investing these monies in a diverse portfolio designed to protect the assets while at the same time increasing the value of the Retirement Board’s assets.



## **Trust Funds, Grants and Other Special Funds**

Towns may belong to County or Regional Retirement Systems. The County or Regional Retirement Boards assess each town its apportioned share of the County or Regional costs. These funds are transferred to the County or Region and remain under their jurisdiction.

Since most retirement boards tailor their payment schedules to fund the system earlier than 2028 if investments make sizeable gains or the community is able to pay more than the yearly assessment, there is not much need for municipalities to stash money away in the Pension Reserve Fund allowed by statute. A few wealthy communities have already fully funded their retirement systems and are only required to pay annual normal costs.

Should such a pension reserve fund exist, these are the parameters under which it must be held. Any year's appropriation may not exceed 5% of the previous year's levy, and the aggregate amount in the fund at any time may not exceed 5% of the equalized valuation of the city or town. All interest earned on fund monies becomes part of the fund. The treasurer, as custodian, may invest fund monies "in national banks or invest the proceeds by deposit in savings banks, cooperative banks or trust companies organized under the laws of the commonwealth, or invest the same in such securities as are legal for the investment of funds of savings banks under the laws of the commonwealth or in federal savings and loan associations situated in the commonwealth or may participate in the Pension Reserve Investment Trust (PRIT) Fund in accordance with Ch. 32 §22(8)." (40

### **Unemployment Compensation Fund**

To provide for the anticipated costs of funding reimbursements to the Commonwealth for unemployment compensation benefits under the provisions of Chapter 151A, municipalities may appropriate monies into an unemployment compensation reserve fund. Any year's appropriation may not exceed one tenth of 1% of the equalized valuation of the city or town, and the aggregate amount in the fund at any time may not exceed 1% of that equalized valuation. All interest earned on fund monies becomes part of the fund. The treasurer, as custodian, "may deposit or invest fund monies in such manner as may be legal for other city, town or district funds under the laws of the commonwealth including, without limitation, the Massachusetts Municipal Depository Trust." (40:5E) See Chapter 7 under "Unemployment Compensation (151A:14A)" for information on the purpose, limits, and use of unemployment compensation benefits.

### **Scholarship Fund or Education Fund**

Municipalities, through acceptance of Ch. 60 §3C, may establish a scholarship fund to provide educational financial aid to deserving city and town residents and to establish a local educational fund to provide supplemental educational funding for local educational needs or to provide funding for existing adult literacy programs. Communities establishing such funds may designate a place on their property tax bills and/or motor vehicle excise bills, or upon a separate form enclosed with those bills, whereby the taxpayers can voluntarily check off, donate and pledge an amount to be deposited into the scholarship fund and/or education fund. Donations increase the overall amount due. The treasurer, as custodian, must invest such funds at the direction of the board of commissioners of trust funds or other trust fund authority. All interest earned on fund monies becomes part of the fund. The scholarship committee or education fund committee, established under the act, shall select the recipients of and amounts of financial aid from the scholarship fund and educational fund. The

## **Trust Funds, Grants and Other Special Funds**

scholarship committee may distribute monies from both the interest and principal of the fund, without further appropriation, and must notify the treasurer, at least annually, of the amount that will be authorized for distribution in order that the monies may be made available in a timely manner. (60:3C)

### **Elderly and Disabled Taxation Fund**

Municipalities, through acceptance of Ch. 60 §3D, may establish an elderly and disabled taxation fund to defray the real estate taxes of elderly and disabled persons of low income. Communities establishing such funds may designate a place on their property tax bills and/or motor vehicle excise bills, or upon a separate form enclosed with those bills, whereby the taxpayers can voluntarily check off, donate and pledge an amount to be deposited into the elderly and disabled taxation fund. Donations increase the overall amount due. The treasurer, as custodian, must invest such funds at the direction of the board of commissioners of trust funds or other trust fund authority. All interest earned on fund monies becomes part of the fund. The taxation aid committee, established under the act, must adopt rules and regulations to carry out the provisions of the act and to identify the recipients of aid from the fund. The fund, together with accrued interest, may be expended without further appropriation.

### **Law Enforcement Trust Fund**

Proceeds from the sale of property seized from illegal drug-related activities may be deposited to a Law Enforcement Trust Fund and expended to defray certain qualified law enforcement costs as outlined in Ch. 94C §47. The police chief may authorize expenditures without further appropriation.

### **Other Special Revenue Funds:**

- Ambulance receipts reserved fund (40:5F)
- Beach & pool receipts reserved fund (40:5F)
- Bond proceeds fund (44:20)
- Certain insurance proceeds fund (up to \$20,000) (44:53)
- Conservation fund (40:8C)
- County dog fund (140:147A,172)
- Golf course receipts reserved fund (40:5F)
- Health claims trust fund (32B:3A)
- Highway & water pollution grants fund (44:53)
- Law enforcement trust fund (94c:47)
- Lost books/industrial arts supplies fund (44:53)
- Municipal buildings trust fund (40:13)
- Off-street parking receipts fund (40:22B,22C)
- Parking meter fees fund (40:22A)

## Trust Funds, Grants and Other Special Funds

- Recycling commission fund (40:8H)
- Sale of real estate fund (44:63)
- Skating rink receipts reserved fund (40:5F)
- Waterways improvement fund (40:5G & 60B:2(i))
- Weights & measures violations civil citations fund (98:29A)
- Wetlands protection fund (131:40)
- Workmen's compensation insurance fund (40:13A)

### Accounting for Trust Funds

When accepting gifts or trust funds, the donor should be issued a receipt, which becomes the original source document for an audit trail. The appropriate department benefiting from a gift should acknowledge its appreciation by a written acceptance that may be used for tax purposes. A trust fund which is to be administered by the Trust Fund Commissioners must be accepted by Town Meeting, or City Council.

The Treasurer must record the receipt of a gift or trust in the cashbook so that notification may be properly transmitted to the accountant who will allocate the gift or trust as expendable or non expendable. The accountant must create a permanent record of all transactions concerning donations and trusts.

To provide an adequate audit trail of trust fund disbursements, the treasurer must process them by vendor warrant. The warrant process should also acknowledge any negative earnings or losses in net asset value.

Treasurers' trust fund records must include a subsidiary ledger that documents all income and expense information about each trust fund. Most investment institutions offer pooled accounts and provide individualized earnings reports that simplify the book to broker reconciliation process as long as the records clearly identify expendable and nonexpendable monies within each fund. On a monthly basis, the treasurer should report all interest earned on trust funds to the accounting officer and reconcile all trust fund records with the accounting officer.

### Federal and State Grants

The federal and state governments give monetary assistance to cities and towns through numerous grant programs. Two particularly well known examples include Community Development Block Grants and Chapter 90 Highway Grants. The Commonwealth distributes monies to cities and towns for transportation purposes through the Chapter 90 grant program, funded by the Legislature with the enactment of transportation bond bills. The federal government distributes Community Development Block Grants to promote the development of viable urban communities within the commonwealth, pursuant to sections 300, *et seq.*, of the Omnibus Budget Reconciliation Act of 1981.

## **Trust Funds, Grants and Other Special Funds**

### **Accounting for Grants**

Upon a municipality's receiving a grant, its finance officials should obtain a copy of the grant document and familiarize themselves with its accounting and financial reporting requirements. Subsequently, they must set up whatever bank accounts and subsidiary records that are mandated by grant agreement.

In administering a grant, the finance officers must maintain the necessary accounting and fiscal records to properly record the receipt, expenditure, and current balances of the funds received from the grantor. Upon the culmination of the grant program or activity, they should maintain records showing the ultimate disposition of all grant monies.

Treasurers, in their role as custodians of all funds, including grants, should pay particular attention to depository and investment requirements. Grant agreements generally include a requirement to maintain a separate accounting for the grant program. In order for the treasurer to pool grant monies for investment purposes, the accounting officer must maintain a separate accounting of those monies. If so required by a grant agreement, the treasurer must segregate grant monies, depositing them into separate checking accounts.

Interest earned on grant funds stays with and becomes part of the grant only if expressly specified in the grant agreement. Otherwise, these monies must be deposited into the municipality's general fund.

Overall, grantees must be vigilant in complying with all grant provisions and in documenting their compliance. Otherwise, upon a final audit, the municipality might be required to rebate misapplied or unsubstantiated amounts.

### **Revolving Accounts**

The General Laws also permit cities and towns to establish revolving accounts, whereby revenues from a specific service are deposited into the account and subsequently expended, without appropriation, to support the particular service.

The Departmental Receipts Revolving Fund, authorized by Ch. 44 §53E½, constitutes a sort of hybrid revolving fund, because the appropriating authority retains some control over spending purposes and levels. The legislation stipulates that each departmental revolving fund must be re-authorized each year at annual town meeting or by city council action and that a limit on the total amount that may be spent from each fund must be established at that time. The aggregate of all revolving funds may not exceed 10% of the amount raised by taxation by the city or town in the most recent fiscal year, and no more than 1% of the amount raised by taxation may be administered by a single fund. Wages or salaries for full-time employees may be paid from the revolving fund only if the fund is also charged for all associated fringe benefits.

Massachusetts law permits a variety of other, particular revolving funds for specific, municipal programs. The more general departmental revolving fund may be implemented in addition to or in conjunction with these other statutory revolving funds, provided that the departmental revolving

## Trust Funds, Grants and Other Special Funds

fund does not conflict with provisions of the other revolving funds. Examples of existing, statutory revolving funds include:

- Adult/continuing ed./school property revolving fund (71:71E)
- Arts lottery council money revolving fund (10:58)
- Community school programs revolving fund (71:71C)
- Culinary arts program revolving fund (71:17A)
- METCO reimbursement revolving fund (71B:12,12A)
- Non-resident students' tuition revolving fund (71:71F)
- Off duty or special work detail revolving fund (44:53C)
- Overlay account revolving fund (59:25,70A)
- Parks and recreation revolving fund (44:53D)
- Performance bond forfeitures revolving fund (41:81U)
- Police special details revolving fund (44:53C)
- Reimbursement conservation land debt revolving fund (132A:11)
- School athletic fund revolving fund (71:47)
- School day-care receipts revolving fund (71:26C)
- School E&D revolving fund (70:11)
- School lunch fund revolving fund (548 of Acts of 1948)<sup>3</sup>
- School rental receipts revolving fund (40:3)
- Tuition for state wards revolving fund (76:12B)
- Vocational ed. program receipts revolving fund (74:14bB)
- Zoning/planning board consultants revolving fund (44:53G)

## Student Activity Accounts

The sound management of Student Activity Accounts for School Departments is most important. A municipal treasurer should work with school business offices to make sure that proper procedures are followed. The safety of student activity money as well as the reputations of town and school officials is at stake. Chapter 71, Section 47 of the General Laws spells out the most straight forward method of dealing with these monies, examples of which are proceeds from yearbooks, class proms, plays, concerts, and field trips. The money is generally collected from students, parents, or the public and used for specific student activities.

## Trust Funds, Grants and Other Special Funds

The entire statute may be found at the [mass.gov/legislature/general laws](http://mass.gov/legislature/general_laws) website. The MASBO (Massachusetts School Business Officials) website has a manual on managing Student Activities Accounts. It can be found at [masbo.org](http://masbo.org). From the home page, click on “Bookshelf” and then click on Financial Resource Management. The section on Cash Management, Investments, and Debt Management contains the manual.

The key paragraphs of Chapter 71, Section 47 which relate to Student Activities Accounts are as follows:

The school committee of a city, town or district may authorize a school principal to receive money in connection with the conduct of certain student activities and to deposit such money, with the municipal or regional school district treasurer, into an interest bearing bank account, hereinafter referred to as the Student Activity Agency Account, duly established by vote of the school committee to be used for the express purpose of conducting student activities. Interest earned by such Student Activity Agency Account shall be retained by the fund and the school committee shall determine for what purpose such earnings may be used. In addition to such Student Activity Agency Account, the school committee may authorize the municipal or regional school district treasurer to establish a checking account, hereinafter referred to as the Student Activity Checking Account, to be operated and controlled by a school principal and from which funds may be expended exclusively for student activity purposes for the student activities authorized by the school committee. Such account shall be used for expenditures only and funds received for student activities may not be deposited directly into such account.

The school committee shall vote to set the maximum balance that may be on deposit in such Student Activity Checking Account. The principal designated to operate and control such Student Activity Checking Account shall give bond to the municipality or district in such amount as the treasurer shall determine to secure the principal’s faithful performance of his duties in connection with such account. To the extent that the funds are available in such Student Activity Agency Account, funds up to the maximum balance set by the school committee shall be transferred from the Student Activity Agency Account through the warrant process to initially fund such Student Activity Checking Account.

Periodically, to the extent that funds are available in such Student Activity Agency Account, the municipal or regional school district treasurer shall reimburse such Student Activity Checking Account, through the warrant process, to restore the limit set by the school committee. The principal shall adhere to such administrative procedures as the municipal or regional school district treasurer or accountant may prescribe. There shall be an annual audit of the student activity funds which shall be conducted in accordance with procedures as agreed upon between the school committee and the auditor based upon guidelines issued by the department of education.

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<sup>11</sup>For the purposes of Ch. 40, Section 1 of that chapter states, “Except as otherwise expressly provided, cities shall have all the powers of towns and such additional powers as are granted to them by their charters or by general or special law, and all laws relative to towns shall apply to cities.”

## Trust Funds, Grants and Other Special Funds

<sup>[2]</sup>*Ibid.*

<sup>[3]</sup>As amended

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## **Chapter 7**

# **Payroll**

### **Responsibility/Overview**

The treasurer possesses statutory responsibility to pay all bills and to account for all monies belonging to a municipality. Consequently, the treasurer generally inherits the obligation to prepare municipal payrolls, a responsibility that entails maintaining payroll records and complying with federal, state and local reporting requirements. Although a different officer or department in some municipalities administers the payroll, this chapter is written from the perspective that the treasurer possesses this responsibility. In communities in which some other officer or department performs the payroll function, references to the treasurer in this chapter should be read to include the words, “or other officer in charge of payrolls for the municipality.”

For payroll administration purposes, the treasurer should be familiar with the following sections of the General Laws:

1. Treasurer’s duties and bond requirements. (41:35)
2. Compensation for:
  - elected and appointed officials and all non-union, non-classified employees. (41:108)
  - classified appointed officials and employees. (41:108A)
  - union employees. (150E:7)
  - civil service employees (roster requirement). (31:71)
  - special detail or off-duty employees. (44:53C)  
(See also IGR 80-3, pp. 7-26 & 7-27.)
  - disability income (police and fire in lieu of workmen’s compensation). (41:111F)
  - worker’s compensation. (152:69)
  - wages due upon death. (41:111I)
  - vacation pay due upon retirement. (41:111E)
3. Payroll administration issues and requirements:
  - timeliness of payments and provisions for cashing checks. (149:148)
  - information required on payroll. (41:42)
  - oath to payroll by department head. (41:41)



- penalty for noncompliance. (41:43)
- delivery of paychecks to department heads. (41:41A)
- direct deposit to financial institution. (41:41B)
- prepaid vacation pay. (44:65)
- deferred compensation. (44:67; 29:64B)
- IRAs. (44:67A; 29:64C)

A later section of this chapter deals with statutory provisions relating to various withholdings from wages.

## Enrolling a New Employee

A treasurer should take the necessary steps to gather the requisite documentation *prior* to a new employee's appearing on a payroll warrant. These steps might include:

1. Establishing a requirement that all department heads timely notify the treasurer of the hiring of a new employee by completing a *New Employee Form*, or other similar form
2. Requiring all new employees to provide a copy of their Social Security cards to enhance correct wage deducting and reporting.
3. Sending to all departments a *New Employee Packet* for their new employees to complete. This packet should include:
  - *Form I-9*. The 1986 Immigration and Reform Act seeks to reduce illegal alien migration by eliminating employment as an enticement for unauthorized persons to enter the United States. To accomplish this, the act imposes a responsibility on all employers to provide documentation confirming that their employees are eligible to work in the U.S. and that their identities match the information on their employment authorization documents. Employers must also require their employees to fill out a *Form I-9* within 3 business days of commencing employment (or on the 1<sup>st</sup> day of employment if a job will last less than 3 days). Employees must also submit the appropriate identity and employment eligibility documents. The treasurer should retain copies of these identity documents with the *Forms I-9* in a separate file.
  - *Form W-4/M-4*. All new employees must complete a *Form W-4* for federal tax withholding purposes. Any employee who undergoes a pay lapse for a period greater than 2 weeks, such as for an unpaid leave of absence, must fill out a new *Form W-4*. All new employees must fill out a *Form M-4*, as well, for state income tax withholding purposes unless they choose to claim the same number of exemptions for both state and federal income taxes, in which case they need only to complete a *Form*

## Payroll

W-4. For each newly hired employee, the treasurer must send, for child support enforcement purposes, either the employee's name and Social Security number or a copy of the employee's *Form W-4* to the Child Support Enforcement Division of the Department of Revenue within 14 days of the commencement of employment. (P.O. Box 7032, Boston, MA 02204; Web site [www.dor.state.ma.us/](http://www.dor.state.ma.us/); Fax: 617-887-5049)

- For any employee who claims more than 10 withholding allowances, or who claims "exempt," the Treasurer must include a copy of the *Form W-4* with the next remittance of *Form 941* to the IRS Service Center.
- *Form W-5*. An employee who is eligible for the "Earned Income Credit," a refundable federal income tax credit for low-income working individuals and families, must fill out a *Form W-5*, instead of a *Form W-4*.
- Retirement Forms. Federal law adopted in 1990 requires that all employees be covered by some type of retirement plan. The options are: The Massachusetts Retirement System under the Board serving the governmental entity where the employee works, the Federal Social Security Retirement Plan (FICA), or a 457 Deferred Compensation Plan.
- The Massachusetts Retirement laws leave it up to the Retirement Board serving a municipality to determine eligibility for their system. In general, all full time employees must belong, but the minimum number of hours for membership varies from system to system. Municipalities do not offer social security to employees who are eligible for the retirement system.
- Eligible full-time employees must complete the new member enrollment form for retirement benefits in their respective municipal, county or regional retirement system and must supply copies of their birth certificates. If they have served in the military, that information should also be noted on the enrollment form and the employees should provide a copy of their discharge papers (*Form DD-214*). Effective January 1, 2005, new employees must also complete a new federal form, "Statement Concerning Your Employment in a Job Not Covered by Social Security." A signed copy of this form should be forwarded to the appropriate retirement system, and another copy should be kept on file in the office. For new employees, most retirement systems currently withhold 9% of employees' regular compensation, up to \$30,000.00 annually, with an additional 2% withheld on any regular compensation exceeding that amount. If the new employee has been previously employed in a Massachusetts state or local job and was a member of the Massachusetts Retirement System, then the withholding amount may be 5 %, 7 %, 8 % or 9 %. (See also Chapter 8 on Retirement.)
- FICA (Federal Insurance Contribution Act). FICA is an acronym for the "Federal Insurance Contributions Act," a federal government insurance

program designed to help retired and disabled persons to pay their living expenses.

- FICA withholdings are composed of two parts. For the section known as Social Security, 6.2% of the employee's pay is deducted from all earnings up to a specific earnings ceiling, which is modified each year by the Social Security Administration. In 2016, that earnings ceiling was \$118,500. Social Security coverage is voluntary for local governmental employers who are members of a public retirement system that meets the minimum benefit requirements established by the Internal Revenue Service. However, their participation in Social Security requires a written agreement between the state and the Social Security Administration. Such an agreement must comply with the provisions of Section 218 of the Social Security Act and is therefore designated a "*Section 218 Agreement*." In general obtaining such a 218 agreement is difficult as a governmental entity does not want to pay into both Social Security and guarantee a defined benefit plan to an employee.
- The other part of FICA is known as Medicare. Medicare is a federal government-sponsored insurance program that provides medical insurance coverage for senior citizens. Local governmental employees hired after March 31, 1986 are generally subject to the Medicare tax, which is 1.45% of their gross pay, and which, unlike the Social Security tax, has no earnings ceiling. The assessment pertains to full-time, part-time and seasonal employees alike. A former elected official, whose original election occurred prior to March 31, 1986 and who was reelected subsequent to that date to the same or some other office within the same community, is not subject to the tax. Similarly, a worker hired prior to the March 31, 1986 date who later transfers from one department to another within the same community is not subject. However, the Medicare tax does apply to a person who transfers from one community to another. Temporary workers hired for certain emergencies and unemployed individuals participating in re-employment programs are expressly excluded from coverage.

Filing Status	Threshold Amount
Married filing jointly	\$250,000
Married Filing Separately	\$125,000
Single	\$200,000
Head of Household (With Qualifying Person	\$200,000
○ Qualifying Widow(er) with dependent Child	\$200,000

○

## Payroll

- For both the Social Security and Medicare parts of FICA, the employer is required to match all employee deductions and to remit the total amount due along with the federal withholding taxes whenever such taxes are due.
- OBRA. If the municipality does not offer Social Security as a retirement option, , and an employee is not eligible for the public retirement system, the employee must participate in a 457 Deferred Compensation Plan, an alternative to Social Security coverage as permitted by the federal Omnibus Budget Reconciliation Act of 1990 (COBRA). (29:64D) Normally, OBRA employees are part time, seasonal, or temporary.
- An OBRA employee must contribute at least 7.5% of gross compensation per pay period to the plan on a tax-deferred basis. When enrolling in the OBRA plan, employees should also complete the federal form “Statement Concerning Your Employment in a Job Not Covered by Social Security.” A copy of the completed form may be sent to the OBRA sponsor and another copy kept on file in the office. Note: No OBRA is taken from foreign country employees or from retired employees who work no more than 960 per year in a community that is a member of the same retirement system from which they retired.
- Sexual Harassment Policy. Ch. 151B §3A requires all Massachusetts employers to adopt a policy against sexual harassment and to annually provide an individual written copy of that policy to all employees. A new employee must be provided with a copy at the time of commencement of employment. The employer should obtain from the employee a written acknowledgement of receipt of the policy. If a community has a separate personnel office, the treasurer should check with that office to determine whether the dissemination of this information will be the responsibility of the personnel office or of the payroll office.
- Work Permits. No person may employ any child under the age of 16 except a child over 14 who has been granted an employment permit by the local superintendent of schools. (149:86) Students can generally acquire “work permits” through their school’s guidance office. In seeking an employment permit, a minor must present a certificate, signed by a school or family physician, or by a physician appointed by the school committee, attesting a sufficient soundness of health to perform the particular work. (149:87) An employer should not permit a minor to work until after that minor has obtained a work permit. On termination of employment, the employer must return the permit within 2 days to the superintendent of schools.
- Direct Deposit. In a municipality that has accepted Ch. 41 §41B, employees may have their wages, salary or other compensation deposited automatically into their bank accounts. Treasurers must ensure that such deposits are made in a timely manner. A treasurer

might incorporate a short trial period as part of implementing direct deposits for an employee setting up a new account to make certain that the account and routing numbers are correct. The treasurer should include a copy of a direct deposit request form in the new employee packet.

- **Insurance Information.** The treasurer should also include in the new employee packet the requisite forms for selecting health, dental, life, disability and other insurance plans available to employees, as well as forms and information about the municipality's "cafeteria plan," if the municipality offers such a plan. The included materials should also provide information about the deadlines for applying for any available municipal plans. The treasurer should make sure that any employee who decides not to participate in any municipal health or life insurance plan or cafeteria plan signs a waiver.
- **Drug Free Workplace and Substance Abuse Policies.** In a community that has adopted a Drug Free Workplace Policy and/or a Substance Abuse Policy, the treasurer should include copies of these policies in the new employee packet.
- **Other Material** – Some municipalities include other materials in their new employee packets. These materials may consist of such documents as the personnel bylaws or the forms an employee must fill out to join a credit union or to purchase savings bonds.

## **New Employee Checklist**

The treasurer should create a "New Employee Checklist" that identifies all the documents that should be contained in the new employee packet and make certain to receive from every new employee a signed receipt, acknowledging that the employee has received all the statutorily mandated information. This procedure will help to avoid questions in the future about whether a particular employee was supplied with the required information.

Upon receipt of all of the requisite forms properly filled out by a new employee, the treasurer should enter the employee into the payroll system. *Forms W-4* and *M-4* constitute the best sources from which to record an employee's name, address, Social Security number, marital status, and number of withholding allowances. The treasurer should use the pertinent other forms to set up retirement and benefit deductions.

## **Independent Contractor**

The treasurer is ultimately responsible for determining whether a newly hired person is an independent contractor or an employee. In general, an independent contractor does not take direction from the employer, is not necessarily an individual person, provides his or her own tools and materials to perform the job,



## **Payroll**

and has a finite time for the job to be completed which is indicated in the appointment or contract. This distinction between independent contractor and employee is very important, because income taxes are required to be withheld from an employee and not from an independent contractor. An independent contractor provides all of his or her benefits, and is not covered by a municipal retirement plan, social security, or OBRA. There is no health insurance, or workers' compensation given to an independent contractor. Publication 15-A, Employer's Supplemental Tax Guide, which can be downloaded by clicking on "Publications" at the web site [www.irs.gov](http://www.irs.gov), for information on how to determine whether an individual providing services is an employee or an independent contractor.

## **Senior Citizen Property Tax Work-Off Abatement**

Communities that have accepted MGL Ch 59 Sec 5K, with approval of the governing body, may establish a property tax work-off program for senior citizen taxpayers. Acceptance of the tax work-off program may be revoked, but communities must wait at least 3 years after acceptance of the statute.

1. Establishment of the work-off program establishes:
  - a. Eligible taxpayers must be over 60 years of age
  - b. Taxpayer must be the assessed owner of the property, or acquire ownership before the work is performed and the abatement applied
  - c. The maximum abatement that can be earned is \$750 per fiscal year, unless changed by local ordinance.
  - d. The rate used for the abatement should be no higher than the state's minimum wage
    - i. Compensation is exempt from state income taxes, but are computed for federal taxes, FICA and Medicare, and a W2 issued
  - e. Participation in the work-off program does not exclude taxpayers from any other tax exemptions they are eligible for under other statutes.
  - f. The board, officer or department supervising the taxpayer must certify to the assessors the hours of service performed by the taxpayer before the actual tax for the fiscal year is committed.
  - g. Earned credits are applied to the actual tax bill.
  - h. The municipal share of Social Security and Medicare taxes may be charged to the overlay, unless otherwise provided
2. Municipalities may, with the governing body's approval, adopt rules and regulations for the senior work-off program to be consistent local rules and procedures.

## **Election Workers**

Election workers are hired by municipalities to perform services at polling places in connection with all elections (national, state and local). These workers should be considered employees and payment for these services should be considered compensation and reported accordingly.

## **New Hire Reporting**

Pursuant to Ch. 62E §2, all employers, including cities, towns and districts, must report newly-hired employees, as well as independent contractors who are to be paid \$600 or more over the course of a year, to the DOR within 14 days of hire. Additional information on new-hire reporting requirements and reporting methods may be obtained on-line at [www.mass.gov/dor](http://www.mass.gov/dor). A treasurer may also file reports using paper forms, which are available on-line as well.

## **Preparation of Payrolls**

A treasurer may prepare the municipal payroll in-house, either manually or computer-assisted. Alternatively, the treasurer may contract out the work to a payroll service through the bid process. In either case, however, the treasurer is ultimately responsible for the payroll function.

The treasurer's payroll processing begins with the receipt of the payrolls, initially sworn to by the various department heads and approved by the auditor or accountant. The treasurer must enter the amount of each employee's earned wages and calculate the appropriate mandatory and voluntary deductions. Most municipalities utilize a computer payroll program specifically designed for municipal payroll needs.

Ch. 41 §42 identifies the information that must make up the content of a payroll. This information consists of each employee's (a) name, (b) title or position, (c) salary, wages or other compensation, and (d) dates of employment.

Ch. 41 §41A permits the treasurer to deliver payroll checks to department heads or their designees for distribution to the employees of their respective departments, with the approval of the mayor or selectmen. While cities and towns may vary in their distribution procedures, payroll processing must comply strictly with statutory requirements in every municipality. Importantly, the treasurer must never distribute payroll checks until after receipt of a sworn payroll and an approved, signed warrant. (41:41 & 52)

## **Payroll**

The treasurer should maintain a file that clearly lists who has been designated by each department head to accept responsibility for that department's paychecks. It may also be advisable to keep a log that each department head or designee will initial to verify that the paychecks have been picked up or distributed each pay period.

## **Deductions**

The treasurer is responsible for the administration of all payroll deductions. A payroll deduction may only be made if expressly authorized by law. Some deductions, such as deductions for tax withholdings, require no specific authorization from the employee. Other deductions, however, such as deductions for union dues, must be expressly authorized, in writing, by the employee. Payroll deductions are typically made for the following:

### **Federal Income Tax (58:28A)**

The amount of an employee's federal tax deduction is based on the employee's taxable wages, marital status, and number of withholding allowances. Therefore, since this information comes from the employee's *Form W-4*, the treasurer should make certain to have on file a current *Form W-4* for each employee. The IRS provides tax tables to assist employers in determining the correct amount to deduct from their employees' compensation for federal income taxes. (See *Circular E, Employer's Tax Guide* which is mailed to all Treasurers by the Federal Government and may also be obtained on line at [www.irs.gov](http://www.irs.gov)) Circular E is revised every January, and may even be revised more often if the federal tax tables change in mid-calendar year. Particularly useful is the table in Section 15 entitled "Special Rules for Various Types of Services and Payments," which outlines the tax treatment for certain types of wages and/or employees.

### **State Income Tax (62B:2)**

Massachusetts income tax withholding law parallels federal income tax withholding law. Correspondingly, the amount of the state income tax deduction is based on an employee's taxable wages, marital status, and number of exemptions claimed. A *Form M-4* is only necessary if an employee claims different exemptions for state income tax purposes than for federal income tax purposes. (See *Circular M, Massachusetts Income Tax Withholding Schedules* which is distributed by the State Department of Revenue)

### **Retirement Contribution (32:22)**

The percentage of an employee's regular compensation that the treasurer must withhold for retirement contribution depends on the date that employee was first enrolled in a public retirement system in the Commonwealth, as long as the employee's membership is still active and accumulated deductions have not been previously refunded to the employee. The percentages range from 5% to 9%, as

follows: 5% for an employee who was enrolled on or before January 1, 1975; 7% for an employee who was enrolled on or after January 1, 1975, but before January 1, 1984; 8% for an employee who was enrolled on or after January 1, 1984, but before July 1, 1996; and 9% for an employee who was enrolled on or after July 1, 1996. Moreover, in any community which has accepted the local option provision contained in paragraph (1)(b $\frac{1}{2}$ ) of Ch. 32 §22, for every employee who was first enrolled in a public retirement system in the Commonwealth on or after January 1, 1979, the treasurer must withhold an additional 2% of the amount of that employee's regular compensation that exceeds \$30,000. (See table, pg. 7-62.) An exception to these percentages exists in the case of teachers participating in the alternative superannuation retirement benefit program, set out in Ch. 32 §5, as amended by Ch. 68 §12 of the Acts of 1999. For these employees, the treasurer must withhold 11% of their regular compensation, pursuant to a list of participating teachers having been submitted to the treasurer by the school committee, board of trustees or other employing authority.

Ch. 35 §32A and Ch. 40 §5D require that all federal grants received by local governments be charged for pension costs incurred because of the grant. County, municipal and district treasurers must make provisions for charging federal grants for the pension costs of all active members of a retirement system whose salaries are paid from these grants. This charge is separate from the member's mandatory contribution. The Public Employee Retirement Administration Commission (PERAC) has determined that the appropriate charge for all federal grants is 9% of total grant salaries. (See IGR 90-106, in the Addendum to this manual.

### **Group Life and Health Insurance**

Municipalities which accept the provisions of Ch. 32B may provide their employees with a group life and health insurance plan. The amount withheld from an employee's compensation for participation in such a plan will depend on the plan's cost and the percentage of that cost which the municipality votes to contribute. The municipality must pay at least 50% of the life and health insurance cost under the plan and may vote to pay any amount more than that minimum, up to 90%. Different sections of Ch. 32B afford different eligibilities, rights and coverage ratios. A municipality's responsibilities regarding these variables depends on the particular sections of Ch. 32B which it has accepted.

The Massachusetts Health Care Reform Law requires that employers of more than 11 FTEs must provide a Section 125 plan to their employees to facilitate the mandatory health insurance requirement for all Massachusetts residents. Municipalities must create or amend their existing Section 125 plan to provide coverage to employees that work at least 64 hours per month. The statute does not require that an employer contribute towards the premiums for this sub-set of employees only that it provide a Section 125 plan option and elect a health insurance carrier. Additionally, Employee HIRD forms must be completed by all

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new employees that are eligible for benefits under MGL Chapter 32B or the Massachusetts Health Care Reform Law. Employer HIRD forms are also required to be submitted annually. For more information, go to the Commonwealth Connector website at [www.mahealthconnector.org](http://www.mahealthconnector.org).

Each employee eligible for insurance coverage must either (a) specify to the treasurer the particular plan desired and the identity of the employee's dependents or (b) decline insurance coverage. The treasurer must maintain good insurance records, both for employees who are covered under the municipal plan and employees who have declined coverage. Periodically, the treasurer should update beneficiary information on various benefit plans and retirement records. Well-maintained and updated records become extremely valuable when questions arise regarding insurance coverage and beneficiaries.

### **Annuities and Deferred Income**

The General Laws provide various programs which permit employees to defer certain income from taxation. Since these are in addition to the retirement plans described above, only the plans rules for amount deducted and paid apply. The plan rules, however must reflect federal regulations. Taxes are not paid on this compensation, but are deferred until the employee takes a distribution from his or her contributions into the plan. For each program, different rules apply. The treasurer should become familiar with the relevant statutes in order to understand the rules, restrictions and administrative procedures for each program. These include:

1. Individual Retirement Accounts. (44:67A)
2. Deferred compensation. (44:67) (457 Plans)
3. Tax Sheltered Annuities: (403(b) Plans)
  - a. school personnel. (71:37B)
  - b. municipal hospital employees. (40:55)

Some communities select plan administrators for IRAs and deferred compensation through competitive bids. Others utilize the state-selected carriers.

### **Workers' Compensation**

G.L. Ch. 152 provides workers' compensation benefits to employees who are injured during the course of their employment or suffer from work-related mental or emotional disabilities or occupational diseases. These benefits include weekly compensation for lost income during the periods they cannot work. Indemnity payments vary, depending on the average weekly wage of an employee and the degree of the employee's incapacitation. The statute dictates a maximum benefit of 100% and a minimum benefit of 20% of the state average weekly wage. In addition, an employer's insurer must furnish medicines and medical treatment, as

needed. The insurer must also pay for the vocational rehabilitation services of an employee deemed eligible by the Department of Industrial Accidents.

Payments under Ch. 152 are subject to neither federal unemployment or income tax, nor state income tax. They are, however, subject to Social Security and Medicare taxes to the same extent as an employee's regular wages until after the expiration of 6 months following the last calendar month in which the employee worked for the employer.

### **Lost Time Pay & Indemnification of Injured Police Officers and Fire Fighters**

Pursuant to Ch. 41 §111F, police officers and firefighters receive leave without loss of pay for any periods during which they are incapable of carrying out their responsibilities due to injuries sustained in the performance of duty without fault of their own. "Injured-on-duty pay" is exempt from both state and federal taxes.

Chapter 41 Section 100 addresses the indemnification of injured police officers and fire fighters. Rehabilitation of, medicines for and medical treatment of the injured police officers or fire fighters are the responsibility of the employer. In a city, town, or district, the board or officer authorized to appoint police officers or fire fighters shall determine whether it is appropriate to so indemnify an employee.

Police officers and fire fighters who receive a disability retirement as a result of on the job injuries also receive medications and treatment for those injuries from the community if the community has adopted Chapter 41 100 B for this responsibility.

### **Garnishments**

A garnishment is a legal or equitable procedure through which some portion of a person's earnings is required to be withheld by an employer for the payment of a debt. A person's earnings may be garnished for unpaid federal taxes and for unpaid state taxes. (26 USCA §§6321-6236; 62C:50) However, Title III of the Consumer Credit Protection Act limits the amount of an employee's earnings that may be garnished for federal tax delinquencies, and, in similar manner, Ch. 62C §55A sets out wage garnishment limits for state tax delinquencies.

**Child Support:** An employer may be required to withhold court-ordered child support from an employee's compensation and remit the withheld amount to DOR's Child Support Enforcement Division. (The withholding must begin with the first compensation payment that occurs more than 3 days after the employer receives notice of the withholding requirement and must continue until the employee leaves the employment or DOR notifies the employer to terminate the withholding. If the employee leaves the employment, the employer must notify DOR of the departure and identify the subsequent employer, if known, prior to the time that the next payment is due to DOR. A child support enforcement agency in

## Payroll

another state may request DOR to enforce a child support order issued by a court or administrative agency of that state. (119A:8)

**Delinquent Taxes Owed a Municipality:** Under the set-off provisions of Ch. 60 §93, the treasurer may withhold payment of any money payable to any person who owes taxes, assessments, rates or other charges that have been committed to the tax collector. The amount withheld may include interest and collection costs added to the original amount due. Wages of a municipal employee may be set off under this statute against delinquent amounts owed by the employee. However, the treasurer should be certain that the employee receives at least those minimum amounts required under federal and state garnishment laws, cited above.

### **Other Deductions (149: 178B):**

Treasurers need to be wary of having too many optional payroll deductions for the convenience of employees. If possible, the Treasurer should work with Town and School officials who have jurisdiction over collective bargaining so that the municipality does not agree to deductions which would be costly, time consuming, or difficult to administer.

The treasurer of a city or town that has an ordinance, by-law or collective bargaining agreement so requiring shall, and unless contrary to a by-law or ordinance the treasurer may, make deductions from an employee's salary in an amount the employee authorizes in writing for purchasing shares of, making deposits in, or repaying loans of eligible institutions. (149:178B) Eligible institutions include:

- Credit unions.
- Savings or cooperative banks.
- Trust companies.
- National banking associations.
- Federal savings and loan associations.
- Federal credit unions.
- Banking or Morris Plan companies.

Within 14 days of a deduction under this statute, the treasurer must transmit the deducted money to the appropriate officer of the financial institution for the purpose(s) specified by the employee.

A treasurer may deduct monies from the pension or retirement allowance of a retired municipal employee for deposit into a credit union specified by the retired employee in such amounts as the employee designates in writing. (41:41C)

The treasurer may make payroll deductions for the purchase of U.S. Savings Bonds. (154:8) The treasurer may also make payroll deductions for the payment, in whole or in part, of premiums on employees' group automobile and homeowner's insurance policies. (175:193R)

G.L. Ch. 180 permits payroll deductions for the following purposes:

- Union dues. (180:17A)
- United fund or community chest contributions. (180:17B)
- Teachers union or association dues. (180:17C)
- Teachers income protection insurance premiums. (180:17D)
- School nurses union or association dues. (180:17E)
- Mass. independent health agency contributions. (180:17F)
- Agency fees in lieu of union dues. (180:17G)
- Public transportation periodic passes. (180:17H)
- Health insurance premiums for members of employee associations. (180:17J)
- State teacher association contributions. (180:17I)
- Qualified state tuition program. (180:17L)

## **Reconciliation of Payroll Deductions**

The treasurer should reconcile payroll deductions at least monthly to make certain that the amounts deducted from individual employee checks equals the aggregate amount transmitted to the IRS, DOR, insurance companies, agencies and other organizations. The treasurer should also substantiate that the detailed listings balance with the actual payroll deductions. Performing bookkeeping functions carefully will help avoid making overpayments, on the one hand, and encountering the kinds of liabilities that can arise from mistakenly omitting an eligible employee from the municipality's group insurance plan, on the other.

Treasurers in smaller communities generally perform reconciliations on their own. In larger communities, though, treasurers may use payroll services that provide payroll reports with an automatic reconciliation. Utilizing such services, however, does not free the treasurer of the ultimate responsibility to verify the accuracy of those reconciliations.

## **Examples of Payroll Records to be Kept on File**

Federal and state law require that adequate payroll records be maintained on a calendar year basis, i.e., January 1<sup>st</sup> through December 31<sup>st</sup>. Failure to keep



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adequate records may subject a municipality to penalties. Free pamphlets and brochures are available from various federal and state agencies, such as the Internal Revenue Service, Massachusetts Division of Employment and Training, and the Department of Revenue that explain the various records required for each type of payroll, provide instructions for creating the required reports, and include comprehensive income tax withholding tables. Payroll forms that must be kept on file include the following:

1. **Employee Forms.**

- a. *Form I-9*, together with employee identification materials.
- b. *Forms W-4 and M-4*, signed by respective employees.
- c. Cafeteria plan records. A Cafeteria plan is a “qualified” employee benefit program offered by an employer under §125 of the Internal Revenue Code. Employees under such a plan may select the particular benefits desired. The plan must offer at least one nontaxable benefit (e.g., accident or health insurance coverage) and at least one taxable benefit (e.g., cash). Treasury regulations require that a cafeteria plan be in writing and formally adopted before the first pre-tax salary reduction. Participating employees may choose to divert a portion of their taxable salary to nontaxable fringe benefits, such as accident or health insurance coverage. They can choose only those benefits they desire and pay for them by pre-tax or after-tax salary reduction. Plans are administered under regulations issued by Congress, the Internal Revenue Service and the Department of Labor.

If an employee selects tax-exempt benefits under a cafeteria plan, Federal income tax withholding and Social Security, Medicare and unemployment taxes generally do not apply to the chosen benefits, even though the employee could have selected cash. On the other hand, if the employee chooses cash instead of benefits, all of these deductions will apply as they would to ordinary wage payments. Importantly, if a benefit is taxable outside a cafeteria plan, it continues to be taxable when provided under a cafeteria plan.

2. **Payroll Warrants.** Payroll warrants contain each employee’s name, hours worked, pay rate, gross pay, deductions and net pay. The treasurer should reconcile payroll records on a quarterly basis. Each warrant must be signed by the appropriate authority, i.e., the accountant and selectmen in towns and the auditor and council in a city or an appointee, or designee, of the approving board. Warrants are designated as permanent records on the Secretary of State’s record retention schedule. Unsigned computer records cannot constitute the only payroll record for record retention purposes.

3. **Payroll Checks and Direct Deposit Registers.** Payroll checks and direct deposit registers that disclose employees' names, payroll check numbers and net amounts paid each pay period must be retained per retention schedule.

## Reporting and Payment Transmittal Requirements

Since the payroll deductions made by a treasurer must be disbursed to a variety of governmental units and other agencies, proper reporting of these deductions is critical. Generally, municipal payroll reports provide a summary of the municipality's actual wages paid, deductions taken, and payments made for some discrete period of time, i.e., a week, month, quarter or calendar year. Payroll registers provide the primary basis for most of a treasurer's payroll reports. In carrying out reporting requirements, treasurers should pay particular attention to due dates for specific reports. Missing a due date might subject the municipality to interest and penalty assessments. Federal tax and FICA payments are particularly sensitive to timely payments, and subject to heavy fines for late filed money or reports.

### Social Security, Medicare and Income Taxes:

The treasurer must withhold monies from municipal employee compensation for Medicare, Social Security taxes and income taxes. Employers are required to match employee payroll contributions for Medicare and Social Security taxes. The treasurer must make certain that the requisite monies are deducted from payroll checks and that these monies, together with the community's Medicare and Social Security matching contributions are forwarded to the Internal Revenue Service, using *Form 941*. *Form 941* must be filed quarterly, in accordance with the following schedule:

- For the first quarter, ending March 31<sup>st</sup>                      April 30<sup>th</sup>
- For the second quarter, ending June 30<sup>th</sup>                      July 31<sup>st</sup>
- For the third quarter, ending September 30<sup>th</sup>                      October 31<sup>st</sup>
- For the fourth quarter, ending December 31<sup>st</sup>                      January 31<sup>st</sup>

### Child Support

The treasurer must transmit all monies deducted from employees' salaries pursuant to court-issued child support judgments to the Department of Revenue's Child Support Enforcement Division within 3 days of the date the employees are paid. (119A:12)

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### Financial Institutions; Credit Unions

The treasurer must transmit all monies deducted from employees' compensation for deposit into credit unions or other financial institutions within 14 days of making the deductions. (149:178B)

### Federal Tax Deposit Requirements for Employment Taxes

Employers are generally required to make periodic deposits of monies deducted from payrolls for federal employment tax purposes, including monies withheld for Federal income taxes and Social Security and Medicare taxes, regardless of how many employees an employer has. The deposit schedule for these employment taxes may be either monthly or semi-weekly, depending on the amount withheld during a four-quarter look-back period. The look-back period for any particular calendar year is the July 1<sup>st</sup> through June 30<sup>th</sup> interval which preceded that calendar year. For example, the look-back period for calendar year 2006 would be the 4 calendar quarters from July 1, 2004 through June 30, 2005.

### Making Payments Electronically or Manually

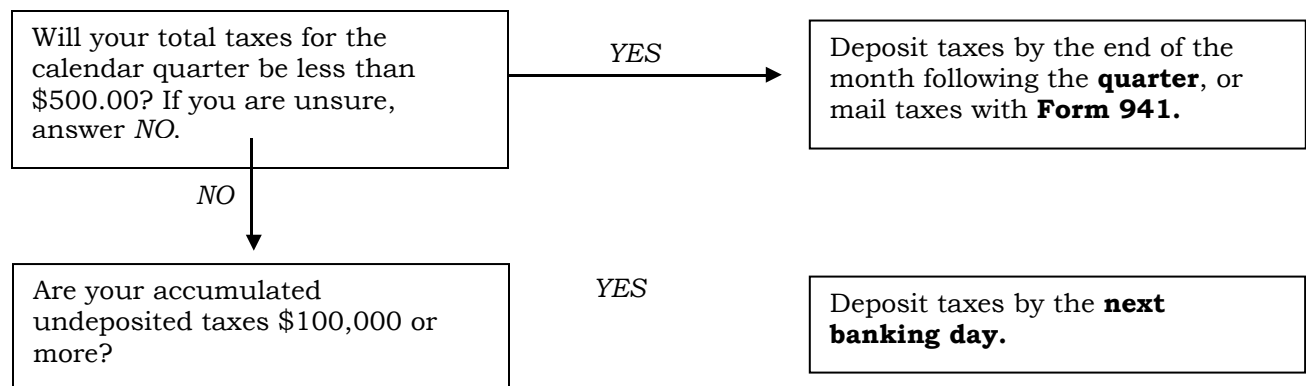
A treasurer may transmit employment tax payments on-line, using the Electronic Federal Tax Payment System (EFTPS), a convenient and secure payment method. To enroll in EFTPS, the treasurer can visit the website [www.eftps.gov](http://www.eftps.gov) or can telephone 1-800-945-8400 or 1-800-555-4477. The treasurer may also make arrangements with the municipality's main depository bank to make EFTPS payments using a deposit system set up by the bank. There is, however less control if a bank does the transmission. If the bank errs on the time schedule, or does not pay timely, the municipality must pay the fine.

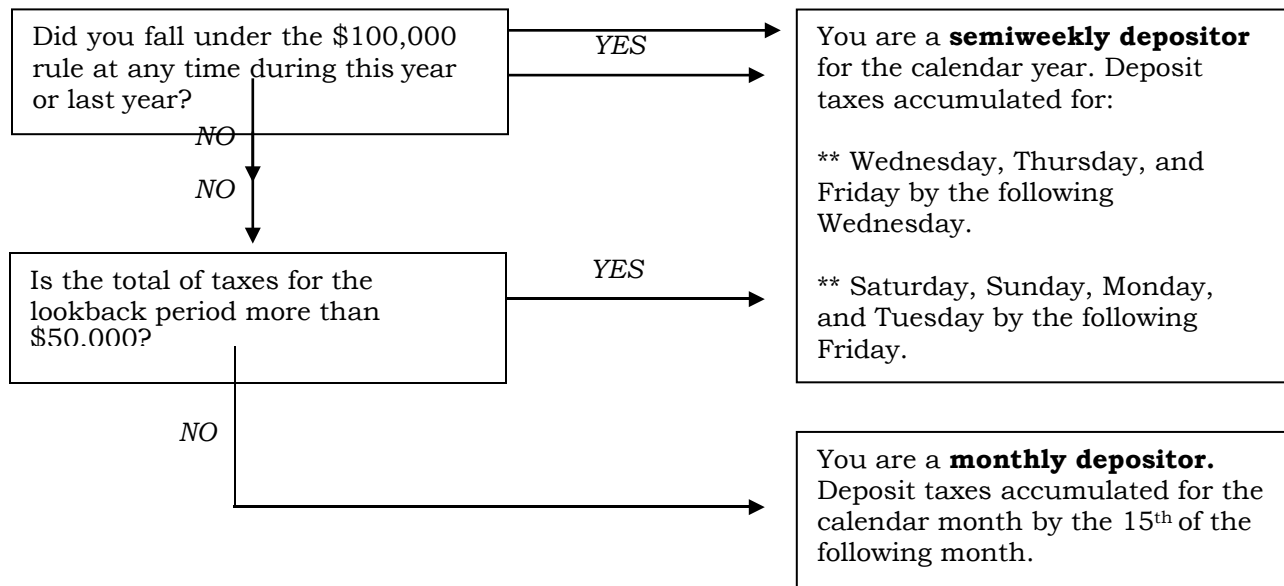
### Deposit Schedule

The following schedule illustrates the frequency with which employment taxes must be deposited:

### When to Deposit Employment Taxes

Start Here:





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### State Tax Deposit Requirements for Employment Taxes

Employers must timely transmit to the DOR all monies withheld for state employment taxes. Payments must be accompanied with a payroll tax return. The payment due date depends on the aggregate amount withheld during the calendar year. (See 830 CMR 62B.2.1.) The following table identifies the due date and the proper tax return for each of the statutory ranges of withheld amounts:

<u>Amount Withheld Per Year</u>	<u>Type of Return</u>	<u>Payment Schedule/Due Date</u>
\$100 or less.	M-941A	Annual – January 31.
\$100 – \$1,200.	M-941	Quarterly – January 31, April 30, July 31, October 31.
\$1,200 – \$25,000.	M-942	Monthly – 15 <sup>th</sup> day of the following month.
More than \$25,000.	M-941W	Weekly – third business day following the 7 <sup>th</sup> , 15 <sup>th</sup> , 22 <sup>nd</sup> , and the last day of the month.

### Filing Requirements

Reports relating to payroll deductions and payments of deducted monies must be made at different intervals, i.e., monthly, quarterly or annually, depending on the specific report and the kind of deduction.

**Monthly requirements:** The treasurer must transmit monthly to the appropriate agency monies deducted from employees' compensation for tax-sheltered annuity plans, health insurance, life insurance, savings bonds, retirement, disability insurance and union dues.

**Quarterly requirements:** The treasurer must mail or file the following reports within 30 days of the end of a calendar quarter. (For example, a payroll return for a quarter ending March 31<sup>st</sup> must be mailed or filed on or before April 30<sup>th</sup>.)

- *Form WR-1, Employer's Quarterly Report of Wages Paid.* Form WR-1 must be filed with the DOR on the 15<sup>th</sup> day of the month following the end of each calendar quarter. DOR will send the form to registered employers on a quarterly basis. The wage reporting system's purpose is to verify a person's eligibility for programs such as welfare, Medicaid, unemployment compensation and workers' compensation. In addition, the system helps to track down parents who fail to pay any child support they may owe. Requirements under this system are separate from requirements to submit income tax withholding forms. Employers also must report all newly hired employees, employees returning to the payroll and independent contractors

within 2 weeks of an employee's first day on the job. Form WR-1 may be submitted electronically by logging on to the DOR web site at mass.gov WebFile for Business.

- **Form 941.** This form must be filed with the IRS by the last day of the month following the end of a calendar quarter.
- **Multiple Worksite Report** – This is a voluntary report that an employer may file quarterly with the Massachusetts Division of Unemployment Assistance. Both employees and wages are divided into subgroups, depending upon the type of service that is provided. Some examples of subgroups might be: Education, Finance, Police, Fire, Public Works, etc. The completed report must include the number of employees and the total wages paid for each subgroup for each month of the preceding quarter. The total dollars for the quarter must agree with amount reported on the WR-1 report and other quarterly reports. The Multiple Worksite Report is due on the last day of the month following the end of each quarter (April 30<sup>th</sup> for January -March, etc.).

#### **Annual requirements:**

- **Form 5500, Report of Employee Benefit Plan.** Formerly, the treasurer had to annually file a *Form 5500* with the U.S. Department of Labor's Pension and Welfare Benefits Administration (PWBA) for every pension benefit plan, welfare benefit plan and fringe benefit plan offered by the municipality. However, the IRS suspended this filing requirement in April of 2002 for cafeteria plans, educational assistance programs, and adoption assistance programs. The suspension of the filing requirement is outlined in the IRS's Notice 2002-24. It applies to all plan years, including years prior to 2001. During the suspension period, the IRS will review reporting requirements and electronic filing options.
- **Forms W-2 & W-3.**
  - The treasurer must prepare a *Form W-2, Wage and Tax Statement*, for every person who was employed by the municipality during the calendar year and transmit that statement to the employee on or before January 31<sup>st</sup> of the following year. *Form W-2* must show the total amount of wages paid, the total Social Security and Medicare taxes withheld, and the amount of federal and Massachusetts income tax withheld for the subject year.
  - Any employer required to file *Form W-2* must also file *Form W-3, Transmittal of Income and Tax Statements*. The treasurer must send *Form W-3*, together with Copy A of each employee's *Form W-2*, to the Social Security Administration, the IRS, and the DOR. The treasurer should retain a copy of *Form W-3* for each calendar year, in addition to Copy D of each employee's *Form W-2* for that year, for at least 4 years.

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- An employer can file *Form W-3* with *Forms W-2* to the IRS and the Social Security Administration either electronically or in paper form. Paper filings must be submitted by the February 28<sup>th</sup> following the end of the calendar year. Electronic filings must be submitted by March 31<sup>st</sup>. The DOR requires employers with 250 or more employees who file electronically with the IRS to file likewise with the DOR. *Forms W-2 and W-3* must be filed with DOR by the last day of February for the preceding year. Employers with fewer than 250 employees are encouraged, but not required, to file *Forms W-2* on magnetic media.
- **Update Tax Tables and Withholding Limits.** After completing the final payroll of a calendar year, the treasurer must update the tax tables and withholding limits for state, federal, FICA and Medicare taxes for the following calendar year. The necessary information may be found in *Massachusetts Circular M*, a booklet of income tax withholding tables, available from the DOR, and *Publication 15*, also known as *Circular E, Employer's Tax Guide*, available from the IRS. The treasurer should maintain these documents as permanent records.
- **Issue Form 1099.** At the end of each calendar year, the treasurer, accountant or auditor should issue a *Form 1099 MISC* to each non-employee service provider who received \$600 or more in payments during that calendar year. Independent contractors receive a 1099. Care must be made to match the name of the contractor and FID number exactly as it is listed in federal records. Compensation paid to an employee should not be reported on a *Form 1099 MISC*, but should be reported on a *Form W-2*.

## Miscellaneous Legal Requirements Information

### COBRA

In 1986, Congress enacted the Consolidated Omnibus Budget Reconciliation Act (COBRA), which extends health benefits to former employees and their dependents, enabling these persons to temporarily continue health insurance at group rates. The law covers group health plans offered by employers with 20 or more employees in the prior year. It applies both to private sector plans and to plans sponsored by state and local governments. It does not, however, cover plans sponsored by the federal government or by certain church-related organizations.

### Covered Individual or Qualified Beneficiary

A covered individual or qualified beneficiary is any individual covered by an employer-based group health insurance plan who would otherwise lose coverage due to the occurrence of a qualifying event. Qualifying beneficiaries include:

1. Employees who have been separated from their employment position or reduced in employment hours.
2. Surviving spouses and children of deceased employees.
3. Separated, divorced, or Medicaid-ineligible spouses.
4. Children (of current employees) who would lose coverage because of age or loss of full time student status.

### **Qualifying Events**

The following are qualifying events under COBRA:

- Death of a covered employee.
- Termination of a covered employee (including dismissal for cause, but not for “gross misconduct”).
- Reduction in work hours of a covered employee which would place that employee under minimum eligibility requirements.
- Covered employee’s becoming entitled to Medicare benefits.

### **Notices under COBRA**

A treasurer must initially notify each new municipal employee and qualifying beneficiary of COBRA rights at the time the employee enrolls in a group health plan offered by the municipality. Subsequently, the treasurer must notify the municipality’s health plan administrator within 14 days of becoming aware of the occurrence of a “qualifying event.” Notification must be made to each terminated employee. Mailing such notices with a return receipt requested and saving these receipts will protect a municipality from lawsuits regarding continued health insurance coverage.

A covered individual or qualified beneficiary must notify the health plan administrator within 60 days of the occurrence of one of the following events:

1. A covered employee’s divorce or legal separation.
2. A dependent child’s ceasing to be a dependent under the health plan.

### **Continuation Coverage**

A qualified beneficiary must elect continuation coverage within 60 days of a “qualifying event” or 60 days from the time notice of that event was given, whichever is later. A beneficiary who elects continuation coverage must pay 100% of the applicable group premium. Additionally, the employer may charge up 2% of the premium amount as an administrative fee.

Continuation coverage must be available to a qualified beneficiary as follows:



## **Payroll**

- Up to 18 months for covered employees, as well as their spouses and their dependents, when workers otherwise would lose coverage because of a termination or reduction of hours.
- Up to 29 months for covered employees who are determined to have been disabled at any time during the first 60 days of COBRA coverage; this coverage applies also to the disabled employee's non-disabled qualified beneficiaries.
- Up to 36 months for spouses and dependents who face a loss of employer-provided coverage due to an employee's death, a divorce or legal separation, or certain other "qualifying events".

COBRA coverage can be ended, however, under the following circumstances:

1. Group health plan is terminated for all employees.
2. Terminated employee or qualified beneficiary fails to make required payments timely.
3. Qualified beneficiary becomes employed and covered by another health plan.
4. Qualified beneficiary becomes eligible for Medicare.
5. Former spouse remarries and becomes covered under another group health plan.

## **Conversion Option**

An employer must make a conversion option available at the end of COBRA coverage if such a conversion option is otherwise available under the group health plan. The treasurer must notify each qualified beneficiary of available conversion options during the 180 days prior to the expiration of the COBRA extended coverage.

## **Premiums**

A plan member who undergoes a qualifying event is responsible for payment of the cost of the health insurance premium. Employers may charge up to 102% of their cost, and the beneficiary may elect to pay this cost in monthly installments. For self-insured plans, the premium is generally equal to the "reasonable estimate of cost of coverage" as determined on an actuarial basis. In some cases the employer may elect to use, as the cost of the plan, the cost for a similarly situated beneficiary for the previous year, adjusted to reflect cost-of-living changes as measured by the gross national product deflator.

## **Notice of Unavailability and Notice of Termination**

Two new COBRA notification requirements became effective January 1, 2005. The first of these is the Notice of Unavailability of COBRA Coverage which must be

provided when the plan administrator receives a notice of the occurrence of a qualifying event or a second qualifying event and then determines that the individual whose coverage is affected by the event is not eligible for continuation coverage. Notice must be provided within 14 days after notice is received by the employer or administrator.

The second new notice is a Notice of Termination of COBRA Continuation Coverage. Plans must provide a written notice to qualified beneficiaries receiving COBRA of any early termination of COBRA coverage. This Notice must be provided as soon as practicable after a determination that COBRA continuation coverage will terminate.

(See Samples of Notices)

### **Veterans Benefits Improvement Act of 2004**

On December 10, 2004, the Veterans Benefits Improvement Act of 2004 was signed into law. Under one section of this act, employees who are on military leave from an employer are now entitled to the COBRA-like benefits for up to 24 months, an increase from 18 months. Accordingly, employees on military leave may now participate in their employer's health coverage for themselves and their dependents for up to 24 months, subject to being charged a premium by the employer not to exceed 102% of the cost of the coverage.

### **HIPAA**

The Health Insurance Portability and Accountability Act of 1996 (HIPAA) protects health insurance coverage for workers and their families when they change or lose their jobs. Portability under HIPAA does not mean that individuals can transfer their current health benefits, plan or policy with them when they proceed from one health plan or policy to another. Rather it means that once an individual has obtained health coverage, this coverage may be utilized to reduce or eliminate any preexisting-condition exclusion to which that individual might otherwise be subject upon moving to another employer's group health plan. Hence, HIPAA protections act to (a) limit exclusions for preexisting-conditions, (b) prohibit discrimination against employees and dependents based on their health status and (c) allow a special enrollment opportunity in a new plan to individuals in certain circumstances. When an employee leaves voluntarily or is terminated from a position, the employer must furnish the employee with a certificate indicating the length of time the employee and dependents were enrolled in the health benefit plan. The employee can then give that certificate to the new employer to demonstrate prior creditable coverage under a group health insurance plan. Furthermore, HIPAA responsibilities do not eliminate or replace employers' responsibilities under COBRA.

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Protected Health Information – In April, 2003, an additional section of HIPAA concerning Protected Health Information (PHI) became effective. Under this section of the statute, employers are required to ensure and maintain privacy requirements concerning employees' health information. Protected Health Information may not be used or disclosed except as authorized by the individual who is the subject of the information or as explicitly required or permitted by the rule. Permitted and Required Uses and Disclosures include:

- To the individual that is the subject of the information.
- For purposes of “treatment, payment and health care operations.”
- Pursuant to an authorization.
- Disclosures concerning victim abuse, neglect or domestic violence.
- Certain uses and disclosures concerning decedents
- Certain uses and disclosures for research purposes
- Uses and disclosures to avert a serious threat to public health or safety
- Disclosures for worker's compensation purposes

Employers must implement a privacy policy and appoint a Privacy Officer to deal with any grievances or concerns on the part of employees regarding any unauthorized disclosure of PHI. Employees who enroll in the municipality's health insurance group must be given written information concerning their privacy rights under HIPAA.

## **TEFRA**

The Tax Equity and Fiscal Responsibility Act (TEFRA), passed by Congress in 1982, amended the Age Discrimination in Employment Act of 1967. Section 116(b) of TEFRA requires employers to offer active employees aged 65 and over, and their spouses aged 65 and over, the same group health plans they offer to younger workers. Employers subject to TEFRA must permit employees and their spouses aged 65 and over to remain on the employer's plan as Medicare will not pay for anyone eligible for coverage under an employer sponsored plan. At such time as the employee retires, both retiree and spouse may elect Medicare if they are 65 or over. If either the employee or spouse is not 65 when the employee is retiring, they would remain on the group plan for those under 65 as an individual.

## **Unemployment Compensation (151A: 14A)**

Although municipalities may choose to self insure and not make premium payments to the Division of Employment and Training (DET) for unemployment compensation purposes, they must, nevertheless, reimburse DET for benefits actually paid by that agency to eligible workers. Municipalities may make reimbursements either by contributing a percentage of their annual payrolls,

based on their respective unemployment compensation histories, as calculated by DET, or by tendering payment on a monthly or quarterly basis, on a pay-as-you-go basis, for benefits paid by DET.

## **Family and Medical Leave Act of 1993 (FMLA)**

FMLA requires “covered employers,” i.e., employers who employed 50 or more employees for each working day during 20 or more calendar workweeks in the current or preceding calendar year, to provide up to 12 weeks of unpaid job-protected leave to “eligible” employees for certain family and medical reasons. An eligible employee must work at a worksite that employs 50 or more employees within 75 miles, and the employee must have been employed for at least: (1) 12 months (need not be consecutive); and (2) worked 1,250 hours during the previous 12-month period.

### **Reasons for Taking Leave**

An employee may take leave under FMLA for any of the following reasons: (1) birth of a child and to care for the newborn child after birth, (2) placement of a child for adoption or foster care, (3) care for a spouse, son, daughter or parent with a serious health condition, or (4) serious health condition that renders the employee unable to perform one or more of the essential functions of the job.

### **Advance Notice and Medical Certification**

An employee seeking leave under FMLA may be required to provide the employer with advance notice of a request for leave. Generally, an employee must provide at least 30 days advance notice when the request is “foreseeable.” The employer may also require an employee to provide medical certification in support of a request for leave because of a serious health condition. Further, the employer may require that employee to obtain a second or third opinion (at the employer’s expense). The employer may deny a request for leave if the employee fails to meet these requirements. Finally, an employer may require an employee who takes leave because of a serious health condition to provide a fitness report before returning to work.

### **Job Benefits and Protection**

An employer must maintain an employee on group health coverage for the duration of FMLA leave. The employee need pay only the employee’s share of the health insurance premium. If, however, the employee does not to work after FMLA leave, an employer may charge the employee for the employer’s share of the coverage during the leave. Upon the employee’s return to work, the employee must be restored to the original or an equivalent pay, benefits, and other employment terms. The use of FMLA leave cannot result in the loss of any employment benefit that accrued prior to the start of an employee’s leave.

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Employers may not interfere with, restrain, or deny an employee's exercise of any FMLA right. In addition, employers may not discharge or discriminate against any employee involved in any proceeding under or relating to FMLA.

### **Massachusetts Maternity Leave Act (149:105D)**

The Massachusetts Maternity Leave Act permits a female employee to take up to 8 weeks of unpaid leave upon (1) the birth of a child, (2) the adoption of a child under 18 years old, or (3) the adoption of a person under 23 years old who is mentally or physically disabled.

By its terms MMLA provides maternity leave to female employees only. However, providing these benefits only to female employees would, in most circumstances, constitute sex discrimination in violation of CH. 151 B. An employer who provided such leave only to female employees, and not to male employees might also violate federal prohibitions against sex discrimination, even though the employer had acted in compliance with MMLA.

To be eligible for MMLA benefits, an employee must have worked for the employer in a full-time position for at least three months or have finished a probationary period (which cannot exceed six months), and the employer must give the employee two weeks notice of (a) the departure date and (b) an intention to return to the job.

Under return to employment, the employer must restore the employee to the same position or to a reasonably similar position with the same status, pay, length of service credit and seniority.

The Massachusetts Commission against Discrimination (MCAD) enforces MMLA.

### **Fair Labor Standards Act (29 USCA §§ 201-219)**

Federal legislation, known as the "Fair Labor Standards Act" establishes minimum wages, overtime pay, record-keeping requirements and child labor standards for federal, state, and local governments as well as most workers in the private sector. While this legislation was passed many years ago, it is still extremely important to follow its requirements. The federal government has conducted audits of Massachusetts communities in recent years and fined those not in compliance.

#### **Overtime Provision and Record Keeping**

Under FLSA, employers must maintain all records pertaining to wages, hours, and other types of pay. Calculations for overtime pay must be readily available and discernable as to the makeup of the overtime rates paid. Treasurers need either to keep these records themselves, or make sure that departments involved are keeping the required detail.

FLSA legislation requires that covered employees, unless otherwise exempt, be paid not less than 1 ½ times their regular rates of pay for all hours worked in excess of forty in a workweek. Included in the overtime pay rate for FLSA must be longevity pay and other compensation which may not be included in the normal regular rate of pay. Municipalities may pay overtime after thirty-five or thirty-seven and one half hours, or other work weeks as bargained with unions. FLSA only applies to anything over forty hours, regardless of local practices or regulations. Public Works Departments and School Building Maintenance Departments need are two departments which are apt to be subject to the FLSA on a regular basis. Special provisions in the FLSA pertain to law enforcement and fire protection personnel.

### **Law Enforcement and Fire Protection Personnel under FLSA**

FLSA contains special provisions pertaining to law enforcement and fire protection personnel of state and local governments. First, it sets out an overtime exemption for such personnel in a community that employs less than five law enforcement or fire protection employees.

The legislation also permits the payment of overtime to police officers and firefighters in any municipality on a “work period” basis. A “work period” may be from seven consecutive days to twenty-eight consecutive days in length. Fire protection personnel are due overtime under a “work period” plan after they have worked 212 hours during a twenty-eight day period. Law enforcement personnel, on the other hand must receive overtime after 171 hours worked during a twenty-eight day period. For work periods of at least seven, but less than twenty-eight days, overtime must be paid when the number of hours worked exceeds the number of hours which bears the same relationship to 212 (fire) or 171 (police)\_ as the number of days in the work period bears to 28.

Overtime pay earned for certain outside details by police officers, and sometimes fire fighters often become subject to FLSA rules. The Quinn bill compensation or other education incentives as well as longevity pay are some of the types of pay which need to be included in the rate. Pay for outside details performed for the municipality (ie. for water, sewer, light, school departments, etc.) has to use the FLSA rate. Pay for outside details performed for companies or entities separate from the municipality, such as telephone companies, cable companies, shopping centers, etc. do not have to include the FLSA rate.

### **Compensatory Time**

Employers under FLSA may provide “compensatory time”, leave time earned in lieu of pay time worked beyond the forty hour standard workweek, pursuant to the provisions of a collective bargaining agreement. Compensatory time must be earned at a rate not less than one and one half hours for each hour of employment for which overtime compensation is required. The act imposes limitations on the amount of compensatory time that can be accrued. Under

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these limitations, an employee may not accrue more than two hundred forty hours of compensatory time for overtime worked unless that person is involved in public safety, emergency response, or seasonal work. In these later instances, the maximum accrual limit is four hundred eighty hours.

### **FSLA Exemptions**

The FSLA contains provisions which exempt some employees from the act. The exemptions provisions most relevant to cities and towns are those which exempt employees of public agencies who are not subject to the civil service laws of the state, political subdivision, or agency which employs them and who are either holders of public elective office or members of the office holder's personal staff, appointed by elected officials to policy making positions or who serve as immediate advisors to elected officials with respect to the constitutions or legal powers of the officeholder. The Small Necessities Leave Act

The Small Necessities Leave Act (MGL c. 149 Sec. 52D) mandates that certain employers provide up to 24 hours of unpaid leave during any twelve month period to "eligible employees." This leave is in addition to the 12 weeks already allowed under the Federal Family and Medical Leave Act. Employees are eligible for the 24 hour leave under the statute if their employer has 50 or more employees working within 75 miles of the worksite of the employee requesting the leave. In addition, the employee must (1) have been employed for at least 12 months by the employer from whom the leave is requested, and (2) provided at least 1250 hours of service for the employer during the immediately previous 12-month period.

**Allowable Reasons for Leave:** The 24 hour unpaid leave may be taken for any of the following reasons:

- To participate in school activities directly related to the educational advancement of a son or daughter of the employee, such as parent-teacher conferences or interviewing for a new school; or
- To accompany the son or daughter of the employee to routine medical or dental appointments, such as check-ups or vaccinations; or
- To accompany an elderly relative of the employee to routine medical or dental appointments or appointments for other professional services related to the elder's care, such as interviewing at nursing or group homes.

To be entitled to the leave, employees must provide notice to the employer as follows:

- If the need for leave is foreseeable, the employee must request the leave not later than 7 days in advance;
- If the need is not foreseeable, the employee must notify the employer as soon as practicable under the particular circumstances of the individual case.

To the extent possible, employees must provide written notice to the employer. If not feasible, employees may request leave orally.

## Sexual Harassment

As noted above, Ch. 151B §3A requires all Massachusetts employers to adopt a policy against sexual harassment, to annually provide an individual written copy of that policy to all employees and to review this policy with their employees on a yearly basis. All new employees should be required to sign an acknowledgment that they have received and understand the policy.

## Personal Use of Municipally-Provided Vehicles

Under the Internal Revenue Code, the personal use of a municipally-provided vehicle by a municipal employee constitutes a taxable fringe benefit. Therefore, if a municipal employee uses a municipally-provided vehicle for personal reasons, the treasurer must determine the value of that use and withhold the applicable Social Security and Medicare taxes. The treasurer must also either withhold income taxes on the value of that benefit or, alternatively, inform the employee and include the value of the use on the employee's *Form W-2*.

### Non Personal-Use Vehicles

Certain vehicles, however, are characterized as “non personal-use vehicles” by the IRS. Personal use of these vehicles is not subject to taxation as a fringe benefit. Qualifying vehicles include (a) clearly marked police and fire vehicles, (b) unmarked vehicles used by law enforcement officers, provided the officer is authorized to carry a firearm, execute search warrants and make arrests, (c) ambulances and hearses used for their specific purposes and (d) school buses.

### Calculating the Value of Personal Use of a Municipally-Provided Vehicle

To calculate the value of an employee's personal use of a municipally-provided vehicle, the treasurer must use either the lease rule, the cost-per-mile rule or the commuting value rule, as appropriate in each particular case.

- **Automobile Lease Rule.** The treasurer must determine the fair market value of the vehicle and then calculate the annual lease value using IRS *Publication 15-B*.
- **Cents-Per-Mile Rule.** The treasurer must ascertain that at least 50% of the use is business-related, that the vehicle is driven at least 10,000 miles per year and that the fair market value of the vehicle is less than \$15,300 in order to use this rule. In a qualifying situation, the treasurer must apply the cents-per-mile rate established by the IRS for the applicable year.
- **Commuting Value Rule.** The treasurer must add \$3 for each two-way commute and \$1.50 per each one-way commute to the employee's income.



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This method may be utilized only if the vehicle is owned or leased by the municipality, the employee is required to commute with the vehicle for business reasons, the municipality has a written policy permitting use of the vehicle only for commuting and minimal personal use and the employee uses the vehicle only for commuting and minimal personal use. Privacy Issues

The Massachusetts General Court has amended the Public Records Law to provide that the home addresses and home telephone numbers of municipal employees are no longer public records. Therefore, the custodian of such information must treat it as confidential information.

The treasurer's office is generally both the payroll and employee benefits office, and since this personal employee information is inevitably included on a wide variety of payroll and benefits forms it may be prudent for treasurers to adopt procedures in their offices to ensure that this information remains confidential.

### Website Sources for Payroll Forms and Information

The treasurer may obtain current payroll forms and other publications by visiting a federal or state office as well as by requesting the materials online at the following addresses:

State Forms:            Massachusetts Department of Revenue  
[www.mass.gov](http://www.mass.gov)

Federal Forms:        Internal Revenue Services online at  
[www.irs.gov](http://www.irs.gov)

The treasurer may also obtain current forms by visiting the following Websites:

[www.irs.ustreas.gov](http://www.irs.ustreas.gov)

Federal Tax Information

[www.irs.gov](http://www.irs.gov)[www.irs.gov/govt/fslg](http://www.irs.gov/govt/fslg)

Federal Tax Information for State and Local Governments

[www.mass.gov](http://www.mass.gov)

Commonwealth of Massachusetts

[www.mass.gov/legis](http://www.mass.gov/legis)

Legislature

[www.mass.gov/dor](http://www.mass.gov/dor)

State Tax Information

[www.mass.gov/dls](http://www.mass.gov/dls)

Division of Local Services

[www.dor.state.ma.us/webfile](http://www.dor.state.ma.us/webfile)

Webfile for Business (File WR1 forms, New Hire Forms, State W2 forms)

[www.comm-pass.com](http://www.comm-pass.com)

MA Procurement Information

[www.detma.org/revenue](http://www.detma.org/revenue)

Dept. of Employment and Training Revenue Service

[www.whitehouse.gov](http://www.whitehouse.gov)

White House

[www.senate.gov](http://www.senate.gov)

United States Senate

[www.house.gov](http://www.house.gov)

United States House of Representatives

[www.savingsbond.gov](http://www.savingsbond.gov)

Bureau of the Public Debt Online

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## **Chapter 8**

# **Retirement System**

Municipal treasurers are treasurers of the retirement system if their community is one of the 106 independent retirement boards statewide. Responsibilities generally include deducting employees' retirement contributions, transmitting them to the applicable retirement system, and being responsible for the cash to cover payments for retirement payroll and bill roll warrants. Public school teachers, except in Boston, receive their retirement benefits from the Massachusetts Teachers' Retirement System; other municipal employees receive their retirement benefits from their respective municipal, county or regional retirement systems.

### **Legal Foundation for Retirement System**

Chapter 32 of the Massachusetts General Laws is the law governing the State's retirement systems. An amendment to the statute formulated the Public Employees Retirement Administration Commission (PERAC) to administer and regulate all of the member pension systems. There are 106 independent Retirement systems, some run by municipalities, some by counties, regions, and some by the State. The Retirement systems are autonomous and separate from governing oversight by cities and towns. PERAC oversees the accountability, financial condition, legal compliance, rights and equities of each system.

PERAC consists of seven members, three appointed by the governor, three by the state auditor, and a final member, who acts as chairman, chosen by the other six members. Of the governor's appointees, one is the governor or the governor's designee, another is a representative of a public safety union, and the third is a person proficient in the investment of funds. Of the state auditor's appointees, one is the auditor or the auditor's designee, another is the president of the Massachusetts AFL-CIO or his designee, and the third is a representative of the Massachusetts Municipal Association. (7:49)

An executive director, selected by PERAC, plans, directs, coordinates, and executes administrative functions of the agency in conformity with the commission's policies and directives. PERAC promulgates whatever rules, regulations, directives and guidelines it deems necessary for the efficient administration of public employee retirement systems. Ch. 7 §50 sets out PERAC's powers and duties. Among those duties is investigating fraud, monitoring the earnings of disability retirees to ensure that excess earnings are recouped by the retirement systems, and evaluating disability retirees for possible restoration to active service. Treasurers should address technical questions concerning public employee retirement systems to PERAC.

Publications and pension information can be found at PERAC's website, [www.mass.gov/perac](http://www.mass.gov/perac). Since regulations and laws change frequently, it is a good idea to visit this website regularly.

## **Municipal Retirement Systems**

Each city and town retirement system must be managed and supervised by a five-member retirement board. Two separate statutes provide alternative procedures for selecting the membership of the retirement board. Under the first statute, Ch. 32 §20(4)(b), the accountant or auditor serves as an *ex officio member*. The remainder of the board consists of one member appointed by the chief executive officer, two members elected by the members and retirees of the retirement system for terms not exceeding three years, and one member, not an employee, retiree, or official of the governmental unit, chosen by the other four board members for a three-year term. The second statute, Ch. 32 §20(c), is a local acceptance provision. In communities that accept this statute, the board is made up of two members appointed by the chief executive officer and two other members elected by the members and retirees of the retirement system for terms not exceeding three years. The fifth member is appointed by PERAC after having been nominated by the other four members. However, if these four cannot agree on a nominee, each member must submit a list of three names of individuals ready and willing to serve, and the commission then appoints the fifth member from the list. This member cannot be a current or former member of the retirement system or an official of the governmental unit.

Ch. 32 §20(5) sets out the general powers and duties of municipal retirement boards.

### **Early Intervention Plan**

Ch 32 §5B requires that employers establish an early intervention plan for the formulation of programs and procedures to assist injured employees, to furnish education programs that encourage safety, and to identify workplace hazards. This statute seeks to reduce accidental disability retirements by promoting wellness and fitness activities in the workplace. The early intervention plans have proved unwieldy and expensive and are frequently not established in municipalities.

## **Funding the Pension Systems**

In general, municipal pension systems are funded by:

- Contributions from members.
- Appropriations from the municipality.
- Income from investments.

### **Unfunded Liability**

In 1987, the Pension Reform Act mandated an amortization of the state's unfunded pension liability. Each of the 106 systems was required to develop a funding schedule designed to correct years of not properly funding future pension obligations to the State, municipal, and county employees. (32:22D) These schedules are based on actuarial studies of the retirement system done bi-annually and updates done in the off years. All systems must be fully funded by 2028. When the systems are funded, they are only responsible for the yearly normal costs.

## **Retirement System**

### **Municipal [40:5D] and County [35:32A] Pension Reserve Funds**

An old statute, CH. 32 § 22, provides for a Municipal Pension Reserve Fund. Since the 1987 Pension Reform Act provides for funding the pensions system there is little need for these accounts. If this fund exists in a municipality, the treasurer is the custodian of the fund and accrued interest remains with the fund.

Counties, or regional systems where counties have been abolished, may establish pension reserve funds for county systems under Ch. 35 §32A, and they may annually appropriate to those funds an amount not exceeding 5% of the amount they raised in the preceding year from their assessments under Ch. 32 §22(7)(c). These monies must be obtained through an additional assessment upon the member municipalities.

Neither municipal nor county pension reserve funds may be expended for current pension liabilities or for other retirement board obligations without a funding schedule to amortize the unfunded liability of the system and approval by the state actuary. [32:22(6A), (7)(c) & (9); 32:22D(3)]

In addition, PERAC must annually determine the amount of each municipality's required contribution to the pension system for the fiscal year, based on actuarial calculations. [32:22(7)(c)(i)] Following its receipt of PERAC's determination, the retirement board must certify this amount, or an amount based on its own actuarial valuation, to the mayor or selectmen and to the treasurer for appropriation and payment to the treasurer of the retirement system. [32:22(7)(c) (iii)] PERAC must approve. If the municipality fails to include any certified amount in its appropriations for a fiscal year, the assessors must nevertheless include the amount in the next tax levy. [32:22(7)(c)(iv); see *Everett Retirement Board v. Assessors of Everett*, 19 Mass. App. Ct. 305 (1985), for a discussion of a municipality's obligation to pay retirement board costs.]

### **Investment of Retirement Funds**

PERAC has promulgated extensive regulations governing the investment of retirement funds (840 CMR 16.00 *et seq.*). A unit within PERAC known as the Pension Investment Advisory Unit, advises retirement boards on investments.

A municipality may elect, pursuant to Ch. 32 § 22(8), to participate in the Commonwealth's Pension Reserve Investment Trust (PRIT) fund, which is a pooled investment trust. In any community so electing, the Pension Reserves Investment Management (PRIM) board holds and manages pension monies. Ch. 32 §23(2A) outlines the powers and duties of the PRIM board. The PRIT fund is highly diversified and carefully monitored by many investment managers. PRIT was founded in the early 1980's and has achieved a yearly rate of return in excess of 10 % since that time. As of June 30, 2006, there were 70 retirement boards investing all or a portion of their pension funds in PRIT; the PRIT Fund contained 42 billion dollars. Both the state workers' and teachers' retirement funds are invested in PRIT. Retirement Boards who opt not to participate in PRIT must select an investment advisor to invest the funds in their system. Many of these advisors have managed the investment portfolio very well, resulting in very favorable rates of return. Retirement Boards who do not use PRIT also select a custodian for pension funds. The custodian holds the securities and accomplishes trades at the behest of the advisor, who works with the retirement board on developing

asset allocations which reflect diversity and safety. The authority of investment managers to invest funds derives from 840 CMR 16.01. Retirement Boards receive an exemption pursuant to 840 CMR 19.00 and are then required to authorize a qualified investment manager to invest and reinvest funds on behalf of the board in accordance with the board's statement of investment objectives. Every board shall also designate one or more banks or trust companies as custodian of the securities and assets of the system. (840 CMR 16.04) See manual Addendum.

Municipal treasurers have no jurisdiction over the investment of pension funds unless they sit upon the local Retirement Board.

### **A Municipal Treasurer's Procedures for Handling Pension Fund Cash**

A municipal treasurer possesses the responsibility to:

- Receive and record pension fund cash Protect and safeguard the cash, usually in a bank's savings or checking account , or a money market account such as Massachusetts Municipal Depository Trust (MMDT)
- Disburse the cash under the direction of the Retirement Board; cash is usually disbursed soon, either to cover payroll or bill roll warrants, or to the custodian of the investment funds
- Report regularly and comprehensively on the cash to the municipal retirement board.
- Keep a separate record of Retirement Receipts as part of the Treasurer's Cash

Pension fund cash receipts allocated to the treasurer's custody generally include, but are not limited to, the following:

- Contributions from members, including payroll deductions, voluntary contributions, late entry payments, redeposits and transfers from other systems.
- Appropriations and other contributions from the municipality and from other member employers, reimbursements from other systems, reimbursements for individuals employed under federal grants<sup>[111](#)</sup>, and cost of living adjustments.
- Contributions to the Pension Reserve Fund, which are rare as described above

Treasurers may only disburse retirement system funds upon the authority of a warrant previously authorized by the retirement board and signed by two persons designated by that board. The designated persons must provide specimen signatures prior to their signing any warrant authorizing the disbursement of retirement system funds. Furthermore, no warrant may be drawn unless it has been previously authorized by majority vote of the board.

Purposes for which disbursement may be made include the following: [32:23(2)(a)]

- Payments of annuities and pensions.
- Payments to beneficiaries.
- Refunds to members.
- Transfers to other systems.

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- Administrative expenses.
- Purchases of investments.
- Payments to agents for retiree payroll withholdings.

Retirement Boards must establish and maintain a cash book showing both receipts and disbursements in a format under PERAC's direction. PERAC audits this book as the official record. Treasurers are not involved in this exercise.

### **Application for Membership in System**

The treasurer is responsible for ensuring that new employees complete an application for membership in the retirement system at the same time that they fill out tax withholding and group insurance benefit forms. The retirement board must then determine the new employee's eligibility for membership, based on statutory provisions and on local board rules, which must be approved by PERAC. [840 CMR 14.00] Ch. 32 §3(2) explains the eligibility rules the board must follow. Clause 3(2)(d) of this statute treats the eligibility of part-time, provisional, temporary, seasonal and intermittent employees. Elected officials may opt not to belong to the retirement system, pursuant to Clause (2)(a)(vi).

An actively employed individual may not withdraw from a contributory retirement system established under Ch. 32. Any employee who, while a member of such a system, becomes employed in a position in any other governmental unit in which such a system is operative, must thereupon have the membership transferred to the second system. [32:3(8)]

A former employee who returns to active employment may buy back time in the retirement system by paying the amount withdrawn, together with regular interest, from the accumulated regular deductions made during the time of earlier employment. Upon tendering this payment, either in one sum or in installments, upon whatever terms and conditions the board prescribes, the employee will be entitled to all of the creditable service that resulted from the previous employment. The retirement board must calculate both the buy back sum and the amount of the creditable service. An employee may make buy back payments through payroll deductions if the board so approves. [32:3(6)(d)]

### **Contributions from Members of Municipal Retirement Systems**

Ch. 32 §22(1)(b) sets out the various percentages that the treasurer must withhold from the regular compensation of municipal employees for deposit into the retirement fund, depending on the date each particular employee began service with the municipality, and Ch. 32 §1 defines "regular compensation," i.e., the salary, wages or other compensation to which these percentages must be applied. In determining the amount to deduct from each employee for retirement contribution, the treasurer should follow the definition of "regular" compensation in Ch 32 § 1 and 840 CMR 15.03. The CMR changes frequently and should be checked in PERAC's website, [www.mass.gov/perec](http://www.mass.gov/perec). This CMR as of April, 2006 can be found in the Addendum of this manual.



### Pension Contribution Rates

The treasurer must initiate retirement withholdings upon “written notice from the [retirement] board...” [32:22(1)(b)] All employees are deemed to have consented and agreed to such withholdings. [32:22(1)(f)]

The percentage of an employee’s regular compensation that the treasurer must withhold for retirement contribution depends on the date that employee began service with the municipality. If an interruption occurs in an employee’s service and the employee’s retirement contributions remain on deposit in the retirement system during the interruption, the employee’s contribution rate will remain at the pre-interruption rate upon the employee’s returning to service. On the other hand, if an employee withdraws retirement contributions upon leaving service and later returns to service, that employee’s contribution rate will be determined by the date of reentry to service. [See 840 CMR 15.02(2)(b); *Johnson v. Teacher’ Retirement Board*, Contributory Retirement Appeal Board, Case CR-88-082. (7/25/ 89)]

Contribution rates range from 5% to 9%, as follows: 5% for an employee who began service on or before January 1, 1975; 7% for an employee who began service on or after January 1, 1975, but before January 1, 1984; 8% for an employee who began service on or after January 1, 1984, but before July 1, 1996; and 9% for an employee who began service on or after July 1, 1996. Moreover, in any community which has accepted the local option provision contained in paragraph (1)(b)½ of Ch. 32 §22, for every employee who entered service with the municipality on or after January 1, 1979, the treasurer must withhold an additional 2% of the amount of that employee’s regular compensation that exceeds \$30,000.

An exception to these percentages exists in the case of teachers participating in the alternative superannuation retirement benefit program, set out in Ch. 32 §5, as amended by Ch. 68 §12 of the Acts of 1999. The treasurer must withhold 11% of their regular compensation, pursuant to a list of participating teachers submitted to the treasurer by the school committee, board of trustees or other employing authority.

### Tax Status of Pension Contributions

Under Internal Revenue Service law, and employee’s pension contributions are not subject to federal income tax. Massachusetts law, however, allows a more limited exclusion. Only an amount up to \$ 2,000 that an employee contributes to a Massachusetts retirement fund is not subject to state income tax. If an employee is married and the couple file jointly, each spouse may claim up to \$ 2,000 of contributions.

### Transmittal of Funds

Upon withholding retirement contributions, the treasurer must transfer these monies “forthwith” to the retirement system, accompanying them with a statement or voucher itemizing the deductions. The retirement board must then credit the amounts to the accounts of the respective members for whom the deductions were made. [32:22(1)(h)] The treasurer must transmit monthly all amounts withheld from teachers’ salaries to the secretary of the teachers’ retirement system by the 10<sup>th</sup> day of

## **Retirement System**

the succeeding month. [32:22(1)(i)] Retirement Boards must maintain a cash book in a format under PERAC's direction

### **Handling Withholdings from Pensions**

Deductions may only be made from an annuity, pension or retirement allowance if expressly authorized by statute. Ch. 32 §19A-C permits deductions for premium payments for medical insurance, life insurance, income tax withholdings and child support payments. As the custodian of retirement funds, the treasurer is responsible for withholding designated amounts and for disbursing payments to the proper agencies.

To make deductions for medical insurance and tax withholdings, the treasurer must have previously received written authorization from the retiree. A retired employee may also authorize the treasurer to make deductions for child support payments. However, even if a retired employee does not provide such written authorization, the treasurer must, nonetheless, make child support deductions following the receipt of notice from the Child Support Enforcement Division of the Department of Revenue that a retiree is subject to a lien, notice or order for child support. (119A:6, 12:209D) The treasurer must continue to make such child support deductions until receipt of notice from DOR that the lien, notice or order has terminated and all arrears have been paid.

To disburse monies withheld from an employee's compensation to a company or agency, the treasurer must take the following steps:

- Reconcile the amount of the withholdings with the payee's bill or order.
- Prepare a voucher.
- Submit the voucher to the accountant or auditor for inclusion on a warrant.

### **Reconciliation to Bank Records**

A conscientious management of a municipality's pension fund, just as a proper management of all of a municipality's cash, requires prompt and frequent cash reconciliations.

Reconciling the retirement system cash to bank statements entails the same procedure as that outlined in Chapter 4 for all municipal revenues. The treasurer should transmit reconciliations of all cash to the retirement board on a monthly basis.

In conducting a reconciliation, the treasurer should promptly research and resolve all variances. The treasurer should reconcile treasury records with the accountant or auditor on a monthly basis. The treasurer should research outstanding checks within 90 days and may replace checks determined to be "lost" after payments on those checks have been stopped. The treasurer should return all other outstanding checks to the retirement board for disposition pursuant to Ch. 32 §11.

### **Compensation for Treasurer's Duties**

Ch. 32 §20(4)(g) authorizes treasurers to receive compensation in an amount not to exceed \$1,500 for their services as treasurer for retirement funds. Ch. 32 §20(4)(h), a local option statute, permits communities accepting its provisions to compensate treasurers in an amount up to \$3,000. The

treasurer's compensation is payable from the expense fund (investment earnings) of the retirement system, subject to the approval of the board.

### County and Regional Retirement Systems

In communities belonging to a county or regional retirement system, the treasurer's responsibilities include three major functions: (1) serving on the retirement board advisory council, (2) withholding and transferring employee contributions to the retirement system and (3) completing and submitting a *Treasurer's Monthly Report* to the retirement board. A number of counties have been abolished under the provisions of either Ch. 34B or Ch. 151 of the Acts of 1996. Notwithstanding a county's having been abolished, the cities, towns, districts and other governmental units that belonged to that abolished county's retirement system remain as members of that retirement system. (34B:18) Regional retirement boards, structured as set out in Ch. 34B §19, manage the retirement systems of abolished counties.

### County and Regional Retirement Boards and Advisory Councils

County retirement systems are managed by five-person boards, each composed of the county treasurer, who serves as chairperson, two members elected by the membership of the system, one member appointed by the county commissioners to an unspecified term, and one member elected by the county retirement board advisory council. [32:20(3)(b)] A county retirement board advisory council is made up of all the treasurers, elected or appointed, of each town, unit or district belonging to the county retirement system and the county treasurer. [32:20(3)(g)] Regional retirement systems are also managed by five-person boards, structured as set out in Ch. 34B §19B. A regional retirement board advisory council is made up of all the treasurers, elected or appointed, of each town, unit, or district belonging to the prior county retirement system. [34B:19(g)] The members of the regional council elect a chairman from among the members.

Annually, each county retirement board and regional retirement system must submit to the council, at a meeting specifically called for the purpose, a proposed budget of the anticipated expenses of administering the system in the ensuing year. After collaboration, the council and board must certify their consensus expense budget to PERAC's actuary. [32:20(3)(g)] The actuary, by December 15<sup>th</sup>, must specify in writing the amounts that will be allocated to each governmental unit for these expenses. Payment amounts to each member unit are allocated in the proportion that the aggregate regular compensation of the members of each unit, as of September 30<sup>th</sup> of the preceding fiscal year, bears to the aggregate regular compensation of all members of the system on that date, as set forth in an actuarial evaluation of the system. [32:22(7)(c)(i)]

### Contributions from Members of County or Regional Retirement Systems

Ch. 32 §22(1)(b) places in the municipal treasurer the responsibility to withhold retirement contributions from eligible county or regional employees. Procedures whereby the treasurer must calculate the appropriate amount of such contributions are the same as previously described for municipalities. For employees who receive compensation for services in more than one department, the treasurer must calculate and show the amounts separately in the *Treasurer's Monthly Report*. The treasurer must transmit all pension contributions to the county or regional retirement system at least once a month.

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### **Payroll Deductions for Employees Who Work for Multiple Units**

In municipalities that have accepted the local option provision contained in paragraph (1)(b½) of Ch. 32 §22, whereby the treasurer must withhold an additional 2% of the amount of an employee's regular compensation that exceeds \$30,000, the treasurer must be certain to withhold the additional amount from the compensation of an employee who works for more than one governmental unit in the same retirement system and whose combined compensation exceeds \$30,000. Accordingly, in such situations the retirement system must contact each of the units for which the employee works and obtain from them the necessary information to determine the amount of the employee's combined compensation. In cases in which the combined compensation exceeds \$30,000, the retirement system must then notify the governmental unit from which the employee receives the largest compensation and instruct this unit to withhold the additional 2%. The governmental units involved must subsequently notify the retirement board of any change in the employee's salary rate or employment status. When a change occurs, the retirement system must notify the unit making the additional withholding in order for that unit to make any appropriate adjustment.

### **Semiannual Payments to County or Regional System**

The treasurer is responsible to make certain that the amount certified by PERAC as the municipality's fiscal contribution to the pension system is transmitted to the retirement board. Payments must be made in two, equal, semiannual installments, on July 1<sup>st</sup> and January 1<sup>st</sup> of the fiscal year. [32:22(7)(c)(ii)] Since this assessment must be raised in the tax rate if it has not been appropriated [32:22(7)(c) (iv)], the treasurer must notify the assessors before the tax rate is set if an insufficient amount has been appropriated.

### **The Treasurer's Monthly Retirement Deduction Report**

Treasurers must transmit retirement contributions to the retirement system using either the *Treasurer's Monthly Retirement Deduction Report* or, with the board's approval, some other form, either manually or computer generated.

The following list contains general instructions for completing a transmittal report. (Retirement boards may differ with regard to the specific employee information desired.)

1. The treasurer must submit the monthly deduction report on or before 10<sup>th</sup> day of the succeeding month, accompanying the report with a check for the total amount of contributions withheld during the preceding month.
2. The report should include the names (group classifications, contribution rate and social security numbers, if required) of all employee members. It should also contain the names of non-eligible employees. (Teachers have their own retirement system, which requires a separate deduction report.)
3. For new employees whose names appear for the first time on a monthly report, the treasurer should include *New Member Enrollment Forms*, together with copies of the employees' birth certificates and military discharges (if applicable).

4. In making deductions for members who receive an allowance for boarding and housing in addition to cash payments, the treasurer should place a distinguishing symbol, such as a single asterisk (\*), in the deduction column of the monthly report.
5. The treasurer should place a distinguishing symbol, such as a double asterisk (\*\*), beside the names of all employees who are employed in more than one governmental unit in the retirement system.
6. In the case of employees not members of the retirement system, the treasurer should place in the deduction column the appropriate symbol from the list below.
7. The treasurer should enter the total of the monthly deductions for all employees on the monthly report and remit that amount to the retirement board.
8. The treasurer must sign the monthly report.

### Symbols Designating Non-Members of the Retirement System

- E.O. Elected Official
- E. Emergency Employee
- N.E. Not eligible for membership
- W.C. Workmen's Compensation
- M.S. Military Service credit

The following descriptions clarify the applicability of these symbols:

1. **E.O. (Elected Official):** Any person elected to a town or district office after July 1, 1947 may become a member of the retirement system by timely filing an application with the retirement board. The symbol, "E.O.," should be used to designate those elected officials who (a) hold no other municipal position which would make them eligible to become members of the retirement system and (b) do not timely file a membership application following their election to office.
2. **E. (Emergency Employee):** The symbol, "E," should be used to designate a retired person receiving a pension or retirement allowance who is called back to perform services in an emergency. [32:91] The treasurer must deduct from the compensation of a retired person employed for emergency service, unless that person is employed by a city police department under Ch. 32 §83, an amount equal to the retirement allowance or pension received by that person for the time of employment.
3. **N.E. (Not Eligible for Membership):** The retirement board possesses sole jurisdiction to determine the membership eligibility of all employees engaged part-time, provisionally or intermittently by a unit employer. Upon the engagement of such an employee, the treasurer must forward a "New Member Enrollment Form" for that employee to the retirement board. (See pp. 8-22 & 8-23). The symbol, N.E., should be placed in the deduction column of the monthly report for employees whom the retirement determines to be ineligible for membership in the system. Persons ineligible for membership in a contributory retirement system must participate in the Massachusetts Deferred Compensation Plan, an alternative to

## Retirement System

Social Security coverage as permitted by the federal Omnibus Budget Reconciliation Act of 1990 (COBRA). (29:64D) An OBRA employee must contribute at least 7.5% of gross compensation per pay period to the plan on a tax-deferred basis

4. **W.C. (Worker's Compensation):** The treasurer should place the symbol, "W.C.," in the in the deduction column of the monthly report for employees receiving worker's compensation benefits because worker's compensation payments do not constitute regular compensation. Conversely, sick leave and accumulated vacation pay should be included as regular compensation for deduction purposes. [32:14(1)]
5. **M.S. (Military Service credit):** The treasurer should place the symbol, "M.S.," next to the names of employees serving in the armed forces. Entries should only be made in the earnings column, together with deductions, for employed receiving compensation while on military leave. [32:4 & 22(4)]

## Teachers' Retirement System

### Teachers' Retirement Board

The Teachers' Retirement System is managed by a 7-member board consisting of the Commissioner of Education or his designee, who serves as an *ex officio* member and chairs the board, the state auditor or his designee, the state treasurer or his designee, a retired public school teacher appointed by the governor for a 4-year term, two members elected by the active and retired members of the retirement system for terms not exceeding 4 years; and one member selected by the other six members for a 4-year term. (15:16)

The Teachers' Retirement Board determines the eligibility for membership in the teacher's retirement system in accordance with statutory provisions. [See definition of "teachers," 32:1; see also 32:3(2)(a)(iv) & 3(2)(d).] Each school district or collaborative must (a) generate the requisite documentation for retirement purposes (i.e., enrollments, retirements, resignations, leaves of absence) as well as the other pertinent data required for administration of the retirement system and (b) prepare the *Monthly Deduction Report and Deduction Summary Report*.

### Calculating Deductions

The treasurer is responsible to deduct retirement contributions from school employees' compensation and to transmit the monies deducted to the retirement board. Although the treasurer must initiate retirement withholdings from other municipal employees upon written notice from the retirement board, the notice in the case of retirement holdings for school employees comes from the local school department. Upon receiving notice, the treasurer should make retirement deductions for school employees in the same manner as for other municipal employees. The deduction percentage, however, differs for teachers participating in the alternative, superannuation, retirement benefit program, set out in Ch. 32 §5. The treasurer must withhold 11% of their regular compensation, pursuant to a list of participating teachers submitted to the treasurer by the school department.

The Teachers' Retirement Board, in accordance with statutory provisions, must determine the contribution rates for retirement deductions, as well as the types and limits of compensation subject

to those deductions. The board must transmit this information to the municipal treasurer via the school department through the internal payroll process.

### Report of Deductions

The treasurer, as custodian of municipal funds, is responsible for the payment of teacher retirement contributions. Generally, the school district or collaborative prepares the deductions report and summary. The treasurer must transmit retirement contributions to the secretary of the Teachers' Retirement Board on or before the 10<sup>th</sup> day of the next succeeding month. [32:22(1)(i)] All disbursements for teachers' retirement deductions must utilize the warrant process.

Upon receiving retirement contributions, the secretary must credit members' accounts with their respective deductions and pay the contributions to the state treasurer for deposit in the retirement system's annuity savings fund.

The treasurer must accompany retirement contribution payments with a *Monthly Deduction Report* and a *Deduction Report Summary*, setting out compensation amounts and deduction totals. The Teachers' Retirement System, in Chapter 5 of its *Employer's Manual*, has set out helpful information about acceptable formats for these transmittal reports. This manual is a must for every Treasurer's office and may be obtained from the Teachers' Retirement Board (website listed below). The *Monthly Deduction Report* must contain each employee's social security number, name, contribution rate, contract term, monthly regular compensation, regular retirement contribution, additional 2% contribution and service code. Service codes denote full time or part time service: 1 = full time, .5 = half time, .75 = three-quarter time, etc. The *Deduction Report Summary* must include the following:

- Name of school district or collaborative.
- Deduction period.
- Record of check number(s), date(s) and amount(s).
- Total of check(s) remitted.
- Name, title and phone number of contact person.
- Certification by school official, with name and title of that official and date of the certification.

The treasurer should direct questions concerning deduction turnover forms and calculations to the Teachers' Retirement Board. The website for the Teachers' Retirement Board is [www.mass.gov/mtrs](http://www.mass.gov/mtrs). Click on the Employer's area (designated in row of options at top of home page). In this Employer's area, there are updates, forms, training schedules, and bulletin archive.

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## CHAPTER 9

### BORROWING

#### Introduction

Municipalities regularly borrow money for a variety of purposes. Ordinary borrowing purposes include satisfying cash flow needs, financing the acquisition of capital assets and paying for the construction and repair of municipal infrastructure. State law strictly regulates the purposes for which cities and towns can borrow and the time periods for which these borrowings can occur. Borrowing purposes and maximum loan durations are set out in Ch. 44 §§7 & 8.

Municipalities may incur both short-term and long-term debt. Generally short-term borrowings are for periods of one year or less, often in anticipation of a particular municipal revenue source. The short-term debt instrument is called a “note,” which is a written document containing an express promise of the signer to pay a definite sum of money at a specified time not more than a year from the execution of the note.

Long-term debt, on the other hand, involves loans with a final maturity date of 12 months or more. It is issued using an instrument called a bond, which is a written document containing an express promise of the bond issuer to repay a specified sum of money, alternately referred to as the face value, par value or bond principal, to the buyer of the bond on a specified future date(s), called the maturity date(s), together with periodic interest at specified rate(s).

Notes are categorized according to the purpose for which they are issued. For example, notes issued in anticipation of the receipt of operating revenues are called Revenue Anticipation Notes (RANs); notes issued in anticipation of bond proceeds are called Bond Anticipation Notes (BANs); and notes issued in anticipation of state and federal grant receipts are called State Grant Anticipation Notes or Federal Grant Anticipation Notes (SAANs and FAANs).

Ch. 44 sets out strict rules and procedures regarding municipal borrowing. The issuance of long-term debt always requires a two-third vote of the legislative authority. Certain types of debt, such as debt for landfill capping, also require the approval of various state agencies or boards.

The Bureau of Accounts (BOA) of the Department of Revenue (DOR) possesses jurisdiction and responsibility to monitor and maintain records of municipal indebtedness. On or about July 1st of every year, BOA’s Director of Accounts sends to each community a form called, Statement of Indebtedness, which the community must fill out and return to the bureau. Furthermore, upon a city, town, or district’s authorizing debt, the clerk must notify BOA by furnishing the Director with a copy of the vote within 48 hours after the vote has become effective.

## Debt Limitation

Cities, towns and districts must comply strictly with Ch. 44 in all matters of public debt. Ch. 44 §2 asserts this requirement, stating, “Except as otherwise expressly permitted by law, cities, towns and districts shall incur debt only in the manner of voting and within the limitations as to amount and time of payment prescribed in this chapter....”

Ch. 44 enunciates numerous limitations and procedures that govern local debt issues. One of these limitations places a ceiling on the maximum amount of debt a city or town may have authorized at any one time. Ch. 44 §10 states “a city or town shall not authorize indebtedness to an amount exceeding 5 per cent of the equalized valuation of the city or town”. The statute permits municipalities to exceed these limits only with the approval of the Municipal Finance Oversight Board (MFOB). With Board approval, a City or Town’s borrowing limit may be increased by an amount up to an additional 5% of its EQV, sometimes for a term provided.

The aggregate amount of a community’s authorized and outstanding debt for purposes of the Ch. 44 §10 debt limit, however, includes only the debt authorized under Ch. 44 §7. The borrowing purposes set forth in this statute are “inside” the debt limit. The borrowing purposes set forth in Ch. 44 §8, on the other hand, are “outside” the Ch. 44 §10 debt limit. The table at the end of this chapter reference the borrowing purposes both inside and outside the debt limit, as they appear in Ch. 44 §§7-8.

Regional school districts do not have a debt limit. With regard to other districts, the debt limit of a district wholly contained in one municipality is calculated by multiplying that municipality’s EQV by a fraction, the numerator of which is the assessors’ valuation of the taxable property of the district for the preceding year and the denominator of which is the assessors’ valuation of the taxable property of the entire municipality in which the district is located for the preceding year, multiplied by five percent. The debt limit of a district located in two or more communities is calculated by multiplying the sum of the EQVs of those communities by a fraction, the numerator of which is the assessors’ valuation of all of the taxable property of the district in the respective communities for the preceding year and the denominator is the assessors’ valuation of all of the taxable property of all the communities for the preceding year, multiplied by five percent.

## Municipal Finance Oversight Board

The Municipal Finance Oversight Board is an entity established under General Laws to oversee and authorize the issuance of certain debt by municipalities. It is defined in Chapter 44, Section 1 of the General Laws. A municipality cannot issue debt in excess of its debt limit unless authorized by the MFOB. [44:10] Municipalities also must obtain the prior approval of the MFOB before they can issue debt for the following purposes:

1. Establishing, purchasing, extending, or enlarging a gas or electric plant or a community antenna television system if the amount borrowed exceeds in a town 5% and in a city 2.5 % of the equalized valuation of the town or city. However, the amount borrowed, even with MFOB approval, cannot exceed in a town 10% and in a city 5% of its EQV. [c.44 §8(8) and c.44 §8(8A)]
2. Constructing sewers, sewerage systems, and treatment plants and disposal facilities, or making the lump sum payment of a tie-in to these services in a city or town if the municipality does not have a fully self-supporting enterprise fund. [c.44 §8(15)]

3. Approving public works projects that are receiving federal assistance. [ch.74 of the Acts of 1945]

The MFOB designates issues of “Qualified Bonds” under Ch.44A. The treasurer of the city, town or regional school district, with the approval of the city council, city manager, or the mayor in a city, the board of selectmen in a town, or the regional district school committee may file an application and certified copy of the vote as passed with the board to qualify the bonds pursuant to the provisions of c.44A. The written request must contain a letter explaining the need, completed qualified bond questionnaire, a copy of credit reports and the most recent official statement. The request should also contain a breakdown of the proposed work, with the estimated cost of each phase, useful life analysis, copies of any applicable state or federal grant(s) and an Environmental Assessment Form for the project, signed by the responsible official. The request, with the requisite materials, must be sent to:

Municipal Finance Oversight Board  
1 Ashburton Place, Room 1819  
Boston, MA 02108  
617 727-6200

The MFOB will schedule a hearing and issue its resolution of approval, in writing, within 60 days of the hearing and will require Bond Counsel to issue its opinion for the sale of the bonds.

## **Issuing Debt**

Once debt has been properly authorized by a municipality’s legislative authority and all other legal requirements have been met, the municipal treasurer must prepare and sign the notes or bonds. For debt issued by a city, the debt instruments must be countersigned by the mayor, unless the charter otherwise provides. In towns, a majority of the selectmen must sign the instruments. The chairman of the school committee must sign debt instruments for regional school district borrowings, and a majority of the prudential committee or commissioners must sign these documents in other kinds of districts.

## **Short-term Debt**

### **Purposes for Short-term Borrowing**

The various kinds of short-term debt include:

1. Revenue Anticipation Notes (RANs) or Tax Anticipation Notes (TANs), i.e., notes issued to satisfy temporary cash flow needs. [44:4]
2. Grant Anticipation Notes (GANs), also known as State Aid Anticipation Notes (SAANs) or Federal Aid Anticipation Notes (FAANs), i.e., notes issued prior to the receipt of a state or federal grant to begin a project. GANs are repaid when grant funds are received. [44:6A; Ch. 74 of the Acts of 1945]
3. Bond Anticipation Notes (BANs), i.e., notes issued prior to the issuance of long-term debt to begin a project. BANs may be fully repaid when the long-term debt is issued. [44:17] Payment of BANS, without renewal or long term financing, extinguishes a like amount of borrowing authorization. BANs may also be issued when the total amount of a bond issue is not needed immediately or when the long-term issue is intended to include several different projects that have different startup dates and construction schedules. Sometimes, a municipality may issue BANs when bond interest is high, postponing to a more favorable time the issuance of long-term debt.

## Revenue Anticipation Notes (RANs)

Ch. 44 §4 permits cities, towns and tax-levying districts to incur short-term debt in any fiscal year in anticipation of taxes and other current revenues of that fiscal year. Such borrowing requires approval of the same official or board authorized to countersign the notes, generally the mayor or the selectmen. The borrowing amount cannot exceed the municipality's "certified" revenue borrowing capacity, which is the aggregate of: (1) the tax levy of the preceding fiscal year, (2) the net amount collected in the prior fiscal year from motor vehicle and trailer excise, and (3) payments made to the municipality by the Commonwealth in lieu of taxes during the prior year as reimbursement for property taken for State purposes. For a district, the borrowing cannot exceed the district's aggregate receipts from taxes, rates, and service fees in the year preceding that for which the debt is incurred.

The aggregate amount borrowed by a municipality or district must be approved by the Director of Accounts or bond counsel and must be shown on an estimated cash flow statement prepared on a form approved by the Director. Borrowings for periods less than one year may be renewed, so long as the total term does not exceed one year from the date of the original borrowing. Revenue anticipation notes must be paid within one year of their date; however, payment may span two separate fiscal years.

## When and How Much to Borrow

Treasurers may borrow on or after July 1st of any fiscal year that their cash flow analysis indicates a need for borrowing. To determine whether a need exists, treasurers should analyze monthly operating cash receipts for the preceding one or two years, the comparative expenditures made during those years and the anticipated disbursements for the subject year. If this analysis indicates the likelihood of a cash deficit at any time during the fiscal year, the treasurer may initiate a revenue anticipation borrowing.

The treasurer can borrow the projected net cash shortfall prior to the expected receipt of revenue for the fiscal year. The treasurer can also borrow a larger amount in order to provide a cash reserve to counteract any reduction or tardiness in anticipated receipts or to advance payments for the acquisition of capital equipment funded by an appropriation. The treasurer should update the cash flow statement at least monthly and be continually on the lookout for any extraordinary payments that could transform cash flow projections. (Chapter 11 provides a more detailed discussion of cash flow projections.)

Treasurers must be aware when making municipal borrowings that the federal arbitrage laws, set forth in §103 of the IRS Code, restrict the investment of tax-exempt bonds and note proceeds in higher yielding, taxable securities and requires that certain earnings on such notes and bonds be paid to the IRS. Treasurers may not borrow in anticipation of revenue if other revenue funds are invested.

The treasurer should fix the due date of revenue anticipation borrowing to occur shortly after the tax due date. In setting the date, the treasurer should allow sufficient time after the tax due date for (a) collection and turnover of adequate tax receipts for the debt payment and (b) completion of the necessary procedures to make that payment.

The decision whether to perform all tax anticipation borrowing for a fiscal year at one time or more than once during that year depends on several factors:

1. Likelihood of revaluation or recertification-related delays or budget issues in obtaining tax rate approval.

2. Issuance costs for single or multiple offerings.
3. Interest projections for varied amounts and terms.
4. Effect on the municipality's ability to comply with the federal Tax Reform Act of 1986 restrictions. (See below.)

In determining how frequently to issue tax anticipation bonds, the treasurer may consult with other municipal treasurers, with Bureau of Accounts (BOA) Debt Section and with local and regional bankers. The treasurer should take full advantage of the expertise of the financial advisor employed by the municipality. Ultimately, decisions about when and how often to borrow lie with the treasurer.

### **Issues Relating to Revenue Anticipation Borrowings**

1. Cities, towns and most districts do not require authorization from their legislative bodies to issue RANs or TANs. However, regional school district treasurers must obtain authorization from their school committees for such borrowings. They should acquire this authority early in the fiscal year to avoid last minute crises.
2. The total amount of each borrowing should not exceed the amount reasonably required and should be substantiated by a cash flow projection.
3. Since the federal government has established strict arbitrage laws and regulations relating to the amount of tax-free interest a local governmental entity can earn on the investment of note and bond proceeds, the treasurer should regularly consult with the municipality's financial advisor and bond counsel to make certain that municipal borrowings do not contravene these laws and regulations.
4. Tax anticipation notes must be payable, and paid, not later than one year from their date of issue and cannot be renewed or paid by the issuance of new notes beyond that period.

### **Grant Anticipation Notes (GANs)**

Municipalities regularly receive grants of money from the Commonwealth and from the federal government for diverse municipal projects. Frequently, the municipality must pay the project costs up front and apply for reimbursement of these costs later, as the project work is completed. Massachusetts law permits municipalities to make borrowings to pay up front project costs in anticipation of reimbursement from grant proceeds.

### **State Aid Anticipation Note (SAANs)**

If a municipality receives a grant from the Commonwealth to reimburse the municipality for up front expenditures for any project for which the municipality could borrow for 5 years or longer, the treasurer can incur debt outside the debt limit and issue state aid anticipation notes for the project for a period not exceeding 2 years. [44:6A] The loan may be renewed from time to time, as long as the grant remains payable in an amount at least equal to the amount of the outstanding loans. The availability of grant funds must be verified by an accountant's letter with each renewal.

Borrowings under Ch. 44 §6A do not require town meeting vote. Rather, they require, in towns, the approval of the selectmen and, in cities, the approval of the official whose approval is required by the city charter for the borrowing of money. The notes must be

signed by the treasurer and approved by either BOA or bond counsel. The grant proceeds may be used to discharge the loan without the need for additional appropriation.

Borrowings in anticipation of state grants may also be made under Ch. 44 §6. However, borrowings are infrequently made under this statute, partly because they require a majority vote of the legislative body. Furthermore, the purposes for which borrowings may be made are more limited under this statute. Municipalities may only borrow under its provisions for the costs of altering a grade crossing, constructing a highway, installing traffic lights or paying land damages.

### **Federal Aid Anticipation Notes (FAANs)**

Federal aid anticipation notes may be issued to provide temporary financing for projects that will ultimately be funded by federal grant proceeds. [Ch. 74 of the Acts of 1945]

Issuing FAANs does not require approval of the legislative body; however, the legislative body must have voted to approve the project and have authorized debt for the local share of the project costs. If a grant is awarded to reimburse the costs for a public works project, the municipality must obtain approval from the MFOB and the Governor before undertaking the project or issuing FAANs. To obtain such approval, the municipality must submit to the MFOB an application containing an environmental statement, grant documentation, a project cost breakdown and a copy of the town or city vote accepting the grant.

Upon obtaining the necessary approvals, a municipality may issue notes in anticipation of federal aid for a maximum of 2 years. The municipality may from time to time renew these notes, so long as the accountant or auditor certifies that at the time of the refunding, the municipality is entitled to receive from the grant an amount at least equal to the amount of the refunding loan.

### **When and How Much to Borrow**

If a community desires to borrow in anticipation of reimbursement from the Commonwealth for an infrastructure project, such as highway resurfacing or reconstruction, the treasurer should consider the two following questions in developing a borrowing plan:

1. What is the cost of the project for which a contract is about to be awarded?
2. What is the anticipated completion date of that project?

For projects like highway construction or reconstruction, the work may be performed in the spring, summer and fall. When soliciting bids for such a project, a treasurer should always carefully consider how the timing of the performance of the work on that project might be staggered. Such consideration will enable a better formulation of the bid documents.

If, for example, a highway construction contract for \$100,000 were to commence on July 1st and be completed on August 15th, funds would only have to be available upon the passage of 30 days following the award of the contract, i.e., on August 1st, unless the

particular contract otherwise specified. If the work were completed on September 1st and the public works department immediately filed evidence of that completion with the granting agency, the grant proceeds would probably be received by the municipality within 60 days of that filing, i.e., by November 1st. In such a situation, the treasurer should structure the borrowing to have available the \$100,000 needed to advance fund the project from August 1<sup>st</sup> to December 1st in order to allow leeway for the state reimbursement.

Grants for other kinds of infrastructure projects, such as water system rehabilitation and sewer construction, might entail different reimbursement schedules. To determine the most appropriate term for a borrowing in anticipation of reimbursement for such a project, the treasurer should obtain from the department charged with the responsibility for that project an estimated project payment schedule. The treasurer should also determine the likely dates and amounts of the reimbursements to be received. From this information, the treasurer should create a project cash flow chart. The treasurer should take steps to receive an updated completion schedule at least every 3 months during a construction program in order to be aware of any alterations in contract timelines since such adjustments will affect the timing of reimbursements.

A good rule of thumb for treasurers for projects for which the upfront funding will derive from grant anticipation borrowing is to have proceeds on hand in an amount at least the equivalent of two months' estimated billings. The treasurer should fix the payoff date not earlier than the date sufficient reimbursement payments will have been received to discharge the temporary loan obligation.

The treasurer should be cognizant of the payment schedule for each ongoing project. Making payments in accordance with the construction contract will help the municipality to avoid significant interest penalties. Also, being aware of the payment schedule will help the treasurer to protect against unnecessary borrowings. In timing grant anticipation borrowings, the treasurer should take care to avoid federal arbitrage penalties.

### **Bond Anticipation Notes (BANs)**

Municipalities may issue bond anticipation notes (BANs) in anticipation of contracting long-term debt. [44:17] Prior to issuing BANs, a municipality's legislative body must have specifically authorized the long-term debt with a 2/3 vote.

Municipalities can issue BANs for up to 2 years without having to make principal payments. They can refund BANs for up to 10 years from the date of the original loan. However, municipalities that refund BANs must make principal payments in every year following the second year. Each paydown must be at least equal to the minimum payment that would have been required if the temporary loan had been converted to a serial loan.

*Exception:* A municipality can issue BANs for a feasibility study required to apply for a school facilities grant for up to 5 years with no principal payments. [70B:6(e)]



**Example:** Pleasantville issues a BAN for \$100,000 to purchase 2 police cruisers and a pickup truck. The maximum allowable term to borrow for the acquisition of departmental equipment (without approval of the Board of Selectmen or Mayor) is 5 years. Pleasantville can issue BANs for 2 years without making a principal paydown. Subsequently, the community must make the requisite principal payments in the third, fourth and fifth years and repay the debt in full within 5 years. [44:17]

Amount Issued	Issue Date	Maturity Date	Amount Paid at
\$100,000	1/1/2001	1/1/2002	\$ 0
\$100,000	1/1/2002	1/1/2003	\$ 0
\$100,000	1/1/2003	1/1/2004	\$ 34,000
\$ 66,000	1/1/2004	1/1/2005	\$ 33,000
\$ 33,000	1/1/2005	1/1/2006	\$ 33,000

For a project with a 10-year term:

Amount Issued	Issue Date	Maturity Date	Amount Paid at
\$100,000	1/1/2001	1/1/2002	\$ 0
\$100,000	1/1/2002	1/1/2003	\$ 0
\$100,000	1/1/2003	1/1/2004	\$ 12,500
\$ 87,500	1/1/2004	1/1/2005	\$ 12,500
\$ 75,000	1/1/2005	1/1/2006	\$ 12,500

After five years the municipality could bond \$62,500 for no longer than five years.

Any BAN proceeds remaining when a serial loan is issued should be applied to the payment of the BAN. However, if a serial loan is issued after the final costs of a project are known and those costs are less than the amount for which the BAN was issued, the serial loan may only be issued for the amount of the project costs.

Some municipal borrowing purposes require the approval of the MFOB or other state agencies prior to the issuance of the serial loan or BANs. [44:7&8] Moreover, if a municipality seeks to incur debt in an amount of \$500,000 or more, BOA may require the municipality to obtain a preliminary legal opinion from bond counsel attesting to the legality of incurring that debt.

## Procedures for Short-Term Borrowing

Once a municipality's legislative authority has authorized a borrowing, the municipality has satisfied all of the legal requirements for the borrowing, and project plans have been completed, the treasurer should initiate the short-term borrowing procedure by notifying prospective purchasers that bids will be accepted at a particular time and place and for a particular amount. Bids may be submitted in writing, by fax, by telephone or electronically.

The municipality, together with its financial advisor, must determine whether the notes will be designated as qualified tax-exempt obligations, i.e., “bank-qualified,” for purposes of Section 265(b)(3) of the IRS Code. A municipality’s borrowing is bank qualified, if that municipality does not reasonably anticipate issuing more than \$10,000,000 of new money debt in a calendar year. Such a municipality is defined as a “qualified small issuer” in the IRS Code. If the issue is offered as bank qualified, the municipality will have to provide the purchaser with a Certificate of Designation so indicating. The issuing bank will be allowed a tax deduction for a portion of its interest expenses allocable to the notes.

For issues in the amount of \$100,000 or more, a municipality must submit to the IRS a Form 8038-G, Information Return for Tax-Exempt Governmental Obligations, on or before the 15th day of the 2nd calendar month after the close of the calendar quarter in which the issue was issued. For issues less than \$100,000, the municipality must submit to the IRS a Form 8038GC. Usually, a municipality’s financial advisor will provide these forms for signatures of the appropriate officers.

Since federal securities law imposes penalties on debt issuers who provide false or misleading information to investors or who withhold requisite information from investors, the treasurer should be particularly diligent in preparing a disclosure statement relating to notes that might be sold or resold to other than Massachusetts major institutional investors. (See Municipal Securities Disclosure Requirements, pg. 9-23 & 9-24.)

In evaluating bids after their receipt, the treasurer should take into account the following market conventions:

- Bids are usually expressed in hundredths of a percent.
- A hundredth of a percent (.01%) is called a basis point.
- A difference of one basis point for a period of six months on \$100,000 is \$5.00

Some underwriters will add a premium to break a tie or to make a bid more competitive. Subsequent to the effective date of the Municipal Modernization Act on November 7, 2016, if a municipality receives a premium, that premium, together with any accrued interest resulting from the delivery of the notes on a date subsequent to their dated date, must be used in one of two ways [44:20]:

- The premium must be segregated in a separate fund and appropriated for a capital project with an equal or longer statutory borrowing term than the borrowing that generated the premium; or
- The premium must be applied to pay costs of the project being financed, and thereby reducing the amount borrowed for the project.

Upon accepting or rejecting a bid, the treasurer or financial advisor must notify all bidders of the decision.

## State House Notes

State House Notes are debt instruments for municipalities, counties and districts certified by the Director of Accounts [44:23-28]. These instruments are payable annually. Usually,

they are limited to maturities of 10 years. The notes do not require an official statement or full disclosure. State House Note forms are available on the DLS website at [www.dls.state.ma.us](http://www.dls.state.ma.us) Select City & Towns, Bureau of Accounts, and Public Finance Section for an overview and online forms.

Ch. 44 §23 requires the Director to furnish forms to each municipality and district treasurer for the issuance of notes for money. To comply with this requirement, the Director delivers to each treasurer a book of serially numbered notes. The notes, as required by Ch. 44 §24, contain blanks for the treasurer to insert an issue date, interest percentage and due date.

Whenever a municipality or district votes to borrow money other than by issuing bonds, the treasurer, using the forms provided by the Director, may make notes for the amount of the proposed loan. The treasurer may use one or more of these forms, filling in the blank spaces. The notes must be issued in serial order. If a note is somehow ruined, the treasurer must return it to BOA.

The treasurer must sign all notes, and they must be countersigned by a majority of the selectmen, in a town, by the mayor in a city and by a majority of the prudential committee or the commissioners in a district. The district treasurer and the chairman of the school committee must sign school district notes. The clerk of the city, town or district must attest all signatures.

The treasurer must retain a duplicate record of each note issued on the “treasurer’s stubs” in the book of state house notes. If a municipality uses notes prepared by a bank instead of state house notes, the treasurer must still record the details of the loan in the book of state house notes. In this case, the treasurer must send the next serially numbered note from the state house notes provided by the Director with the bank-prepared notes. BOA will void the state house note and return it to the treasurer. After making a duplicate record, the treasurer must forward the state house notes, with a copy of the loan authorization, all signatures having been attested by the clerk, to the Director for his certification. The Director, after certification, must return the notes by registered mail to the treasurer or forward them to the purchaser. The Director may not certify a note more than 5 days before the issue date appearing on the face of the note. [44:24]

### **Issuance of Notes**

When a municipality or district votes to incur debt, the treasurer must provide bond counsel with a certified copy of the authorizing vote. Bond counsel must review the validity of the vote and the legality of the borrowing purpose and, if all is in order, issue a preliminary opinion approving the borrowing.

The treasurer and the financial advisor must create a financing plan based upon the cash needs of the borrowing. Once a plan has been established, the treasurer or financial advisor must notify potential bidders of the particulars of the sale.

Bidders may submit their bids in writing, by fax, by telephone or electronically, declaring the rate of interest at which they will loan the amount sought. Promptly after having accepted a bid, the treasurer must notify all bidders of the bidding results.

The financial advisor and bond counsel must prepare the necessary documents and certificates and transmit them to the treasurer for the appropriate signatures. Sometimes local ordinances provide that signatures must be certified. When the documents have been properly signed, the treasurer or the financial advisor must turn them over to bond counsel for review and for preparation of an approving opinion.

Following the receipt of bond counsel's approving opinion, the treasurer or financial advisor must deliver the notes to the purchaser. At that time, the purchaser must tender the agreed price for the notes. The treasurer must notify the Director of Accounts of the amount, purpose, date, and term of the loan. The treasurer must maintain a record of each loan to ensure compliance with the borrowing limits imposed by Ch. 44 §10.

## **Procedures for Long-term Borrowing**

### **Introduction**

When issuing long-term debt, a treasurer should generally employ the services of a bond counsel and a financial advisor. The issuance process involves the preparation of a disclosure document, an application for a credit rating and, generally, a formal, competitive bidding procedure.

A number of outside factors affect the interest rate a municipality will have to pay on its sales of bonds or State House Notes. These factors include:

1. General market conditions.
2. The financial standing of the community, which is generally reflected in its bond rating.
3. The term of the loan.
4. The restrictions of the Tax Reform Act of 1986. (See below.)

### **Role of Bond Counsel**

Bond counsel plays an important role in the bond issuance process. In order for a municipality to issue bonds, bond counsel must give an approving opinion. This opinion must state that the bonds have been properly issued in accordance with law, that they constitute a binding obligation of the municipality and that they are payable from a described revenue source. The opinion will also describe the tax-exempt nature of the interest to be paid on the bonds.

Bond counsel's approving opinion will be unqualified, stating explicitly that the bonds are valid and the interest is tax-exempt as described. If the bonds turn out not to be valid or the interest turns out to be taxable, bond counsel may be liable to the purchaser.

The services provided by bond counsel in the process of assuring that bonds are properly issued include:

- Determining whether the municipality or district possesses the requisite legal authority to issue the bonds.
- Drafting a motion for a vote whereby the legislative body can authorize the bond issue.
- Making certain that the bonds were properly authorized, that the issuer possesses the legal power to carry out the project the bonds are intended to finance.
- Ensuring that all requisite steps were taken and the necessary certification provided to guarantee that interest on the bonds will be tax-exempt.

Because bond counsel plays a critical role in the borrowing process, communities should be careful to select a law firm that possesses an extensive and widely regarded expertise in this area of jurisprudence. Selecting a bond counsel in whom the investment community has confidence substantially assists a community to market its bonds. Of course, bond counsel receives compensation based on the firm's expertise, as well as on the complexity of the work involved and the extent of the services provided.

### **Structuring a Loan**

A municipality must take the following factors into account when structuring a long-term loan: legal restrictions, market conditions and the borrower's ability to pay. The cost of issuance is also a significant consideration in the case of smaller loans. Frequently, these factors may be in conflict, necessitating a compromise in the final structure of a borrowing. In any case, a municipal treasurer must keep these factors in mind while making the various decisions, discussed below, relating to a loan's structure.

### **Issuing Bonds or State House Serial Notes**

An initial decision when considering long-term borrowing is whether to issue the debt in the form of bonds, approved by bond counsel with an official statement for disclosure, or in the form of State House Serial Loan Notes, approved and certified by the Director of Accounts. The major advantages of using State House Notes are the ease and the relatively low cost of their issuance. The major advantages of using bonds are the liquidity and the marketability of these instruments, attributes that generally result in a lower interest rate for the municipality.

Based upon a consideration of the local banking environment and the size and term of a desired loan, the treasurer should try to ascertain the likely amount of the additional interest the municipality would have pay if it made the borrowing using State House Serial Notes instead of bonds. After that, the treasurer should compare the increased interest cost accompanying State House Notes with the significant administrative expenses associated with the sale of bonds. In the process, the community should investigate BOA's guidelines, which contain information about the maximum size, term, and number of certificates that the bureau will approve for a long-term loan using State House Notes.

With all of this information in mind, the community will be in a good position to determine which debt instrument to use.

## **Determining the Maturity Schedule**

The General Laws govern the maximum term for long-term loans. However, municipalities can borrow for shorter terms than those permitted by statute. Of course, the shorter the term, the lower the ultimate interest cost. The treasurer should take into account the useful life of a project paid for with the loan proceeds when determining the term of a loan.

Ch. 44 §19 permits some flexibility in timing the first principal payment on bonded indebtedness. This payment can be made at any time in the next fiscal year. Thus the municipality through the use of “long or short” first interest payments can time the first and succeeding principal payments to come due at a time of the year when cash flow is most advantageous. However, if the first principal payment date is more than one year after the issue date, the maturity may have to be shortened by one year.

This statute also permits level debt payments instead of level principal payments for all loans. Of course, interest costs over the life of a loan repaid using level debt service will be greater than for those repaid using level principal payments.

Additionally, c.44§19 provides additional flexibility for the final payment which may be made not later than the end of the fiscal year in which such bonds would otherwise have been payable under this chapter, or any other statutory authority under which the issuance of any such bonds was otherwise authorized.

## **Deciding the Manner in Which the Loan Will Be Awarded**

A municipality must also determine the manner in which it wishes to bid and award a loan. Until the late 1970s, the most common method was to require that bids be for the full amount of a loan and at a single rate of interest. Although this method is still frequently utilized for loans of less than 5 years, most communities now permit multiple rates bidding for long-term debt. Under this method, the bidder is allowed to specify different interest rates for different maturities, but no more than one interest rate for bonds of the same maturity.

To prevent aberrations, a bid request may specify the maximum differential permitted between the lowest and highest rates bid. Municipalities then select the winning bids based either on the lowest net interest cost or the lowest true interest cost, after taking into consideration the premium (selling price in excess of par value) offered, if any. In the single-rate method, the award is usually made on the basis of the lowest stated rate bid, and premium is only considered if two or more bidders offer the same low rate. In the vast majority of cases, bonds are still sold on an all-or- nothing basis, although on occasion an issuer might allow different purchasers for different lots of bonds. (See sample NIC calculation on page 9-34)

## **Bond Ratings**

In order to successfully market bonds, an issuer should seek a bond rating on the issue. Through bond ratings, investors, purchasers, underwriters, traders and sellers gauge the relative credit worthiness of municipal bonds. Bond ratings are established by independent, private, rating agencies and reflect the rating agency's judgment as to a community's capacity and willingness to pay interest and principal in a timely fashion. Ratings have a significant effect on the cost of borrowing; indeed, investors will generally accept a lower interest rate for bonds issued by a higher-rated community. The ratings range from Aaa (AAA) to C. The highest four rating categories (Aaa, Aa, A, and Baa by Moody's Investors Service, or AAA, AA, A, and BBB by Standard and Poors) are considered "investment grade." Institutional investors, such as banks and fiduciaries, are often legally prohibited from purchasing bonds that do not have an investment grade rating. The three major rating agencies are Moody's Investors Service, Standard and Poors' Corporation, and Fitch. Having two rating agencies rate the bond issue gives two perspectives, which can often enhance the view of the community's credit worthiness. Securing one or more bond ratings may be worth the cost, depending on the size of the issue. See end of Chapter 10 for a list of the indicators used by credit analysts in rating municipalities.

Most credit agencies issue publications outlining the factors upon which they rate municipalities. They also give seminars to explain the process, and answer questions.

## **Credit Enhancements**

Credit enhancement is the process of using the credit of a stronger, more highly-rated entity to enhance the credit of a lower-rated entity. The major forms of credit enhancement are private bond insurance, bank letters, and lines of credit. The most prevalent credit enhancement for long-term debt issues is municipal bond insurance. Bond insurance is a legal commitment by an insurance company to make debt principal and interest payments if the issuer is unable to make those payments on time.

Providers offer a variety of options for procuring municipal bond insurance, such as direct purchase by the issuer or by direct or optional purchase by the underwriter. The premium for this insurance is usually expressed as a percentage of the total principal and interest; it is payable at the time of closing.

Today the purchase of insurance for cities, towns and districts is almost exclusively done through the optional purchase by the underwriter. With this method, the decision of whether to purchase the insurance is entirely left to the bidding underwriter. The treasurer, through his or her financial advisor should provide the prospective bond insurers with complete information about the bond sale at least 2 weeks prior to the sale date to give the insurers adequate time for their review process. On the sale date the underwriter will decide whether to buy insurance or bid without. Generally, purchasing insurance is not particularly cost effective for short term loans or for loans issued by municipalities with high bond ratings. Bank letters of credit are generally written for a substantially shorter term bond instead of bond insurance. In the case of default, a letter of credit will pay both the principal and accrued interest of a loan to the investor. A line of credit might also pay principal and interest to an investor in the case of a default; however, this kind of credit

enhancement is weaker than a bank letter and has many more conditions that have to be satisfied before it will pay.



## **Alternatives to Competitive Bidding**

The vast majority of municipal bond and note issues in Massachusetts are sold by competitive bid. However, bonds and notes may also be sold by private placement or negotiated public sale.

In the case of a private placement, the securities are sold directly to a single investor or to a small number, less than 5, of sophisticated investors. A private placement significantly reduces the direct cost of issuance by shifting the primary burden of disclosure and rating procurement from the issuer to the investor. Of course, the costs are ultimately paid by the issuer in the form of a higher interest rate on the bonds. A negotiated public sale is usually reserved for large or complex issues of weaker credits, issues that might reasonably attract only one “competitive” bid or that require extraordinary presale solicitation on the part of the underwriters. Negotiated sales are sometimes used for the sale of advanced refunding, especially when the market is particularly volatile.

## **Requisite Actions before Proceeding with a Sale**

Before proceeding with a sale of notes or bonds, the treasurer should ensure that the following actions have transpired:

- The community has selected a financial advisor, a bank to act as paying agent, a bond counsel, and a rating service or services.
- The treasurer and financial advisor have determined how the borrowing will be structured.
- The legal requirements for the loans have been satisfied up to the point of sale, and bond counsel has provided an approving opinion.
- The cost of the project or acquisition for which the borrowing is to be made has been precisely determined.

## **The Offering Documents**

The two, primary documents utilized in a competitively bid, public sale of long- term debt are the Notice of Sale and a prospectus, called the Official Statement. The Notice of Sale sets forth the structure of the loan, bidding restrictions, method of award, anticipated time and place of delivery and method of payment. It is a precise, legal document.

The Official Statement provides more general information about the bonds being offered and, more importantly, communicates to the potential investor all the information reasonably necessary to make a prudent investment decision. This information includes the notice of sale, a description of the issue, financial and other economic data about the municipality, the proposed form of the bond counsel’s opinion and forms for use in submitting offers.

The financial advisor generally prepares or assists in the preparation of the Official Statement, utilizing audit reports, financial statements and other public records and reports, including information from interviews with key municipal officials. No matter who

prepares the statement, however, the primary responsibility for its adequacy and accuracy lies with the treasurer. Federal securities law imposes significant penalties if the statement contains materially false or misleading information or does not disclose material facts.

The Municipal Securities Rulemaking Board, an adjunct of the Federal Securities and Exchange Commission, requires every registered municipal securities dealer to disseminate the information contained in the Official Statement to its customers. The Government Finance Officers Association (GFOA) has promulgated guidelines that have become the industry standard for the content and format of an Official Statement. These documents are typically 30-40 pages in length, with the community's most recent audit attached as an appendix. Depending upon the quality of a community's records and the diligence of its effort, an Official Statement will take from 4 to 6 weeks to generate.

### **Advertising the Sale**

The most common method of advertising a sale of municipal bonds is publishing a notice in the Daily Bond Buyer, the municipal bond industry's primary newspaper and information source, and circulating the Official Statement to prospective purchasing underwriters, locally and nationally. These activities should take place approximately 2 weeks, and no less than 7 days, prior to the sale date.

### **The Sale**

A sale of municipal bonds generally entails opening the sealed, faxed or electronic bids of prospective investors at the office of the financial advisor. The treasurer or financial advisor should immediately notify the apparent low bidder, i.e., the person who offers the most favorable interest rates. Low interest rates constitute the most critical factor in making an award because they result in the highest price being paid for the bonds. Although an issuer usually reserves the right to reject any or all bids, a municipality or district should only exercise this right in unusual or extraordinary circumstances; otherwise, the number and quality of bids submitted for future sales will very likely be diminished. If the market changes dramatically against the issuer's advantage between the dates of advertising and sale, the municipality might be more prudent to delay or cancel a sale rather than to reject all bids.

### **Post-Sale Activities**

Immediately after a sale, the treasurer or financial advisor must assemble the details of the bids and the debt service schedules in order to prepare for the formal award vote. Bond counsel should draft the actual form of this vote. The financial advisor and bond counsel must arrange for printing and delivery of the bonds and for completing the final official statement. Bond counsel must prepare the necessary final papers for delivery, and the financial advisor must arrange for execution of those papers. Delivery usually occurs between 7 and 14 days after the bid opening date.

### **Delivery of the Bonds**

At the closing, the municipality must deliver the bonds, closing papers, final official statements and bond counsel's opinion to the purchaser and the purchaser must electronically transfer the purchase price, accrued interest and any premium to the municipality's account. The municipality should receive a statement of the payment, with a breakdown of the principal, premium and accrued interest. The municipality should also receive a schedule of principal and interest payments, delineating the payment amounts and the due dates. Generally, interest is paid semiannually, and principal is paid annually. The date of the first principal payment can be set more than one year later than the sale date in some instances. Arranging a schedule of repayment late in the fiscal year may help future municipal budgets, improve cash flow, and increase interest earnings on the appropriated funds.

## **Debt Records & Activities**

The treasurer must maintain records of all municipal borrowings; these records must contain the following information for each issue:

- Loan description.
- Name of purchaser.
- Dates of issuance and maturity.
- Annual interest with due dates.
- Annual principal amortization and due dates.
- Loan balance.

If an issue is a multiple purpose loan, i.e., issued for more than one statutory purpose, the treasurer must keep records of the amount and maturities of each component of the total loan. [44:16] Treasurers must determine the amounts of interest and principal becoming due on debt and must notify the accountant or auditor, the finance committee in towns, and the mayor or selectmen for inclusion of these amounts in the annual budget. [41:59]

The accountant or auditor must notify the assessors in writing of the amount of debt becoming due during the next financial year and explain to them what provision has been made for meeting this requirement. [44:16]

Upon receiving each bank statement, the treasurer should reconcile the loan accounts shown on the statement. As bonds mature, the bank will either destroy them or cancel them and return the cancelled bonds to the treasurer. In either case, the bank will provide the treasurer with documents for treasury records. If a balance of loan proceeds remains after the completion of the project for which a loan was authorized, that balance may be appropriated for any purpose for which the municipality could borrow for the same or a longer period as the period actually borrowed for the subject project. [44:20] Unspent amounts less than \$50,000 on completed projects may be appropriated to pay debt service.

## **Call Provisions**

If a treasurer sells bonds with a maturity greater than ten years, the treasurer should include with the offer a condition permitting the municipality to call in the bonds, i.e., to retire them prior to the stated maturity date, at the treasurer's option.

### **Refunding of Existing Debt**

During periods when interest rates decline, municipalities can save money by refunding some or all of their outstanding debt. The refunding process involves the issuance of refunding bonds and is analogous to refinancing a home mortgage to take advantage of lower rates. New debt is issued in the form of refunding bonds, and the proceeds are used to retire the outstanding, higher interest debt, i.e., the refunded bonds. The savings is the difference between the higher annual debt service on the refunded bonds and the lower annual debt service on the refunding bonds.

Refunding is generally classified as either current or advanced. In the case of a current refunding, the proceeds of the refunding bonds are used to retire the refunded bonds on the call date. Under Internal Revenue Service regulations, a current refunding must occur no more than 90 days prior to the payment of the refunded bonds.

Advanced refunding is the procedure whereby one bond issue is replaced with another bond issue. This procedure is utilized typically when a municipality discovers that it can borrow with better terms than the terms of an existing bond issue. The treasurer uses the proceeds of the new bond issue to purchase government securities to be held by an escrow agent. The escrow agent uses proceeds in the escrow to service the outstanding refunded debt. The agent holds the escrow until the first call date of the refunded bonds at which time they are called and paid off.

Bonds must be callable in order for a treasurer to utilize a refunding. Moreover, a sufficient present value savings must be available to make the process worthwhile. Strict federal regulations govern the investment of the refunding bond proceeds. A municipality's financial advisor can advise about the financial feasibility of undertaking a refunding.

## **Qualified Bonds**

Ch. 44A makes available to municipalities with marginal credit ratings, or a need for structuring flexibility not otherwise permitted under Chapter 44, a borrowing procedure under what is referred to as the “qualified bond” program. Under this program, a participating community issues “qualified bonds,” and the state treasurer pays the debt service on these bonds directly from the community’s local aid, thereby increasing the security of the bonds. “Qualified bonds” may be issued for any legal borrowing purpose authorized by a vote of the municipality’s appropriating authority.

Issuing qualified bonds entails the following steps:

1. The treasurer files an application with the MFOB to qualify the bonds, the application are copies of the original vote authorizing the debt and a vote of the mayor or selectmen, authorizing the treasurer to apply for qualified bonds.
2. The MFOB conducts a hearing and investigates the need for the improvements to be financed from the proceeds of the bonds, the ability of the municipality to provide other essential public improvements and to repay the debt service, the reasonableness of the amounts to be expended, and the amount of the local aid payments likely to be made to the municipality.
3. If the MFOB is satisfied that the municipality is entitled to issue qualified bonds, the board adopts a resolution authorizing issuance within 60 days of the board’s application review.
4. The board may require future debt restrictions or other fiscal limitations that it deems necessary as a result of its investigation. These requirements, which must be in writing, are binding, although they may be modified in the future.
5. The municipality issues the qualified bonds for a period of not less than 10 or more than 30 years. The debt securities must contain language on their face that they are issued pursuant to the Qualified Bond Act.
6. Within 10 days after the issuance of the qualified bonds, the treasurer certifies to the state treasurer the following:
  - The maturity schedule of the debt issue.
  - The interest rate or rates.
  - The debt service payment schedule.
7. The state treasurer becomes the paying agent for the full debt service on the qualified bonds. All payments will automatically be withheld from the municipality’s distributable state aid.
8. The treasurer or financial advisor transmits copies of the Official Statement, debt service schedules (maturity schedule) and wire instructions to the Division of Local Services. Since qualified bond payments originate within DOR from annual local aid appropriations, it is critical that municipalities participating in the qualified bond program file the requisite documents with the Division of Local Services.

## **State Distributions to Pay Debt Service**

Ch. 44 §19A sets out a process to forestall a municipality's defaulting on a debt service obligation. If a treasurer believes that the municipality is, or is likely to be, unable to make an installment payment on a borrowing, the treasurer must notify the selectmen or mayor. If the selectmen or mayor concur, they must certify the inability or likely inability to the commissioner of revenue. If the commissioner concurs, the commissioner must immediately certify the inability to the state treasurer who must make the payment from state funds, up to the amount of the municipality's Cherry Sheet entitlement during that fiscal year. Any amounts paid are charged against the amount otherwise due from the state to the municipality.

### **Emergency Appropriation**

Ch. 44 § 8(9A) establishes a procedure by the Municipal Oversight Finance Board (MFOB) to approve the issuance of debt by a city or town to pay the costs of responding to an emergency for which borrowing would not otherwise be authorized. The MFOB consists of the State Auditor, the Director of Accounts, the Attorney General, and the State Treasurer. The statute defines an "emergency" as a "sudden, unavoidable event or series of events which could not reasonably have been foreseen or anticipated at the time of submission of the annual budget for approval."

The MFOB considers a situation to be an emergency only when a community possesses no other option to respond to urgent circumstances except to request authorization to borrow funds under this statute. The statute expressly declares that the funding of collective bargaining agreements or items that were previously disapproved by the appropriating authority for the fiscal year in which such borrowing is sought, cannot qualify as an emergency under its provision.

All requests for MFOB approval must be made in writing upon the majority vote of the city council or selectmen. A request must set forth in detail on prescribed forms:

- The amount and term of the requested loan.
- A detailed description of the emergency.
- All documents supporting the need for the loan.

The MFOB will only consider a request for the approval of an emergency loan when the process for authorizing debt in the manner otherwise provided by law imposes an undue hardship in its ability to respond to the emergency.

### **State School Building Assistance**

In July of 2004, the state legislature passed and the Governor signed a major redrafting of the School Building Assistance Program, creating a new Massachusetts School Building Authority, which functions as an independent public entity under the control of a seven member Board. The State Treasurer serves as chairman of the Board. While most of the State's priority setting standard is similar to that under the prior legislation, there are significant differences in reimbursement rates, application procedures and financing, which should be understood by every city, town and school district.

All cities, towns and school districts that are receiving reimbursements under the prior Authority will continue to receive them as previously scheduled. There will be no reduction in amounts, except those caused by the final state audit of the project. This is the same as the prior law and regulations.

School projects that were on the 2004 priority list were grandfathered. They were funded at the same percentage reimbursement rate as previously listed. The municipality was allowed to take advantage of the new rules and bond only its share of the project. Municipalities that have already bonded a project will continue to receive a yearly reimbursement according to the prior system schedule subject to adjustments upon completion of the final audit.

Municipalities submitting new projects are subject to the rules of the Mass. School Building Authority (MSBA). Effective July 1, 2007, municipalities can apply for State grants for their school projects under the new MSBA program. The Board will consider all the new applications, rank them using previously agreed upon standards, and approve the number of projects within their financial capability. The budget for the new School Building Authority is based on the revenues from one cent of the State sales tax. All other projects not approved must reapply the next year. There is no guarantee when or if a particular school project will be approved. Thus any municipality will be taking a significant risk if it starts a project before a grant is received. The grant will be paid as construction proceeds as reimbursement requests are reviewed and approved. A municipality can borrow short term, but only its own share of the project costs and the MSBA shall have no responsibility for the interest costs of such short term borrowing.

The MSBA program with its new reforms for state aid for school building construction is spelled out in Chapter 70B of the Massachusetts General Laws, as amended by the new legislation. This provides the legislative support for the Mass School Building Authority to receive applications, determine eligibility, rank, and approve the grants to cities, towns and districts to reimburse them for their school building costs. The purpose of the program is "To promote thoughtful planning and construction of school facility space in order to insure safe and adequate plant facilities for the public schools, and to assist towns in meeting the cost thereof."

The MSBA will enforce statutes and regulations pertaining to school building size and cost standards, reimbursement rates and a wide range of other issues. The legislation requires that reimbursement rates for all new (post July 1, 2007) projects be reduced by 10 percent. Thus the reimbursements changed from the 50% - 90% range to 40% - 80%.

For other information about the new program, a treasurer should contact the Massachusetts School Building Authority at 617 720-4466 as well as their financial advisor and bond counsel. Information can also be obtained from the M.S.B.A. online at [www.Massschoolbuilding.org](http://www.Massschoolbuilding.org)

### **Massachusetts Clean Water Trust**

The Massachusetts Clean Water Trust (MCWT) is the state agency established under the provisions of Ch. 29C to administer the Water Pollution Abatement Revolving Fund, set up

pursuant Ch. 29 §2L. This state revolving fund grants low-interest loans to communities, local governmental units and private water suppliers for the construction and rehabilitation of wastewater and drinking water treatment plants and related infrastructure.

The Water Pollution Abatement Trust is governed by a three-member board of trustees, consisting of the state treasurer, the secretary of administration and finance and the commissioner of the Department of Environmental Protection (DEP). It is funded through grants from the U.S Environmental Protection Agency, augmented with a 20% state matching appropriation.

Projects funded under the revolving fund program are eligible for varying levels of financial assistance in the form of loan subsidies. Because of these subsidies, many municipalities find it financially advantageous to issue bonds through the trust rather than to sell bonds on their own.

Municipalities can borrow both short term and long term through the trust. The city or town must authorize a borrowing through its town meeting or city council, obtain a preliminary legal opinion from bond counsel and fulfill all the requirements of DEP as well as the MCWT. Once approved the Municipality or District may request a short term loan, called an “Interim Loan,” which provides funds temporarily until the trust issues long term bonds. Once a loan is in place, the Municipality or District submits invoices associated with the project to DEP for approval. Once DEP approves an invoice, the trust will reimburse funds to the treasurer to pay the invoice costs.

### **Municipal Securities Disclosure Requirements**

The Federal Securities and Exchange Commission’s (SEC) Rule 15c2-12 requires underwriters participating in primary offerings of municipal bond and note issues of \$1,000,000 or more to obtain, review and distribute copies of disclosure documents to investors. This rule was designed to increase investors’ protection by requiring the disclosure to them of relevant information prior to their submission of bids. The rule contains timetables for distribution, as well as specific exemptions.



## Continuing Disclosure

Rule 15c2-12 of the Securities and Exchange Act of 1934, as amended, provides that underwriters may not purchase or sell municipal securities of an issuer unless the issuer undertakes to provide continuing disclosure over the life of the bonds, subject to certain exemptions. In order to make municipal bonds acceptable to the market, issuers covenant at the time of delivery of the bonds to provide continuing disclosure. The obligation of the issuer under the covenant is to provide certain financial information and operating data no later than a specified period following the close of each fiscal year, and to provide notices of the occurrence of certain enumerated events, if material.

The continuing disclosure information is required to be sent to all Nationally Recognized Municipal Securities Information Repositories (NRMSIR) and the appropriate State Information Depository (SID). Massachusetts does not yet have a SID. The Electronic Municipal Market Access database, a service of the Municipal Securities Rulemaking Board, was designated as the sole NRMSIR effective July 1, 2009. Most municipalities in Massachusetts contract with their financial advisor to submit the required continuing disclosure information on their behalf.

## Tax Reform

In 1986, the federal government, in fashioning a sweeping reform of the tax code, introduced various restrictions relating to municipal borrowing. The restrictions limited tax exempt debt, restricted purchasers of tax exempt securities, and imposed rules on arbitrage.

- **Tax-Exempt Debt:** The Tax Reform Act of 1986 instituted a clearer distinction between governmental-use and private-activity bonds. Governmental-use bonds are bonds issued to fund projects beneficial to the general public, such as schools, roads and public buildings. These bonds have tax-exempt status. Private-activity bonds, on the other hand, are bonds issued for purposes that benefit private parties. For example, bonds issued to construct a municipal building to be rented in substantial part to a third party would be private-activity bonds. These bonds are not tax-exempt. Treasurers should work with bond counsel to determine the tax status of their bond issues.
- **Restrictions on Financial institutions:** The tax reform act placed restrictions on certain buyers of tax exempt securities. Prior to this legislation, financial institutions could deduct most of the interest costs they incurred when investing in any municipal bonds. Under the reform act, financial institutions can only deduct a percentage (80%) of their purchasing and carrying costs for bonds of municipalities that do not issue more than \$10 million of bonds annually. Consequently, municipalities that issue a larger annual amount must contend with a more restrictive market when issuing bonds and notes, resulting in their paying higher interest rates.
- **Arbitrage:** Arbitrage limitations constitute a very significant impact of the tax reform act for cities, towns and districts. The legislation severely limits a municipality's ability to earn interest on borrowed funds. Prior to tax reform, treasurers could invest the proceeds of bonds and notes at higher rates in certificates of deposit, treasury bills and money market accounts to maximize earnings. The interest

earnings were usually greater than the interest cost the municipality paid on the borrowed money. These earnings went into the general fund and often meant significant revenue for the city or town.

The new law restricts interest earnings by requiring that investment income of borrowing proceeds higher than the interest expense that is being paid on the bond or note be paid as a rebate to the federal government. A community that fails to comply with this requirement risks losing the tax-exempt status of its securities, retroactive to the issuance date. This would be drastic for the community as the tax-exempt status allows bidders on debt to bid a much lower rate of interest for tax-exempt than taxable debt. Also, debt already sold would become taxable, creating great hardship for holders of the debt. The reputation and credit worthiness of the community would suffer greatly.

### **Arbitrage Rebate Exceptions**

The tax reform act provides exceptions that enable cities and towns in limited situations to earn interest on borrowings without having to pay a rebate. Interest earnings are not subject to rebate in the following circumstances:

- **Small Issuers:** No rebate is required with respect to governmental-use bonds and notes if the issuer can reasonably expect to issue no more than \$5 million in bonds and notes during the calendar year of issue. This limit applies to the total long and short-term debt originally issued during the year. It does not apply to renewals of prior loans. In addition, a municipality that issues \$5,000,000 or more in a year to finance certain public school facilities, the limit increases to \$10,000,000 for that year.
- **Expenditure Exceptions (Bonds and BAN Proceeds):** Even if a municipality is unable to qualify for the small issuer exception, it can nevertheless avoid a rebate under two circumstances:
  - A municipality can avoid rebating interest earnings if it expends 95% of the proceeds of a bond or note issue, including interest earnings, within 6 months and all of the proceeds and earnings within 1 year.
  - Alternatively, a municipality can avoid rebating interest earnings on construction bonds if it expends 10% of the proceeds and earnings within 6 months, 45% within 1 year, 75% within 18 months and 100% within 2 years. In the case of non-construction bonds, the community can avoid rebating interest earnings if it expends 15% within 6 months, 60% within 1 year and 100% within 18 months. The exception provisions also permit an issuer to pay a penalty rather than a rebate if these schedules are not satisfied.
- **Revenue Anticipation Notes:** A municipality is not subject to rebating interest earned on notes issued to cover anticipated tax or grant receipts if the accumulated cash flow deficit exceeds 90% of the face amount of the notes within 6 months of the date of issue. Eligibility for this exemption is not based on the expectation at the time of issuance. Accordingly, if the actual deficit does not turn out to exceed 90% of the face amount of the notes, the municipality must pay an arbitrage earnings rebate.

## Effects of Tax Reform on Municipal Debt

Federal tax reform legislation has made the issuance of tax exempt debt more expensive, complex and time consuming for cities and town. The restrictions that prevent financial institutions from deducting some of their costs when investing in municipal bonds have increased municipal costs when issuing debt. The arbitrage rules that limit the investment of the proceeds of tax-exempt bonds and notes have resulted in the loss of interest earnings. Moreover, the complexity of the legislation has increased the need for municipalities to rely on the expertise of financial advisors and attorneys, significantly increasing borrowing costs, as well.

Besieged with the many pitfalls that currently beset municipal borrowing, a treasurer when issuing debt, can best serve the interests of the municipality by undertaking the following activities:

1. Meet with the financial advisor at the beginning of each year to plan the timing and sizing of note and bond issuance. Communicate regularly with the financial advisor and bond counsel as financing needs change during the course of each year.
2. Review each project for a potential private activity that may threaten the tax-exempt status of municipal debt. Try to think ahead. Do not hesitate to raise questions with bond counsel before issuing debt.
3. Stay alert about proposals for debt authorization, mailing of tax bills, revaluation delays, impending large expenditures and other matters that could affect borrowing requirements and cash flow.
4. Educate local officials, particularly assessors and department heads, about federal tax reform law. Encourage department heads to prepare cash flows relating to capital expenditures in an effort to keep borrowing to a minimum.
5. Ensure that assessors and the tax collectors have sufficient resources for timely mailing and processing of tax bills in order to reduce the need for tax anticipation borrowing. Recommend utilizing estimated tax bills if actual tax bills will be significantly delayed.
6. Try to avoid late fall town meetings, which delay the setting of the tax rate and often necessitate the issuance of tax anticipation notes.
7. Attempt to keep the size of bond issues down by funding equipment and minor renovations in the operating budget rather than from bond proceeds. If this is not possible, consider utilizing the capital outlay exclusion provided in Proposition 2½. [59:21C(i½)]
8. Encourage all department heads to implement a policy whereby major discretionary expenditures are scheduled for a time when the municipality is in a positive cash position.
9. Schedule due dates for bond issues for times of positive cash flow.
10. Encourage the establishment of a capital financing plan to even out borrowing from year to year. This will provide a better chance of complying with statutory

requirements and will provide for a reasonable, long term financing plan for capital projects.

<b>BORROWING WITHIN THE DEBT LIMIT – MGL c.44 §7</b> <b>Maximum Term is Statutory Maximum Term, or DLS Authorized Maximum Term if longer</b>				
Clause	Borrowing Purpose	Statutory Limits/ Approvals	Statutory Maximum Term	DLS Authorized Maximum Term
1	<p>Acquisition of an interest in land for any purpose a city or town authorized to acquire land or interests in land, provided the land or the interest in land has a useful life of at least 5 years</p> <p>Landscaping alteration, remediation, rehabilitation, or improvement of land owned by a city or town, provided the project has a useful life of at least 5 years</p> <p>Dredging, improvement, restoration, preservation or remediation of public waterways, lakes or ponds, provided the project has a useful life of at least 5 years</p>		Useful life of asset or project, not to exceed 30 years	30 Years
1	Acquisition of equipment or other assets, provided the equipment or other asset has a useful life of at least 5 years		Useful life of asset or project, not to exceed 30 years	<p>20 Years</p> <p>Equipment or asset must cost \$5,000 or more than per unit</p> <p>CEO determines 5-20 maximum term based on useful life of equipment or asset</p>
1	Construction, reconstruction, rehabilitation, improvement, alteration, remodeling, enlargement, demolition, removal, or extraordinary repair of municipally owned buildings, facilities, assets, works or infrastructure, provided the project has a useful life of at least 5 years, including (i) the cost of original equipment and furnishings of the building, facilities, assets, works, or infrastructure, (ii) damages under chapter 79 resulting from any such acquisition or project, and (iii) the cost of engineering, architectural or other services for feasibility studies, plans, or specifications as part of any acquisition or project		Useful life of asset or project, not to exceed 30 years	<p>30 years – for projects relating to construction, reconstruction, rehabilitation, improvement, alteration, remodeling, enlargement, demolition, removal or extraordinary repairs of municipal buildings, facilities, works or infrastructure</p> <p>15 years – for projects relating to construction, resurfacing, reconstruction, improvement, repair, paving, resurfacing, extending, or widening public ways or municipally owned parking lots</p> <p>5 years – for projects relating to construction, reconstruction, rehabilitation, improvement, alteration, remodeling, enlargement,</p>

## Borrowing

				demolition, removal or extraordinary repairs of other municipal assets not described above
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Clause	Borrowing Purpose	Statutory Limits/ Approvals	Statutory Maximum Term	DLS Authorized Maximum Term
2	Funding the revolving loan fund established under MGL c.44 §53E¾ to assist in the development of renewable energy and energy conservation projects on privately-owned buildings, property or facilities within the city or town		20 Years	
3	Paying final judgments		1 year or longer if approved by MFOB	
4	In Boston only, constructing (original), extending or widening ways other than public ways, within, bounding or connecting with public park in the city by the board of park commissioners for the city, with permanent pavement of a lasting character conforming to specifications approved by MDOT, including land damages and cost of pavement and sidewalks laid at the time of construction; or constructing the ways with stone, block, brick, cement concrete, bituminous concrete, bituminous macadam or permanent pavement of similar lasting character under the specifications approved by MDOT		10 Years	No change
5	Cost of repairs to private ways open to the public under MGL c.40 §6N		5 Years	No change
6	Making payments under contracts with the Commonwealth under MGL c.40 §4D for purposes for which loans may be authorized under this section	Same as borrowing purpose	Same as borrowing purpose	
7	Paying for feasibility studies or engineering or architectural services for plans and specification for any proposed project for which a city, town or district is authorized to borrow.		5 Years – if issued before debt for the project is authorized Otherwise, same as the project	
8	Paying for energy audits as defined in MGL c.25A §3, if authorized separately from debt for energy conservation or alternative energy projects		5 Years	No change
9	Development, design, purchase and installation of computer hardware or software and computer-assisted integrated financial management and accounting systems		10 Years	No change

**Borrowing**

10	Cleaning up or preventing pollution caused by existing or closed municipal facilities not referenced in clause (20) of section 8, including cleanup or prevention activities taken pursuant to chapter 21E or chapter 21H	DEP must approve project plans before debt is issued	10 Years	No change
11	For other public work, improvements or asset not specified in this section with a maximum useful life of at least 5 years		10 Years	No change

**BORROWING OUTSIDE THE DEBT LIMIT – MGL c.44 §8****Maximum Term is Statutory Maximum Term, or DLS Authorized Maximum Term if longer**

<b>Clause</b>	<b>Borrowing Purpose</b>	<b>Statutory Limits/ Approvals</b>	<b>Statutory Maximum Term</b>	<b>DLS Authorized Maximum Term</b>
1	Temporary loans under MGL c.44 §§ 4, 6, 6A, 17		Per applicable § 4, 6, 6A, 17	
2	Providing and distributing food, temporary shelter and other necessities of life during emergencies under MGL c.40 §19		2 Years	
3	Establishing or purchasing a water supply system; taking or purchasing water sources, either from public land or private sources, water or flowage rights, or land for the protection of water system		30 Years	
3A	Conducting groundwater inventory and analysis of the water supply, including pump tests and quality tests, in connection with the development of new or additional water supply sources		10 Years	
4	Constructing or enlarging reservoirs; constructing filter beds, construction or reconstruction or making extraordinary repairs to standpipes, buildings for pumping stations including original pumping stations equipment, and buildings for water treatment, including original equipment; and acquiring land or any interest in land necessary in connection with those proposes		30 Years	
4A	Remodeling, reconstructing or making extraordinary repairs to reservoirs and filter beds	DEP must approve project plans before debt issued	30 years	
5	Construction or reconstructing, laying or relaying aqueducts or water mains, or for lining or relining such mains and for the development or construction of additional well fields and for wells		40 Years	
6	Purchasing and installing water meters		10 Years	No change
7	Paying share of municipality's cost to increase the storage capacity of any reservoir, including land acquisition, constructed by water resources commission for flood prevention or water resources utilization		20 Years	30 Years
7A	Purchasing, replacing or rehabilitating water departmental equipment		10 Years	No change
8	Establishing, purchasing, extending, or enlarging a municipally-owned gas or electric lighting plant, community antenna television system or a telecommunications system		20 Years	No change
8A	Remodeling, reconstructing, or making extraordinary repairs to a municipally-owned gas or electric lighting plant, community antenna television system or	MFOB must approve debt and term	10 years	No change



	telecommunications system			
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Clause	Borrowing Purpose	Statutory Limits/ Approvals	Statutory Maximum Term	DLS Authorized Maximum Term
9	Emergency appropriation approved bby Director of Accounts  Borrowing may be authorized by (1) treasurer, with the approval of chief executive officer, town or district under expedited procedure or (2) regular procedure  Emergency means sudden, unavoidable event or series of events which could not reasonably have been foreseen or anticipated at the time of submission of the annual budget for approval and does not include funding of collective bargaining agreements or items previously disapproved by the appropriating authority for the fiscal year in which the borrowing is sought	Director of Accounts must approve debt	2 years  Director of Accounts may approve term up to 10 years based on the evaluation of city, town or district financial ability	
9A	Emergency appropriations for capital purposes authorized by treasurer, with approval of chief executive officer, of city, town or district under expedited procedures  Emergency means a sudden, unavoidable event or series of events which could not reasonably have been foreseen or anticipated at the time of the submission of the annual budget for approval	MFOB must approve debt  City, town or district must demonstrate use of regular debt authorization process poses undue hardship in meet emergency	MFOB approved term that may not exceed tern for borrowing purpose	
10	Acquiring land or constructing buildings or other structures including the cost of original equipment as memorials to members of the army, navy, marine corps, coast guard, or air force		20 Years	30 years
11	Acquiring street railway property und MGL c.161 §§ 143-158 operating the same, or contributing toward the capital expenses of a transportation area		10 Years	No change
12	Acquiring, constructing, establishing, improving or protecting public airports, including acquiring land, including those airports jointly owned by two or more municipalities		10 years	30 years
13	Eradicating Dutch elm decease, including payment of assessments and charges made under MGL c.132		10 years	No change
14	Constructing sewers, sewerage systems and sewage treatment and disposal facilities; or making a lump sum payment of the cost of tie-in to those services in a contiguous city of town	MFOB must approve debt unless city or town has a self-supporting sewer enterprise or special revenue fund, as certified by municipal accounting officer	30 Years	No change
15	Constructing and rehabilitating municipal golf courses, including acquiring and		20 Years	No change

**Borrowing**

	reconstructing land, installing and replacing irrigation systems, constructing and rehabilitating buildings and paying for equipment and furnishings.			
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<b>Clause</b>	<b>Borrowing Purpose</b>	<b>Statutory Limits/ Approvals</b>	<b>Statutory Maximum Term</b>	<b>DLS Authorized Maximum Term</b>
16	Making payments under contracts with the Commonwealth under MGL c.40 §4D for purposes for which loans may be authorized under this section	Same as borrowing purpose	Same as borrowing purpose	No change
17	Constructing a regional incinerator for disposal of solid waste refuse and garbage by two or more communities		20 Years	No change
18	Lending or granting funds to industrial development financing authorities and economic development and industrial corporations	Mass Office of Business Development and Dept. of Housing & Community Development must approve debt	20 years	
19	Undertaking projects fully or partially financed by the Farmers Home Administration of the United States Department of Agriculture under chapter 50 of Title 7 of the United States Code		40 Years	
20	Cleaning up or preventing pollution caused by existing or closed landfills or other solid waste disposal facilities, including clean-up activities under MGL c.21E or MGL c.21H	DEP must approve project plans before debt issued	30 Years	
21	Constructing incinerators, refuse transfer facilities, recycling facilities, composting facilities or other solid waste disposal facilities, other than landfills, owned by the city, town or district, and used for disposing of waste, refuse and garbage	DEP must approve project plans before debt issued	25 years	No change
22	Remodeling, reconstructing or making extraordinary repairs to incinerators, refuse facilities, recycling facilities, resource recovery facilities or other solid waste disposal facilities, other than landfills, owned by the city, town or district and used for disposing of waste, refuse and garbage	DEP must approve project plans before debt issued	10 Years	No change
25	Closing out a landfill area, opening a new landfill area, or making improvements to an existing landfill area	DEP must approve project plans before debt issued	25 Years	No Change
24	Acquisition of a dam or the removal, repair, reconstruction and improvements to a dam owned by a municipality, as may be necessary to maintain, repair or improve such dam. Includes dams, as defined by MGL c.253 §4, and appurtenant real property, acquired by gift, purchase or eminent domain not owned or held in trust by Commonwealth when the municipality acquires them		40 Years	

**SCHOOL PROJECTS APPROVED BY SCHOOL BUILDING AUTHORITY  
– MGL c.70B §6**

**Maximum Term is Statutory Maximum Term, or DLS Authorized Maximum Term if longer**

<b>Borrowing Purpose</b>	<b>Statutory Maximum Term</b>	<b>DLS Authorized Maximum Term Based on Useful Life</b>
Undertaking a school construction project approved for school facility grant	25 Years	30 years – same as MGL c.44 §7(1)
Undertaking a feasibility study required to apply for school facility grant	5 Years	

**REGIONAL SCHOOL DISTRICTS – MGL c.71 §16(d) and (n)**

**Maximum Term is 30 Years, or DLS Authorized Maximum Term if shorter**

<b>Borrowing Purpose</b>	<b>Statutory Maximum Term</b>	<b>DLS Authorized Maximum Term Based on Useful Life</b>
Acquiring land	30, or DLS term if shorter	No change – same as MGL c.44 §7(1)
Constructing, reconstructing, adding to and equipping school building	30, or DLS term if shorter	No change – same as MGL c.44 §7(1)
Remodeling and making extraordinary repairs to school building	30, or DLS term if shorter	No change – same as MGL c.44 §7(1)
Constructing sewerage systems and sewerage treatment and disposal facilities; purchasing or using municipal sewer system capacity	30, or DLS term if shorter	No change – same as MGL c.44 §7(1); c.44 §7(14)
Acquiring departmental equipment	30, or DLS term if shorter	20 Years – same as MGL c.44 §7(1) Equipment or asset must cost \$5,000 or more per unit CEO determines 5-20 maximum term based on useful life of equipment or asset
Constructing, reconstructing or making improvements to outdoor playgrounds, athletic or recreational facilities	30, or DLS term if shorter	30 years – same as MGL c.44 §7(1)
Constructing, reconstructing or resurfacing roadways and parking lots	30, or DLS term if shorter	15 years – same as MGL c.44 §7(1)
Constructing other public works or improvements of a permanent nature	30, or DLS term if shorter	30 years – same as MGL c.44 §7(1)
Paying for planning, architectural or engineering services related to any of the purposes above if issued before debt for project authorized	30, or DLS term if shorter	5 years – same as MGL c.44 §7(1)
Paying for planning, architectural or engineering services related to any of the purposes above	30, or DLS term if shorter	Same as project debt – same as MGL c.44 §7(1)

## Calculation of Net Interest Cost - NIC

Company: **Bid-A-Lot**

Principal: \$5,000,000 (1) Principal Payment =  $\$5,000,000 \div 5 \text{ years} = \$1,000,000$   
 Term: 5 years  
 Principal Payment: \$1,000,000  
 Premium Paid: \$125,000

(2)		(3)	(4)	(5)	(6)
Principal Outstanding	Interest Quoted	Sum of Rates	Life Remaining	Weighted Rate	Interest Cost
\$5,000,000	3.75%	22.95%	5	4.59%	\$229,500
\$4,000,000	4.25%	19.20%	4	4.80%	\$192,000
\$3,000,000	4.60%	14.95%	3	4.98%	\$149,500
\$2,000,000	5.10%	10.35%	2	5.18%	\$103,500
\$1,000,000	5.25%	5.25%	1	5.25%	\$ 52,500
			15		
	(7)	Average Life:	3		\$ 727,000
		15 / 5		Less: Premium	<u>\$ (125,000)</u>
			(8)	Net Interest Paid	\$ 602,000
				(9)	NIC 4.01%

- (1) Calculate the principal payment, assume Level Principal unless otherwise stated
- (2) Calculate the outstanding principal for each year  
 Ex: \$5,000,000 year 1, less \$1,000,000 for each year  
 \$4,000,000 year 2, etc. as shown above
- (3) Add the sum of interest rates for years remaining  
 Reduce by first year rate on second line, second year rate on third line, etc.
- (4) Fill in life remaining in descending order: 5, 4, 3, 2, 1
- (5) Divide the Sum of Rates by Life Remaining  
 Ex:  $22.95\% \div 5 = 4.59\%$
- (6) Calculate Interest by Multiplying Weighted Rate x Principal Outstanding  
 Ex:  $\$5,000,000 \times 4.59\% = \$229,500$
- (7) Calculate average life of Note or Bond  
 Ex:  $\sum \text{of Years} \div \text{Term} = \text{Average Life}$   $(5+4+3+2+1) \div 5 = 3$
- (8) Total Interest Paid and subtract Premium = Net Interest Paid
- (9) Net Interest Cost = Net Interest Paid / Average Life / Principal  
 Ex:  $\$602,000 \div 3 \div \$5,000,000 = 4.01\%$

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## **Chapter 10**

# **Financing Capital Improvements**

### **Overview**

The need to improve the nation's infrastructure has evolved into a major public policy concern at the federal, state, and local levels. Like municipalities in other states, Massachusetts cities and towns have experienced impairments in their respective capacities to fulfill infrastructure needs, due to reductions in state and federal construction grants and to limitations in the local and state budgets. The constraints of Proposition 2½ (59:21C) have significantly exacerbated the problem.

Under Proposition 2½, cities and towns find it increasingly difficult to fund capital expenditure debt within tightened operating budgets. Accordingly, many local officials have deferred capital projects in order to sustain their operating budgets. Moreover, as debt has been retired, municipalities have utilized "freed up" monies to pay operating expenses, thereby diminishing further the capital expense portion of the budget. This conduct has inevitably led to inadequate maintenance, repair, replacement and expansion of local infrastructure.

Deferring infrastructure maintenance and improvement, of course, only compounds municipal financial woes, enormously increasing the cost of performing such work in the future. Inescapably, such delay leads inevitably to a diminution in the scope and quality of public services. Every city and town owes to the future the maintenance of its infrastructure in the present.

### **Capital Improvements Programs**

Although not intrinsically responsible for capital planning, the treasurer, as a critical member of any community's financial team, should play a central role in such planning.

Every community should have a capital improvements program (CIP)<sup>[111](#)</sup>, coordinating the city or town's planning, financial capacity and physical development. Any community lacking such a program should move precipitously to develop one. The process might commence with the community's defining "capital asset" since no commonly accepted definition of this term exists. Most would agree that a capital asset must be of significant value and have a useful life of several years. Accordingly, CIP planning should establish working definitions for these terms. Perhaps a capital asset would be defined as a tangible property with a value of at least \$10,000 and a useful life of at least five years.

A capital improvements program should include both a capital "budget," i.e., a spending plan for capital items for the upcoming year, and a capital "program," i.e., a plan for capital expenditures that extends some number of years, perhaps five, beyond the upcoming year.

Developing a sound CIP requires devoted and effective leadership and the amenable involvement and cooperation of all municipal departments. Accordingly, with skilled leadership and broad cooperation critical to success, the community's chief executive officer should serve as chairperson.

The benefits of a successful capital improvement program include the following:

- Preservation of capital assets
- Coordination of capital needs and operating budgets.
- Soundness of municipal credit rating.
- Stabilization of tax rate and debt costs.
- Increase in federal and state aid.

### Steps in Implementing a Capital Improvements Program

In developing a capital improvements program, a city or town should undertake the following steps. (See also *Developing a Capital Improvements Program: A Manual for Massachusetts Communities*, prepared by the Municipal Data Management and Technical Assistance Bureau, found in the Addendum of this manual and at the Department of Revenue website, [www.mass.gov](http://www.mass.gov).)

1. Town meeting/city council adopt(s) a CIP bylaw.
2. Mayor/selectmen appoint(s) a CIP committee.
3. CIP committee:
  - a. Prepares an inventory of facilities and equipment, specifying for each item its current condition.
  - b. Determines the status of previously approved projects, researching the funding situation of each.
  - c. Assesses the community's capability to fund capital projects.
  - d. Solicits, compiles, and evaluates departmental requests for capital projects and equipment.
  - e. Establishes a priority for capital needs.
  - f. Develops a CIP financing plan that recommends a method of financing for each proposed project
  - g. Submits proposed plan, including recommendations for the upcoming year's capital budget and for capital expenditures for the several following years, to the mayor/selectmen for consideration.
4. Mayor/selectmen consider(s) plan and forward(s) it, with any recommended amendments, to finance committee/city council.
5. Finance committee/city council reviews plan and makes recommendation on budget issues.
6. Town meeting/city council adopts plan.

## **Financing Capital Improvements**

7. Mayor/selectmen monitor(s) implementation of plan.
8. CIP committee initiates annual updating cycle by reviewing existing plan, making new recommendations and submitting recommendations to mayor/selectmen.

## **Role of the Treasurer — Identifying and Evaluating Financing Options**

The treasurer's role consists of contributing information about financing strategies to the CIP committee to assist in developing a plan to fund capital improvements. In this role, the treasurer should acquaint the CIP committee with the following persons and agencies that can provide particular knowledge and expertise in municipal finance matters:

- **Division of Local Services, Massachusetts Department of Revenue**

This state governmental agency possesses statutory responsibility and authority to oversee and to provide assistance to cities and towns. Its attorneys, in the Bureau of Municipal Finance Law, and its local finance experts, in the Bureau of Accounts, are readily available to provide legal and financial information and advice on all aspects of municipal government.

The Division also maintains a municipal data bank, which contains an extensive aggregate of information relating to cities and towns. This resource can be assessed in a variety of ways, including via the Internet, and can be very useful in analyzing and comparing a city or town's financial condition.

In addition, its Bureau of Accounts issues "state house notes," debt instruments for cities and towns, certified by the Director of Accounts. The notes are generally less costly and easier to issue than conventional issues for borrowing. They are commonly used for temporary loans and smaller long-term issues.

- **Bond Counsel**

These specialized law firms provide expertise in municipal borrowing matters. Their attorneys guide cities and towns through the involved process of issuing debt. They also issue legal opinions to the purchasers of municipal bonds and notes, advising them about the legal and tax status of such debt instruments.

- **Financial Advisor**

These finance experts possess particular expertise in municipal finance, municipal borrowing and the municipal securities market. Financial advisors guide cities and towns through the planning, authorization and issuance of debt.

## **Debt Planning**

As part of debt planning, a municipality must accomplish three things. First, it must determine how it will pay debt costs. Second, it must obtain authority to incur debt from the town meeting or city council. Finally, it must carry out the actual issuance process.

### Ability to Pay

Municipalities must choose from among three possible options in funding the debt service of a significant project. These include:

- Paying the debt costs from the existing operating budget.
- Dedicating some specific revenue source, such as water and sewer receipts, to payment of the debt costs.
- Obtaining debt exclusion authority under Proposition 2½ and paying the debt costs from the additional levy capacity.

### Absorbing the Debt Service within the Operating Budget

With most cities and towns levying at or near levy capacity, few municipalities can accommodate the payment of new debt costs from existing operational budgets without the necessity of making substantial cuts in existing programs. For loans requiring repayment with annual *principal* payments, the interest due each year regularly declines, freeing up some additional money in each year's budget during the term of the debt. Most loan repayments, however, are structured with equal annual payments, combining interest and principal. In these cases, only in years following the ultimate retirement of an existing debt issue can an operational budget generally absorb new debt costs.

### Designated Revenues

Municipalities sometimes incur debt to pay for capital projects of municipal departments that generate revenue from user fees, such as water and sewer departments. In such an instance, a municipality, in cooperation with the rate-setting authority of the particular department, might decide to pay some or all of the debt costs from those fees. Instead of issuing revenue bonds, however, municipalities in such instances generally issue general obligation debt upon the full faith and credit of the municipality because general obligation debt may be obtained at a lower interest rate and substantially lower issuance costs. This is the most common procedure in Massachusetts.

In cases in which a municipality incurs debt to fund improvements for a limited and determinable area, the municipality might decide to pay debt costs from betterment assessments made upon property owners in those areas. (80:1)

When municipalities incur debt for particular projects, such as school construction, library construction or water pollution abatement, they are entitled to receive partial reimbursement from a particular state grant. School construction grants are awarded under Ch. 70B. Under this grant program, the state reimburses communities a set percentage of the total eligible construction cost, including both principal and interest, over the life of the school construction debt. (See Chapter 9 for additional information about the school building assistance program.) Through its board of library commissioners, the state also provides grants to cities and towns for assistance in constructing facilities to be used as free public libraries (78:19H-19K) and for water pollution abatement projects (29C).

## **Financing Capital Improvements**

### **Proposition 2 ½ Debt Exclusions**

In a community levying at or near capacity, and therefore unable to fund debt costs for a proposed project from its operating budget, the selectmen, or council, with the mayor's approval, may vote, by a two-thirds vote, to seek voter approval at a regular or special election to exempt the debt payment from the Proposition 2½ levy limit. [59:21C(k)] If the voters give approval, all debt costs for the project, both long and short-term, will be excluded from the city or town's levy limit. Once the debt costs have been fully paid, however, the exclusion authority lapses. (See IGR No. 02-101 titled *PROPOSITION 2 ½ DEBT EXCLUSIONS* in the Addendum of this manual. It can also be found on the DLS website, [www.mass.gov/dls](http://www.mass.gov/dls))

### **Managing Debt**

Municipalities must be diligent in planning and controlling the aggregate of their outstanding debt. The impact of a community's incurring unanticipated debt may be severe. Even though the city or town may approve a Proposition 2½ debt exclusion, the attendant tax increase might very well diminish the taxpayers' willingness to support future projects. Therefore, as part of its capital planning process, every community should develop a strategy dealing with the issuance, timing and tax impact of current and future debt. All finance officials, including the treasurer, selectmen or mayor, capital planning committee, and the community's financial advisor, should collaborate in developing the strategy. As part of their planning, these officers should constantly monitor the impact of state and federal legislation and administrative rulings on municipal finances. They should also consider debt issuance practices of other relevant governmental agencies, such as regional school districts, and water/sewer districts, and discuss these practices in their planning.

Formalizing planning about municipal debt should not result in necessary project's not obtaining approval; rather, systematizing planning should, through its effect upon controlling a community's borrowing costs and property tax rate growth, help ensure a financial environment which permits carrying out necessary projects, while minimizing taxpayer distress.

Some communities, as part of their debt maintenance strategy, place all capital projects with a cost in excess of some established amount before the voters at a referendum for a Proposition 2½ exemption vote. Others fund a base level of all capital debt within the general operating budget. Still others set an amount that will be borrowed annually for capital projects within the general operating budget. Communities possess broad discretion in their borrowing practices and strategies.

### **Common Financing Options for Capital Improvement Projects**

Prior to commencing a borrowing, municipal officials, in consultation with their financial advisor, should carefully determine the timing, size and category of borrowing that would best fulfill the community's needs. Their decisions should take into account the community's credit status, the current and anticipated conditions of the bond market, and the capacity of the community's budget to accommodate increased debt service payments. Available debt options include the following debt instruments:

1. General Obligation Bond — A written promise to pay a specified sum of money, called the face value (par value) or principal amount, at a specified date in the future, called the

## **Financing Capital Improvements**

maturity date, together with periodic interest at a specified rate, issued by a municipality and backed by the full faith and credit of its taxing authority. A bond requires an opinion by bond counsel on its legal aspects and tax status unless it is issued through the Bureau of Accounts as a State House Serial Note.

2. Note — A short-term loan, typically with a maturity date of a year or less. It can be issued as State House Notes or with disclosure and a bond counsel legal opinion. If the authorization is greater than \$ 500,000, the Bureau of Accounts will require a preliminary legal opinion from bond counsel for State House Notes.
3. Bond Anticipation Note (BAN) — A short-term note to provide cash for initial project costs issued in anticipation of bond proceeds. BANs may be issued for a period not to exceed five years, provided principal repayment begins after two years (44:17). The final maturity date of the project borrowing, beginning from the date the short-term note was issued, may not exceed the term specified by statute. (44:7 & 8) BANs are full faith and credit obligations.
4. State Aid Anticipation Note (SAAN) — A short-term loan issued in anticipation of a state grant or aid. (44:6A). SAAN'S are full faith and credit obligations.
5. Federal Aid Anticipation Note (FAAN) — A short-term loan to be paid off at the time of receipt of a federal grant. FAANs are full faith and credit obligations.

### **Summary of Short and Long-Term Options**

The tables on the following pages summarize short and long-term options available. Each of the options embodies both benefits and drawbacks and must be examined in the context of the financing needs of the particular project.

## Financing Capital Improvements

### Comparison of Short Term Debt Financing Options

<b><u>Criteria</u></b>	<b><u>Internal Borrowing</u></b>	<b><u>State House Loan Notes</u></b>	<b><u>Notes with Legal Opinion</u></b>	<b><u>Interim Loans – SRF</u></b>
<b>Issuer</b>	City, Town or District	City, Town or District	City, Town or District	City, Town or District
<b>Credit Quality</b>	City, Town or District	City, Town or District	City, Town or District	City, Town or District
<b>Reserve Fund</b>	No	No	No	No
<b>Administrative Requirements</b>	Very Low	Low	Moderate	High to Start
<b>Term (Maximum Feaseable)</b>	Until 6/30	1 Year	1 Year	Until Bond Issue
<b>Flexibility: Timing &amp; Structure</b>	Very High	High	High	High
<b>Flexibility: Refinancing</b>	Very High	High	High	High
<b>How Marketed</b>	Internally	Competitive	Competitive	Private Placement
<b>Market</b>	Local Treasury	Local	Local & National	State Agency
<b>Costs: Issuance Costs</b>	None	Low	Low to Moderate	Low
<b>Costs: Interest Costs</b>	Cash Investment Rate	Low to Moderate	Low	Very Low



## Comparison of Long Term Debt Financing Options

<u>Criteria</u>	<u>Bans &amp; Paydowns</u>	<u>Lease Purchase</u>	<u>State House Serial Notes</u>	<u>Farmers Home Loans</u>	<u>State Revolving Fund Loans</u>	<u>Mini-Bonds</u>	<u>Municipal Bond Issue</u>
<b>Issuer</b>	City, Town or District	City, Town or District	City, Town or District	City, Town or District	State Agency M.W.P.A.T.	City, Town or District	City, Town or District
<b>Credit Quality</b>	City, Town or District	City, Town or District	City, Town or District	City, Town or District	Municipalities, Local Aid Intercept & Reserves	City, Town or District	City, Town or District
<b>Reserve Fund</b>	No	No	No	No	Yes	No	No
<b>Administrative Requirements</b>	Very Low	Low	Low	Moderate	High	Very High	Moderate
<b>Term (Maximum Feaseable)</b>	5 Years	10 Years	10 Years	40 Years	30 Years	5 Years	20 Years
<b>Flexibility: Timing &amp; Structure</b>	Very High	High	High	High	Very Low	Very Low	High
<b>Flexibility: Refinancing</b>	Very High	Depends	None	High	Limited	None	High
<b>How Marketed</b>	Competitive	Private Placement	Competitive	Private Placement	Negotiated	Over the Counter	Competitive
<b>Market</b>	Local	Limited Local	Limited Local	Federal Government	National	Private Citizens	Local & National
<b>Costs: Issuance Costs</b>	Very Low	Low	Low	Low	Low to Moderate	High	Moderate
<b>Costs: Interest Costs</b>	Low (Short Term)	Very High	High (Limited Market)	Moderate (Depends on Category)	Low (Subsidized)	Moderate	Moderate

### Financing Capital Projects at the Best Interest Rate—How Bond Analysts Evaluate Municipalities

Bond analysts, such as Moody's, Standard & Poor's, and Fitch closely review a number of indicators when evaluating a municipality's credit risk. Treasurers, therefore, should thoroughly understand

## **Financing Capital Improvements**

these factors in order to assist them in securing the best credit rating and interest rates for their municipalities. The indicators fall within four, basic areas:

1. Debt structure and burden
  - Long-term debt
  - Long-term debt as a percent of full valuation
  - Debt service as a percent of operating revenue
  - Long-term debt per capita
  - Yearly debt retirement schedules (i.e., the uniformity of annual debt costs)
  - Debt authorized but not yet issued
  - Over-lapping debt, such as the town's portion of debt incurred by a regional school district.
  - Short-term debt
  - Unfunded pension obligations
  - Unfunded other retirement benefit obligations such as health care
2. Financial factors
  - Unrestricted cash reserves
  - Revenue sources
  - Fixed costs as a percent of operating expenditures
  - Actual vs. estimated local receipts
  - Property tax levy vs. levy limits
  - Property tax collections rate
  - Operating deficit or surplus
  - Liquidity
  - User fees
3. Economic health
  - Full valuation of real and personal property
  - Location and natural resources
  - Size and land use characteristics
  - Population change and ages
  - Income
  - Housing characteristics
  - Growth in residential/commercial tax base
  - Unemployment
  - Tax base
4. Management practices

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- Professional management capability (including capital improvement programs and revenue and expenditure projections)
- Accounting record-keeping and auditing
- Municipal services provided
- Intergovernmental relations
- Assessment of property
- Tax administration
- Legal and regulatory limitations
- Litigation cases and pending litigation

By monitoring these factors at least annually, treasurers and other financial officials can help their communities to improve, or at least maintain, their credit positions and to choose capital expense financing strategies most suited to their communities' circumstances. (See Chapter 9 for bond rating information)

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<sup>[1]</sup>Ch. 41 §106B permits a town to establish a capital planning committee by bylaw.

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## **Chapter 11**

# **Effective Cash Management**

### **Importance of Cash Management**

Ch. 44 §55B requires that all municipal monies, except those required to be kept liquid for purposes of distribution, be productively invested at the “highest possible rate reasonably available, taking account of safety, liquidity, and yield.” Liquidity is the quality of being readily convertible into cash without substantial transaction costs. Security is the quality of assurance that the investment expectation will be fulfilled in a timely fashion. Yield is the measure of effective return on an investment, usually expressed as a percent. Accordingly, each municipal treasurer possesses a legal obligation to invest wisely, prudently, and effectively. This goal can be achieved through the implementation of an effective cash management program.

Cash management consists of taking the necessary actions to maintain adequate levels of cash to meet operational and capital requirements and to obtain the maximum yield on short-term investments of pooled, idle cash. A good cash management program is a very significant component of the overall financial management of a municipality. Such a program benefits the city or town by increasing non-tax revenues, improving the control and superintendence of cash, increasing contacts with members of the financial community and lowering borrowing costs, while at the same time maintaining the safety of the municipality’s funds.

### **The Goals of Cash Management**

The primary goals of a good cash management system are:

- To maintain adequate monies at hand to meet the daily cash requirements of the municipality while maximizing the amount available for investment and providing for the safety of the funds
- To obtain the maximum earnings on invested funds while ensuring their safety.

In order to reach these primary goals, a treasurer should strive to:

1. Develop strong, internal control of cash receipts and disbursements.
2. Develop an Investment Policy
3. Establish improved procedures for collecting outstanding taxes.

4. Establish clear lines of communication between the treasurer and department heads.
5. Develop solid professional relationships with local bankers and other members of the investment community.

## Elements of an Effective Cash Management Program

### Bank Relations

The treasurer should strive to be constantly aware of the range of services available from area banks. Since banks' service charges and investment rates vary, the treasurer should regularly evaluate the charges and rates of the banks used by the municipality to make certain that continuing to utilize these banks best serves the interests of the municipality. When selling bonds or notes, the treasurer should endeavor to receive a sufficient number of bids to ensure competitive rates for the borrowed funds. Whether borrowing or investing monies, the treasurer should solicit bids from at least three area banks.

The treasurer should critically review bank statements for treasury checking accounts and should funnel all activity into one account when possible. Also, the treasurer should utilize a uniform system of forms and procedures for all collection, deposit, and disbursement activities. (See Chapter 12, "Procuring Banking Services," for more detailed information about banking relationships.)

### Cash Flow Statements

As a component of implementing an effective cash management program, the treasurer must prepare a cash flow statement, also called a cash budget. Cash budgeting involves the estimation of cash receipts and cash disbursements to determine cash availability. A treasurer can best identify the municipality's major cash items by examining an annual budget, payment and collection records and past cash flow patterns. See end of chapter 11 for a list of common receipts and disbursements of a municipality.)

### Estimating Collection Receipts

Local taxes and state and federal grants constitute the primary sources of municipal funds. By reviewing a municipality's treasury and accounting records, a treasurer can determine the pattern of receipts of that municipality. To assist in determining this pattern, the treasurer should develop a table that displays: (1) the type of each receipt, (2) the total amount of the receipt and (3) the month when each portion of the receipt was received. If the treasurer traces the cash flow back 2 or 3 years, a recognizable pattern should become apparent.

The treasurer should assess the historical patterns of these cash flows in light of current estimates and events. Although making adjustments for changing time

## **Effective Cash Management**

environments is uncertain business, attempting to make such adjustments should improve a collections forecast.

### **Forecasting Disbursements**

Municipal payrolls account for approximately seventy percent of the expenditures of most cities and towns. These expenditures tend to be relatively constant; accordingly, they can be reliably predicted. A treasurer should use prior payroll records, together with the next fiscal year's budget, to calculate the amount of the annual payroll.

The gross payroll, however, is not the amount disbursed. Rather, the amount disbursed is the gross payroll amount less deductions for federal and state income taxes and for fringe benefits, such as workers compensation and retirement. The payroll disbursement forecast should also include adjustments for seasonal or temporary workers and for seasonal payments, such as vacation advances in the summer months. If a municipality offers a lump sum payment option for teachers, the payments are disbursed at the end of the school year.

Disbursement of monies previously withheld for income taxes and for employee benefits constitutes a significant payment by a municipality. To forecast the amount of this disbursement for some discrete period, such as from July 1 through January 1, the treasurer must add all of the deductions from a weekly or biweekly payroll and multiply the sum by the number of pay periods falling within the designated time period.

As part of forecasting disbursements for personnel costs, the treasurer should attempt to estimate the actual cash disbursement if that disbursement deviates from the budgeted or authorized amount. Budgeted amounts can change only with supplemental appropriations, while authorized amounts can change with the increase or decrease of actual employees.

After completing the payroll disbursement forecast, the treasurer should develop forecasts for other kinds of payments. The treasurer might begin by analyzing each departmental budget for non-payroll items and then focusing on the more expensive items first. For each item, the treasurer should converse with the departmental officials familiar with expenditures to discover the pattern of past cash disbursements with respect to that item and the anticipated pattern and amount of expenditure for the item for the upcoming year. The treasurer, based upon a greater familiarity with the timing and volume of cash outflows, should ensure that these patterns and expenditure projections are reasonable.

### **Analyzing Cash Flow and Preparing a Cash Budget**

At a minimum, a treasurer should prepare cash flow data on a monthly basis for the current year. In larger communities, the treasurer should compile cash flow



information more frequently, on a daily, weekly, or biweekly basis, depending on the size of the community.

The treasurer should prepare cash flow summaries using two basic categories of inflows and outflows of cash, recurring and extraordinary. Recurring payments and receipts, such as payroll expenses and property taxes payments, can be anticipated regularly, month after month; extraordinary payments and receipts, on the other hand, result from nonrecurring programs or items, such as federal grants or capital expenditures.

The treasurer should use the history of major collections and disbursements for the previous three to five years to identify recurring expense and disbursement patterns. The treasurer should then extrapolate these past trends into the future, being careful, at the same time, to make adjustments for anticipated changes in timing and payment patterns and to recognize when particular historical data is not representative.

Analyzing the municipality's current operating budget, looking particularly for the percentage increase in payroll and in other expenditures, for changes in seasonal spending patterns and for adjustments caused by the addition or deletion of programs, will provide crucial information for preparing a cash flow analysis. Also, examining the capital budget and communicating with department heads will assist in making projections concerning special cash flow items. Of course, analyzing historical information is of little assistance in projecting special revenues and expenditures in a cash flow analysis.

Because cash availability is the fundamental concern of cash management, some treasurers are very conservative in estimating receipts of funds and liberal in estimating disbursements when they prepare a cash budget. For instance, they might budget a receipt expected to be taken in at the end of a month as being received the following month. Certainly, it is better to err on the conservative side. Notwithstanding, accuracy is critical in estimating and managing a municipality's cash.

### **Suggestions for Improving Cash Flow**

The treasurer can maximize the amount of a municipality's available cash by accelerating cash receipts. A treasurer can increase the available cash amount by:

- Making daily deposits.
- Using a lock box.
- Receiving wire transfers of state aid.
- Applying promptly for reimbursement of state/federal grants.

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- Utilizing, direct deposits, Automated Clearing House payments, and other electronic means of transferring funds, whenever possible, making sure that the appropriate safeguards are in effect.
- Making sure that all departmental receipts are turned over promptly (more than \$ 1,000 should be turned over to the treasurer daily and all departments must turn in all money weekly)

The treasurer should induce municipal departments with large cash receipts to make deposits directly into an account specified by the treasurer, providing the treasurer with a written notice of each deposit, together with the deposit receipt provided by the bank. This practice will result not only in an earlier deposit of the funds, but also in a more accurate deposit record since the bank will check the accuracy of the deposit slip. Examples: Collectors' receipts, Cafeteria receipts, student activity accounts

The treasurer should ensure that checks for large amounts are deposited immediately. If, for example, a tax collector receives tax escrow payments from a mortgagee bank at a time when the collector is too busy to process them, the treasurer should instruct the collector to prepare a deposit slip and deposit the bank check immediately, retaining a duplicate copy of the deposit slip with the payment breakdown. In this way, the money will be available for investment right away, and the collector can process the payment information whenever convenient.

The treasurer should urge the collector to make use of tax takings and other tax payment enforcement remedies allowed by law to expedite the collection of unpaid taxes. The treasurer should actively proceed with tax foreclosures and with land of low value sales in accordance with the best interests of the municipality.

The treasurer can also improve cash flow by working with department heads to schedule certain cash disbursements. For example, if a municipality has appropriated money to the public works department for the purchase of new trucks, the treasurer should encourage the department head to arrange for delivery of the trucks no earlier than late April, close to the due date of the 2<sup>nd</sup> semiannual tax payments or the 4<sup>th</sup> quarterly tax payments, when funds will be on hand to pay for those trucks. Such planning minimizes the need for revenue anticipation borrowing.

When possible, the treasurer should first pay bills that offer discounts, postponing the payments of other bills until the due date. Also, when market conditions permit, the treasurer should schedule the issuance of debt to make the payment due dates coincide with times when the community's cash revenues are at their maximums. Scheduling debt payments as late in the Fiscal Year as possible allows the treasurer to invest the appropriated funds for a longer period, earning more interest for the general fund. The treasurer should require all capital project

managers to provide regular reports of project payment schedules, permitting the treasurer to obtain maximum earnings on project funds.

### Wire Transfers for Bills Payable

The treasurer should wire transfer Fed Funds to cover large payments (over \$100,000) to meet obligations on the date due. Examples: Debt service, health insurance premiums, State and federal withholding tax obligations, large payments for power contracts for municipal light departments, large contractor payments for building projects, obligations to Retirement Board Pension Fund. The treasurer should work with the Accountant or Auditor to have such bills listed in the warrant as “No Check” items so that a check is not produced, but the item is charged to the proper account and the treasurer is authorized to hold a payment until the due date.

The Massachusetts Municipal Depository Trust Funds and some banks do not charge for wire transfers out of municipal accounts.

### Effectively Investing Available Cash

Ch. 44 §55B obligates the treasurer to invest all monies not required for current operations so as to receive the highest rate of return reasonably available taking into account safety, liquidity and yield. To maximize interest income, the treasurer must determine how much money is available to invest by answering the following questions:

- How much cash is on hand?
- How much money is needed to meet weekly or monthly warrants?
- How much money will be deposited weekly or monthly?

The treasurer should use the answers to these questions as a basis for planning investments. By maintaining a chart of deposit accounts, such as the bank ledger discussed in Chapter 3, adding the daily deposits to these accounts, and subtracting amounts transferred or paid on warrants, the treasurer can determine exactly how much cash is available to invest. Furthermore, the cash flow budget will permit the treasurer to determine the length of time for which particular funds can remain in investments.

### The Yield Curve

The cost of money varies according to the length of time for which it is borrowed or loaned. Generally, longer time periods are deemed to have a greater risk associated with them and thus command higher interest rates. This phenomenon, of course, favors a municipality when making long-term investments and disfavors the community when making long-term borrowings. Accordingly, treasurers should use cash flow budgets to design investments for

## Effective Cash Management

the longest reasonable periods in order to obtain the highest yields on these investments.

Treasurers should attempt to be constantly aware of the various interest rates offered by area banks. They should regularly communicate with these banks and ask to be on their mailing lists for publications about bank services and about interest rates on different types of investments over varying time periods. Treasurers should also visit the websites of area banks to review information about interest rates and bank products. Treasurers should seek competition from banks for Certificates of Deposit and other short term investments. Bank rates should be compared to the Massachusetts Municipal Depository Trust (MMDT) rates. (See Chapter 12, Procuring Banking Services.)

## Types of Investments

Many communities maintain written investment policies that serve as a guideline in making investments of short-term funds. These policies delineate investment procedures and considerations and define levels of acceptable risk. Frequently, the policies identify the financial institutions that have satisfied the community's criteria for secure deposits. In addition, the policies generally include specific information about delegation of authority, internal controls, ethics and conflict of interest. A committee for the Mass Collectors and Treasurers Association (MCTA) has developed a Model Investment Policy for the use of its members. When shared with municipal officials and auditors, it can be a very useful tool to insure confidence in the treasurer's ability to invest. See addendum for the model.

Ultimately, the standard to which a treasurer is held in making investments is the "prudent person" standard. A treasurer should always remember to weigh the risk of financial loss when making municipal investments. When investing a municipality's money, the treasurer should carefully avoid high-risk or speculative investments, even if legally permitted.

Ch. 44 §§54 & 55 identify the various institutions into which municipal funds may be deposited. See law in Addendum of this manual or in [www.mass.gov](http://www.mass.gov) website. ("Search for a law" allows one to put in a chapter and section of a law). A treasurer who deposits monies into these institutions will not be personally liable for any loss of money due to the failure of the institutions. (44:55A) Notwithstanding, a prudent treasurer must make certain that deposits and investments are sufficiently insured, adequately collateralized and invested in institutions that have been researched for stability and safety.

The FDIC insures deposits in FDIC-insured institutions. All types of deposits received by insured institutions in their usual course of business are insured up to \$250,000 ~~\$100,000~~ per deposit, including savings deposits, checking deposits, deposits in NOW accounts and time deposits, including CDs. In the case of a bank failure, the FDIC insurance protects deposits that are payable in the U.S.

The treasurer should communicate with the FDIC to determine whether separately named accounts are considered as separate deposits for the purposes of applying the \$250,000 ~~\$100,000~~ limit.

In the past, a number of governmental entities incurred significant losses due to inadequately secured investments. In order to remedy this situation, the Governmental Accounting Standards Board (GASB) issued Statement 3, which requires governmental entities to disclose their policies regarding securitization and safekeeping for deposits and investments, including repurchase agreements, better enabling investors to assess the degree of risk more accurately. These disclosures must inform potential investors about situations in which a greater credit risk exists during the investment period than on the balance sheet date.

Cities and towns should disclose the amount of their total bank balances that are:

- Insured or collateralized with securities held by the municipality or by an agent in the municipality's name.
- Collateralized with securities held by their financial institutions or by an agent in the municipality's name.
- Uncollateralized.

The carrying amount and the market value of investments should also be disclosed for each type of investment as of the balance sheet date. The disclosure should state the total amount of each type of investment and should categorize investments that are:

- Insured or registered or held by the municipality or its agent in the municipality's name.
- Uninsured or unregistered, with the securities held by the counterparty in the municipality's name.
- Uninsured or unregistered, with the securities held by the counterparty but not in the municipality's name.

### **Certificates of Deposit**

A Certificate of Deposit, generally known as a CD, is a written acknowledgement by a commercial bank, savings and loan institution or mutual savings bank containing a promise to pay interest at a specified rate for a fixed period of time for funds deposited in the institution. CDs provide a useful instrument for short-term investments, usually more than 7 days. They are available in almost any denomination, although most have a minimum amount. The bank pays interest on the certificate's face value, and the interest accrues on a 360-day or 365-day basis. Rates vary depending on the length of time for which the certificates are issued, the amount of money deposited and the prevailing market rate. Rates also

## **Effective Cash Management**

vary among banks, making it important for treasurers to obtain quotes from a number of banks before making a purchase.

Because monies are deposited in a CD for a fixed term, the instrument is not considered a liquid investment. A bank can legally refuse to return the money before the maturity date. If a bank allows redemption before the maturity date, the municipality must pay a substantial, early withdrawal penalty. Accordingly, a treasurer should only purchase a CD when it is very probable that the municipality will not have to spend the money during the CD's fixed term, up to 3 years.

On the other hand, if a municipality can afford to tie up money for fixed period, a CD provides an effective vehicle for obtaining fixed interest rates for that period. Of course, timing the purchase of a CD is important since interest rates vary dramatically. The treasurer should strive to make the purchase when interest rates are high. The municipality will then continue to earn the high rate until the CD's maturity. On the other hand, if the treasurer purchases a CD when interest rates are low, the instrument will earn interest at the low rate.

## **U.S. Treasury Bills**

Treasury bills are bearer obligations of the U.S. Government that are issued on a discount basis; that is, a purchaser buys the instruments at less than the face value and receives the face value upon redemption. The difference between the purchase price and the redemption price is the interest income. Treasury bills are backed by the full faith and credit of the U.S. Government and are considered the safest investment. Because of their relative safety and marketability, T-Bills, as they are called, generally provide lower yields than do comparable short-term investments.

## **Repurchase Agreement**

A repurchase agreement, also known as a "repo" or a "buyback," is a contract that requires a seller of securities, most often treasury securities, to buy the investment back in the future at a designated time and price. An advantage of this investment vehicle is the flexibility of its maturity. A repo may be sold for a fixed period of time, on demand, or renewable on a day-to-day basis.

The authority of a municipal treasurer to invest in repurchase agreements is set out in Ch. 44 §55. This statute permits the treasurer to invest in "obligations issued or unconditionally guaranteed by the United States government or any agency thereof and having a maturity from date of purchase of one year or less, or in United States government securities or securities of United States government agencies purchased under an agreement with a trust company, national bank or banking company to repurchase at not less than the original purchase price of said securities on a fixed date, not to exceed ninety days."

However, while repos offer flexibility in maturity dates, they are not without risk. In the past, some banks have used the same security for several, simultaneous repurchase agreements. Accordingly, when investing in a repo, the treasurer should make certain to take possession of the underlying security or to receive written notification of the transaction from a third-party trustee who holds the security on behalf of the municipality. In this way, the municipality will be protected in the case of a bank default.

### **Money Market Deposit Accounts (MMDAs)**

A money market account is a savings account that shares some of the characteristics of a money market fund, a mutual fund that invests solely in short-term securities. These accounts, like other saving accounts, are insured by the Federal government up to \$100,000. Banks generally place restrictions on money market accounts. The restrictions usually include:

- A minimum daily balance requirement, with an interest rate reduction if the balance falls below this minimum.
- A limit on the number of withdrawals, such as 6 per month with a maximum of 3 checks. Under such a limit, a depositor could, for example, write 3 checks and make 3 withdrawal transfers in a month. Alternatively, the depositor might write 2 checks and make 4 withdrawal transfers and two checks, etc.

MMDA accounts provide an ideal investment vehicle to obtain moderate yields while keeping funds liquid. Every municipality should have at least one money market account. It is up to the treasurer to determine how much money should be kept in these accounts.

### **Massachusetts Municipal Depository Trust**

Ch. 29 §38A authorizes the state treasurer to establish, with the advice of an investment advisory council, one or more combined investment funds and to sell participation units to local governments. Under this authority, the state treasurer has established the Massachusetts Municipal Depository Trust (MMDT), a professionally managed investment pool. The trust manager invests in money market securities, such as CDs, T-Bills, repos, banker's acceptances, and commercial paper. It is open to agencies, authorities, commissions, boards, cities, towns, and other public entities within the Commonwealth. Participants purchase shares in the pool by depositing funds. Under the rules and regulations adopted by the state treasurer, no minimums exist regarding either the amounts deposited or the length of time monies may remain on deposit. Rates are subject to fluctuation and are not guaranteed, but have been competitive during the twenty-five years of MMDT's history. Monies deposited in the MMDT are liquid, i.e., they may be accessed at any time by fed funds wire, at no cost to the participant. Pre-authorized wires may be used to pay bills for the participant.

## **Effective Cash Management**

In 2006, the MMDT introduced a Short Term Bond Fund (STBF). Its primary purpose is to offer participation in a diversified portfolio of high quality investment-grade fixed-income assets that seeks to obtain the highest possible level of current income consistent with preservation of capital and liquidity. While the STBF's assets will be invested in high quality instruments, the STBF is not without risk. The STBF's Investment Adviser invests assets only with issuers whose creditworthiness and compliance with the applicable statutes and policies have been reviewed and found satisfactory by the STBF's Investment Adviser and approved by the Treasurer. To assist the STBF's Investment Adviser in managing the STBF effectively, participants need to provide one day advance notice for investments or redemptions from \$ 1million to \$ 5 million, or two day advance notice if the transactions are in excess of \$ 5 million.

Further information may be obtained by calling MMDT Client Services at 1-800-392-6095.

## **U.S. Government Agency Obligations**

Agency obligations, also referred to as "agency securities" are debt instruments issued by government agencies to fund loans to particular groups of borrowers, such as students, farmers and homebuyers. Agency obligations include the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac), the Federal Home Loan Bank System (FHLB), the Federal Farm Credit Bank (FFCB), and the Student Loan Marketing Association (Sallie Mae. Agency obligations generally yield high credit ratings because of their association with the federal government; however, they are not government obligations backed by the full faith and credit of the U.S. Government. Accordingly, agency obligations are slightly riskier than Treasuries, but they also have the potential for higher earnings.

## **Secondary Markets**

Primary markets allow investors to bid directly for the purchase of securities with issuers and, as a result, tend to provide more favorable prices. Secondary markets permit investors to purchase securities at other times than their issuance dates or to sell securities prior to their maturity dates.

General economic conditions affect interest rates, which in turn determine the market behavior of securities in both primary and secondary markets. Confidence in a particular security can also affect its behavior. Confidence is determined by an investor's perception of the financial health of an institution or the collateral behind a security. It tends to be most important in determining the strength and activity of a security in the secondary market. For instance, Treasury Bills are always very active in both primary and secondary markets because they are backed by the U.S. Government. Understanding how markets behave under a variety of conditions and gaining a feel for how various securities will be affected is



a skill acquired through day-to-day experience, as well as by a study of the characteristics of securities.

### **Mutual Fund Money Market Accounts**

Ch. 44 §55 permits municipalities to invest in money market funds managed by mutual fund companies. The underlying securities of the funds must be within the guidelines approved by the Commonwealth, similar to securities that would appear on the “legal list” of investments. The statute limits investment to those money market funds that have received the highest possible rating from at least one nationally recognized statistical rating organization. Money market funds fluctuate with the stock market and as managed by the fund managers.

### **Investment-Related Matters**

Municipalities borrow for a variety of reasons, such as to fund temporary cash needs and to finance the construction of public works. The investment of borrowed funds is heavily regulated by federal arbitrage laws. (See Chapter 9.) Accordingly, the treasurer should work closely with bond counsel to determine the status of existing and proposed federal laws and regulations relating to arbitrage before the municipality effects a borrowing.

A useful resource for treasurers is a “Time Teller Calendar” that computes at a glance interest, elapsed time and maturity dates on notes. Some banks will provide this resource to treasurers. For each day of the year, the calendar exhibits the number of days from that day to any other day in the next nine months.

Every treasurer should keep records of all investments. While the treasurer can design the forms to use for this process, these forms must make it possible to record all the necessary information to provide an accurate picture of each transaction. Type of Security, where purchased, date purchased, length of investment, interest rate and interest amount to be earned should all be included. A treasurer must observe the limitations on deposits in any one bank, set out in Ch. 44 §55. This statute specifies that a municipality may not at any one time have on deposit in a bank or trust company an amount exceeding 60% of the capital and surplus of that institution and that the total of all the municipality’s accounts may not exceed 60% of the bank’s net equity. If a treasurer wishes to exceed this limit, the bank must pledge additional securities to cover the extra amount deposited. Treasurers should retain these securities in their custody. Banks will make available copies of their most recent “Statement of Condition” from which a treasurer can determine the banks’ capital and surplus amounts.

Ch. 44 §55A, absolves treasurers of any personal liability if they, in good faith and in the exercise of due care, deposit public money in the MMDT or in a Massachusetts-organized savings bank, trust company or FDIC banking company

## **Effective Cash Management**

and a loss results from the closing up of the depository or from the liquidation of its affairs. This statute does not, however, absolve from liability a treasurer who invests public funds in a non-FDIC bank outside of Massachusetts.

## Typical Receipts and Disbursements

### I. Receipts

#### A. Property Taxes

##### 1. Characteristics

- a) Major portion of revenues
- b) Collected quarterly or semi-annually

#### B. Projection techniques

- 1. Construct 3-year history of tax collections from historical collection information.
- 2. Determine gross tax levy; reduce by abatement or overlay and amount of uncollectible taxes to obtain net tax levy.
- 3. Multiply net tax levy by 3-year percentage calculated in step I.B.1.
- 4. Make adjustments for anticipated changes in collection patterns.

#### C. Potential adjustments

- 1. Changes in anticipated amounts of abatements granted or uncollectible taxes
- 2. Economic upturns or downturns
- 3. Changes in tax bill issuance dates

#### D. Motor Vehicle Excise

- 1. Usually the largest “local receipt”
- 2. Collection dependent on the RMV’s providing the necessary billing information to the municipality

#### E. State Aid

##### 1. Characteristics

- a) Significant portion of revenues
- b) Includes aid for education and other programs
- c) Collected quarterly, semi-annually or as a reimbursement

##### 2. Projection techniques

- a) Review annual budget to identify all reimbursable or chargeable programs and their estimated amounts.

## Effective Cash Management

- b) Discuss with department personnel the timing of program expenditures and claims processing.
- c) Determine nature of payments, whether cash advances, letters-of-credit, or claim reimbursements.
- d) Discuss with federal and state payment agencies the timing of anticipated payments.

### 3. Potential adjustments

- a) Changes in federal or state programs
- b) Delays or accelerations of program expenditures
- c) Changes in amounts of program expenditures
- d) Changes in claim approval process or payment process by federal or state agencies

## F. Departmental

### 1. Characteristics

- a) Includes user payments for hospital, library, and water and sewer services
- b) May be collected by departments, in which case the timing and amount of revenues collected depends on agency efficiency in billing and collection and remittance agreements with municipal collector

### 2. Projection techniques

Construct collection history, using historical collection patterns, the agency's annual budget, and discussions with agency personnel, and apply amount of anticipated annual revenues

### 3. Potential adjustments

- a) Changes in fees or rates
- b) Increase or decrease in usage
- c) Changes in agency collection procedures

## G. Other Revenues

### 1. Characteristics

- a) Includes cash collections from parking meters, golf courses, and other services as well as licenses, fines, and subscriptions
- b) Small portion of revenues

### 2. Projection techniques

If amounts are material (greater than \$5,000 for any forecast horizon), apply the estimated annual amount evenly throughout collection period. For major amounts, apply in accordance with collection history.

3. Potential adjustments

- a) Changes in rates, fees, or fines (Assure that upcoming amounts are reasonable.)
- b) Changes in usage or delinquency

**II. Disbursements**

A. Salaries and Wages

1. Characteristics

- a) Usually at least 70% of general fund budget
- b) Very predictable

2. Projection techniques

- a) From annual budget and payroll records, determine annual payroll disbursements.
- b) Eliminate payroll deductions to find net cash outflow.
- c) Apportion by established pay dates.
- d) Adjust as necessary for collective bargaining changes.

3. Potential adjustments

- a) Changes in number of employees
- b) Increase or decrease in salaries and wages
- c) Seasonal or overtime payments
- d) Changes in group insurance, income taxes, and other deductions

B. Payroll Taxes

1. Characteristics

- a) Includes federal income taxes and state taxes
- b) About 30% of payroll expenditures

## Effective Cash Management

### 2. Projection techniques

- a) From the salaries and wages forecast, determine annual payroll tax disbursements.
- b) Estimate amount required on due dates by dividing annual taxes into quarterly or semi-annual payments.

### 3. Potential adjustments

- a) See Salaries and Wages
- b) Changes in tax rates

## C. Debt Service

### 1. Characteristics

- a) Payments determined by fixed schedule

### 2. Projection techniques

- a) From debt maturity and coupon redemption schedules, determine amount due on redemption dates.

### 3. Potential adjustments

- a) Additions of new debt issues or adjustments for refinancings in upcoming year

## D. Capital Expenditures

### 1. Characteristics

- a) Irregular, plans often change

### 2. Projection techniques

- a) Develop separate cash flow estimates for each project.
- b) From construction contracts, determine total construction costs.
- c) From discussions with construction supervisors, determine probability of cost increases, pace of construction, and likely payment patterns.
- d) Estimate the timing and amount of payments.
- e) Deduct retainage from in-progress payments and add back to final payment.

### 3. Potential adjustments

- a) Changes in construction schedules (Develop advanced warning system with construction supervisor.)

**E. Employee Benefit Plans**

**1. Characteristics**

- a) Includes funded pension plans, health insurance, group life insurance, and disability income plans

**2. Projection techniques**

- a) As specified in contracts, estimate amounts due on each payment date

**3. Potential adjustments**

- a) Changes in insurance rates
- b) Changes in number of employees
- c) Changes in number and nature of plans in employee benefit package
- d) Changes in number of employees qualifying for benefits, such as new retirees

**F. Materials and Supplies**

**1. Characteristics**

- a) Usually minor portion of expenditures
- b) Includes office supplies, stationery, postage, printed forms, vehicle supplies, and textbooks and school supplies (usually purchased during the summer)

**2. Projection techniques**

- a) From annual budget and purchase contracts, isolate major items.
- b) From discussions with department personnel, predict timing of outflow for major items.
- c) Approximate smaller cash payments based on annual budget and past experience. (If amounts are not significant, do not forecast.)

**3. Potential adjustments**

- a) Usually only minor adjustments, but can be significant during budget cutbacks

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- b) Changes in usage rates due to purchase cycles (e.g., textbooks or vehicles every two years)

### G. Utilities

#### 1. Characteristics

- a) Usually minor portion of expenditures
- b) Monthly, bimonthly, or quarterly payments

#### 2. Projection techniques

- a) Using contracts, historical results, and current rates, estimate timing and amount of utility payments

### H. Potential adjustments

- 1. Rate changes or price increases
- 2. Usage changes, particularly during conservation programs

### I. Other Current Costs

#### 1. Characteristics

- a) Includes travel expenditures, dues and subscriptions, per diem fees, other insurance, court judgments, and tax refunds

#### 2. Projection techniques

- a) From annual budget and discussions with department personnel, estimate timing of nonrecurring costs.

#### 3. Potential adjustments

- a) Changes in timing of payment or cancellation of plans



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## Chapter 12

# Procuring Banking Services

### Introduction

Banking services help a treasurer to achieve optimum cash management as described in Chapter 11. Achieving success as a municipal financial officer requires making educated and lawful decisions about procuring banking services. The banking industry has rapidly evolved in recent years, creating greatly improved products and services. Technological advances, expansion into new product lines, and industry consolidation have considerably altered the ways in which banks assist municipalities to carry out their responsibilities. and Inspector General's Guidance in Procurement

In December, 2004, Inspector General (IG) Gregory W. Sullivan issued a comprehensive publication, titled *Banking Services Procurement Guide for Local Government Treasurers*. It is available on the IG's website, [www.mass.gov/ig](http://www.mass.gov/ig) and in the Addendum of this manual. It should be used as the definitive guide for treasurers when seeking banking services. The Table of Contents is as follows: Section One: Introduction to the Banking Services Procurement Guide

Section Two: Banking Services and M.G.L. Chapter 30 B

Section Three: Issues and Recommendations for The Procurement of Banking Services

Section Four: Listing of Selected Resources for Banking Services Procurement

Appendix A: State Treasurer Recommendations for IFFB/RFP Preparation

Appendix B: Sample Banking Services RFP

Appendix C: Sample Banking Services Proposal Evaluation Form

Appendix D: Sample Investment Advisory Services RFP

The procurement of banking services is governed by one of two laws, Chapter 30 B, the Uniform Procurement Act, or Chapter 44 §53F, the Compensating Balance law. The Uniform Procurement Act establishes uniform procedures for local jurisdictions to use when contracting for supplies, equipment, services, and real property. It provides three different procurement methods, depending upon the dollar value of the contract. The Compensating Balance Law authorizes local jurisdictions to enter into a compensating balance agreement for a period up to three years. These agreements must be approved annually by town meeting or the city council. (See further information at Division of Local Services website, [www.mass.gov/dls](http://www.mass.gov/dls) Table 1, below, presents a list of banking services generally available to assist a municipality to manage its funds. A discussion of the listed services follows the table.

**Table 1**

<b>Service Category</b>	<b>Services</b>	<b>Cash Management</b>
Collection Services	<ul style="list-style-type: none"> <li>• Lock-Box System</li> <li>• Armored Car Services</li> <li>• Night Depository</li> <li>• Wire Transfers</li> <li>• ACH/Direct Deposit/Direct Debit</li> <li>• Credit/Debit Cards</li> <li>• Electronic payments</li> </ul>	Accelerate Cash Receipts
Account Services	<ul style="list-style-type: none"> <li>• Concentration/Zero Balance Accounts</li> <li>• Sweeps</li> <li>• Controlled Disbursements</li> </ul>	Maximization of Returns on Account Balances
	<ul style="list-style-type: none"> <li>• Daily Account Notification via Fax</li> <li>• PC/Online Banking</li> <li>• Checks via CD-ROM</li> </ul>	Maximization of Information on Accounts
	<ul style="list-style-type: none"> <li>• Account Reconciliation</li> <li>• Check Sorting</li> <li>• Direct Payroll Deposit</li> <li>• Wire Transfers</li> <li>• Escrow Accounts</li> <li>• Tracking Accounts</li> </ul>	Maximization of Efficiency Between Accounts

## Procuring Banking Services

Investment Services	<ul style="list-style-type: none"><li>• Bank Investments</li><li>• *Money Market Accounts</li><li>• *Time Deposits (Certificate of Deposits)</li><li>• *Overnight Sweep Investments</li><li>• *Repurchase Agreements</li><li>• *Mutual Funds</li><li>• *U.S. Government &amp; U.S. Government Agency Securities</li><li>• Investment Advisory Services</li><li>• *Retirement Plan Services</li><li>• *Trust Fund Services</li></ul>
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Credit Services	<ul style="list-style-type: none"><li>• Short/Long-Term Notes</li><li>• Bond Redemption Services</li><li>• Bond Transfer and Registration Services</li><li>• Lending Activities Related to Community and Economic Development Projects</li><li>• Lease Services</li><li>• Underwriting</li><li>• Financial Advisory</li><li>• Paying Agent</li></ul>	Meet short and long-term borrowing needs
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## Collection Services

Although collection is not the responsibility of the treasurer, a treasurer's coordinating banking services and other activities with the collector will certainly improve the municipality's overall cash management.

Banks design their collection services to assist communities to accelerate their collections, thereby optimizing investment earnings. The acceleration results from decreasing collection float, i.e., the interval between the time a check is mailed to the collector and the time the municipality can actually spend or invest the money. This interval includes the municipality's internal processing time and the bank's check-clearing time.

Instituting one or a combination of the following banking services can reduce collection float:

1. **Lock-Box System.** A lock-box system speeds up the collection process by eliminating direct handling by municipal collectors of certain routine remittances. Specifically, a lock-box system can be used for any type of remittance made in response to a formal collection effort of a municipality that is accompanied by some sort of “advice,” such as a bill.

A lock-box system functions as follows:

- A bank rents a post office box in a local government’s name.
- Taxpayers mail their remittances to this box rather than to the municipality’s regular mailing address. The bank collects the remittances periodically during the day, pursuant to an agreement.
- A bank employee opens the remittances and sorts the payments and accompanying data.
- The bank processes for deposit on the same day all checks that correspond with the particular bill, invoice, or other data.
- The bank turns over to the local government all non-corresponding checks for local processing.
- The bank forwards daily copies of all normal remittances and accompanying data (invoice, utility bill, etc.) to the local government for its internal processing.

The major advantages of a lock-box system include the following:

- Frequent collection of mail from the lock-box reduces the collection float interval.
- Crediting payments to the municipality’s bank account prior to their being processed and posted to the general ledger further reduces the collection float interval.
- The elimination of most mail-opening and deposit preparation tasks greatly reduces clerical workloads in the municipality.
- Shifting mail-opening and deposit preparation tasks to a bank greatly reduces cyclical workloads that otherwise cluster around key dates, eliminating the need for overtime pay.
- Reduction of the collection float interval accelerates the availability of usable cash balances, generally by several days.

Instituting a lock-box system requires a sizeable investment for a bank; accordingly, banks pass on these costs to their municipal customers. Notwithstanding, the financial rewards of utilizing a lock-box system can far outweigh these costs.

2. **Armored Cars and Night Depositories.** Utilizing armored cars and night depository services can also accelerate the deposit of a municipality’s receipts, thereby hastening a municipality’s ability to put its funds to use. Armored car costs make utilization of this service prudent with high volume receipts. In lower volume circumstances, using a night depository gives the municipality an alternative way to deposit receipts as quickly as possible. In addition to the security advantages afforded by utilizing a night depository, this service is especially beneficial if a municipality’s accounts are structured to earn interest overnight, i.e., beginning immediately upon deposit.

## Procuring Banking Services

3. **Wire Transfers.** Wire transfers entail the electronic transmission of payments from one bank to another electronically. The Federal Reserve Communications System, or “Fed Wire,” constitutes the most commonly used wire system. The fee for wire transfers, however, can make utilization of this service judicious only for large transactions. Wires from the Massachusetts Municipal Depository Trust and some banks do not have fees attached.
4. **ACH/Direct Deposit/Direct Debit.** The Automatic Clearing House (ACH) network is a nationwide system that processes electronic payments. The direct debit or direct payment system works most effectively with utility payments or other regularly scheduled billing processes. The system works by electronically transferring a payment from the payer’s bank account into the municipality’s account. Generally, the collection or payment is setup through a pre-authorization process.
5. **Electronic Payments.** Payment of bills through electronic means has become more and more popular for individual bill payers. Offering this capability through a service company and contracting bank is customer friendly and also speeds collections.
6. **Credit and Debit Cards.** Credit and debit cards continue to gain a wider level of acceptance as a means of payment of municipal charges. However, since municipalities cannot give discounts on municipal taxes, except in the manner set out in Ch. 59 §58, a person paying property taxes with a credit card must bear the municipality’s charge.

### Account Services

The structure of a municipality's banking accounts constitutes an important component of the effectiveness of its cash management system. Therefore, the financial officers should carefully consider what combination of accounts best serves the city or town's needs. The primary objectives in making this determination should be maximizing:

1. Returns on account balances.
2. Efficiency between accounts.
3. Account information.

### Types of Accounts Available and Account Purposes

- A standard "checking account" allows writing checks against the balance in the account. Such accounts are best used for everyday expenses, not for long-term savings. They provide liquidity, keeping monies available for disbursement.
- A vendor account is a checking account specifically designed for paying vendors.
- A "trust account," also called a "concentration account," contains assets from multiple, separate trusts, sometimes called sub-accounts, set aside for specific purposes.
- A "zero-balance" or "sweep account" sweeps the balance from a checking account into some form of investment, usually a repurchase agreement or money market mutual fund.
- A "money market account" is a limited liquidity checking account (for example, allowing a limited number of deposits and withdrawals per month) which usually pays a higher return.

Generally, the greater the service provided with an account (i.e., liquidity, check processing, detailed statements/accounting), the greater the cost (higher fees or lower return). Accordingly, municipal officials should carefully consider the services actually necessary in order to avoid paying for unnecessary services. Shopping around for the services, through procurement is also an important part of the equation.

### Maximization of Information on Accounts

Banks offer account information to customers through a variety of different means and formats. Therefore, municipalities must make a number of decisions about what information they wish to receive and how they wish to receive it. Of course, making these decisions should entail some cost/benefit analysis because costs generally rise in correspondence with the amount of information provided and the convenience and complexity of the format used in providing it.

In some cases, receiving a monthly account statement by mail may satisfy a municipality's needs. In other cases, a municipality may require more frequent information, perhaps even a daily account notification via fax. Internet or Web Banking, of course, allows for information on demand, perhaps providing the most convenient service.



## **Procuring Banking Services**

The format in which one receives information sometimes surpasses the importance of the information itself. More than just performing standard check processing, banks can also provide check sorting, as well as reconciliation of statements and checks via an account reconciliation service. Also, they can issue copies of checks on a CD-ROM. Some banks no longer return paper checks, but will provide a copy of a check when needed. Banks can arrange trust concentration accounts, which congregate information from numerous sub-accounts. These modes of structuring accounts and providing information can afford important timesaving conveniences to local finance officers.

## **Maximization of Efficiency between Accounts**

The ability to move money between accounts provides important flexibility. Different methods of making transfers afford different benefits. Writing a check provides a cost efficient method when timing is relatively unimportant. Alternatively, when moving a substantial sum to a high earning account, an electronic transfer might be more beneficial. A treasurer can effectuate a wire transfer either by a telephone request to the depository bank or by initiating an Automated Clearing House (ACH) transfer through an on-line banking system.

For municipal activities that require periodic transfers, either a set amount or at the same frequency, such as administering a payroll, convenience may be the ultimate priority. For such activities, direct deposit or direct debit accounts provide important benefits.

Regardless of the needs of a municipality, banks offer products and services to meet those needs. For a community to obtain appropriate services, however, the treasurer must first identify accurately the municipality's needs. As part of this process, the treasurer must consider the value of office time, as well as the amount of time required to perform the various necessary tasks. Only then will the treasurer be in a position to acquire the optimum services and products for the smallest cost.

## **Investment Services**

Although banks offer a variety of investment services to assist municipalities in making investment choices, treasurers should bear in mind that they, themselves, bear the ultimate investment responsibility. Also, they should insulate choosing investment services from choosing other banking services. Moreover, they should ensure that any contract for banking services should expressly state that the municipality reserves the right to make investments through any bank or brokerage house it chooses.

The responsibility of treasurers to invest municipal monies arises under Ch. 44 §55B, which imposes upon them the duty to invest all monies "not required to be kept liquid for the purposes of distribution." The statute further obligates them to make their investments "in such a manner as to require the payment of interest on the money at the highest possible rate reasonably available, taking account of safety liquidity and yield." Ordinarily, municipal monies must be invested in accordance with Ch. 44 §55; trust monies must be invested in accordance with Ch. 44 §54.

### **Advisory and Management Services**

Banks offer a wide range of investment services, ranging from comprehensively managing a municipality's portfolio to providing custodial services. In managing investments, a bank implements an investment plan, periodically reviews the plan, and alters it, as necessary, to meet the municipality's changing needs. Ordinarily, such extensive service would be limited to very substantial sums of money over extensive periods of time. Custodial services involve performing administrative tasks associated with making investments.

### **Bank Investment Products**

The Federal Deposit Insurance Corporation (FDIC), an agency established to maintain stability and public confidence in the nation's financial system, insures deposits up to \$100,000 in virtually all United States banks and savings associations. Some Massachusetts banks also maintain insurance from the Deposit Insurance Fund (DIF) on deposits over \$100,000. This additional insurance gives depositors with large balances an additional level of security.

The chief investment product offered by banks is the Certificate of Deposit (CD), which gives an investor a fixed rate for a fixed period of time. Also popular are repurchase agreements. These also offer a fixed rate over a fixed period; however, with these investments, the bank transfers a security to the municipality and agrees to repurchase it at the end of the fixed term.

### **Market-Based Investment Products**

Banks also offer a number of market-based investment products, the foremost of which is a Money Market Mutual Fund. This product operates like a checking account, except that the bank invests fund proceeds in short-term investments. As with any mutual fund, the safety of these instruments depends on the investments of the fund manager. Before investing in any mutual fund, the treasurer should carefully examine both the fund's prospectus and its annual report.

United States Government Treasury Bills constitute the safest term investment. Issued and fully backed by the U.S. Government, they have a fixed rate over a fixed term (one year or less) if held to maturity. U.S. Government Agency Securities, known as "Discount Notes," have similar features, except they are issued and backed by an agency of the federal government.

Given the wide variety of investment options available, treasurers, in light of their statutory obligation to make circumspect investments, must stay well-informed about investment service options. Only through maintaining regular contacts with several banks can treasurers reliably match their needs with the most appropriate products and services available.

### **Massachusetts Municipal Depository Trust (est. 1977)**

While the Massachusetts Municipal Depository Trust (MMDT) is not a bank, it must be considered an important tool in choosing the proper mix of services for a treasurer to consider (See Chapter 11). The MMDT is a pooled trust operated through the State treasurer's office and has been managed by Fidelity Investments Tax-Exempt Services Company for many years. The State Treasurer uses the procurement process to choose an investment advisor to manage the fund. MMDT's client services may be reached at 1-800-6095.

## Procuring Banking Services

Investments in the Trust may be made in any amount for any period of time; dividends accrue daily, including weekends and holidays. Withdrawals may be made at any time, with no penalties or added charges, by wire against MMDT balances. Withdrawals and purchases may be made, and account information obtained through MMDTNet, the MMDT's internet-based account management system. Interest rates are competitive. In 2006, the MMDT offered a Short Term Bond Fund (STBF) option. The primary purpose of the STBF is to offer participation in a diversified portfolio of high quality investment-grade fixed-income assets that seeks to obtain the highest possible level of current income consistent with preservation of capital and liquidity.

## Credit Services

Banks render a variety of credit services related to managing municipal debt. To safeguard the best interests of their respective municipalities, treasurers should separately obtain credit service, rather than bundling such services with their more routine, recurring banking services.

## Short-term Notes

To respond to temporary cash shortages, to provide cash for initial project costs issued in anticipation of bond proceeds and to fund a project in anticipation of a state or federal grant, municipalities issue short term debt. State law recognizes four, separate types of short-term debt instruments:

1. **Revenue Anticipation Note (RAN) or Tax Anticipation Note (TAN)** — A short-term loan issued to be paid off by revenues, such as tax collections and state aid. RANs are full faith and credit obligations. (44:4)
2. **State Aid Anticipation Note (SAAN)** — A short-term loan issued in anticipation of a state grant. (44:6A).
3. **Federal Aid Anticipation Note (FAAN)** — A short-term loan issued in anticipation of a federal grant. FAANs are full faith and credit obligations.
4. **Bond Anticipation Note (BAN)** — A short-term note to provide cash for initial project costs issued in anticipation of bond proceeds. BANs may be issued for a period not to exceed ten years, provided principal repayment begins after two years. (44:17)  
Communities with approved projects on the School Building Assistance (SBA) priority list may defer principal payments up to five years. The final maturity date of the project borrowing, beginning from the date the short-term note was issued, may not exceed the term specified by statute. (44:7 & 8) BANs are full faith and credit obligations. If principal is not fully paid by year 10, permanent borrowing must be issued.

## Long-term Borrowing

Municipalities may issue long -term debt only for those purposes enumerated in the sub-sections of Ch. 44 §§7 &8. Such debt is payable within the periods specified in the respective sub-sections. Many banks provide long-term borrowing services including financial advisory services. They can provide assistance with underwriting bond issues, as well as with bond redemption, transfer and registration.

Treasurers should contract long-term borrowing services on an as-needed basis through separate contractual agreements, rather than bundling them with more routine, recurring banking services, since such credit services involve long-term commitments that will certainly be different in nature from regular banking service arrangements.

### Procuring Banking Services

Acquiring banking services is subject to the Uniform Procurement Law, Ch. 30B. Chapter 30 B also applies when a public jurisdiction is disposing of real property or surplus supplies. When obtaining banking services through the direct payment of fees and/or to obtain higher interest rates, a municipality must use Chapter 30B procedures. If a municipality is obtaining banking services subject to compensating balances, it must still follow Chp 30B, as the exemption for compensating balances has been eliminated. Chapter 30 B should be used to procure both fiscal and/or consulting services and financial/investment advising and/or consulting services.

Chapter 30B establishes three sets of procedures for awarding supply and service contracts depending on the value of the contract. Specifically:

- Contracts for goods or services costing less than \$ 10,000 ~~\$5,000~~ must be obtained through the exercise of sound business practices. [30B:4(c)]
- Contracts for goods or services costing \$10,000 or more, but less than \$50,000 require the procurement officer to seek written or oral quotations from no fewer than three persons customarily providing such supply or service. [30B:4(b)]
- Contracts for goods or services costing \$50,000 ~~\$25,000~~ or more require a formal advertised competition using sealed bids or proposals. A community using the sealed bid process must award the contract to the lowest responsible and responsive bidder. (30B:5) A community using the proposal process may evaluate proposals on the basis of criteria other than price pursuant to criteria previously set forth in the request for proposals. (30B:6) A contract granted must be in writing.
- Multi year contracts must be approved by majority vote, (except for regional school districts) as follows:
  - a. For towns or districts, town meeting or district meeting
  - b. For cities, city council or city commissioners with the approval of the mayor
  - c. For counties, the county commission
  - d. For regional school districts, 2/3 of school committee
  - e. For a redevelopment, housing, or other authority, the governing body

In some municipalities, particularly smaller ones, the competitive process will necessitate including banks outside the local community. Although such a process might clash with a desire to conduct business with the local bank, it increases the likelihood of a more beneficial contract for the community.

## Procuring Banking Services

### Steps in the Competitive Bidding Process

Generally, the competitive bidding process will include the following steps:

- Reviewing the present system and determining the additional services desired and available.
- Preparing a request for proposals (RFP) and distributing the document to all banking institutions in the designated area. (See sample RFP in the Inspector General's publication titled *Banking Services Procurement Guide for Local Government Treasurers* found at [www.mass.gov/ig](http://www.mass.gov/ig).) Holding a pre-bid conference for all potential bidders in order to answer questions and to clarify the RFP.
- Receiving submissions of proposals.
- Evaluating proposals.
- Awarding and executing a contract to the winning bidder. Implementing the contract.

### Evaluating Relationship with Depository Bank

Evaluating the relationship between a municipality and its depository bank should not end with the selection of a bank in which to make deposits. Rather, the municipality should evaluate its relationship with the bank on at least a quarterly basis. This evaluation should include verification that the municipality is receiving the services contracted for and at the agreed price. While it is easy to verify the provision or non-provision of services, determining costs is more difficult. The municipality should require its depository bank to provide a periodic statement of the average earnings the bank has achieved on the deposits of the local government, combined with a statement of the costs of services provided to it. This information gives the municipality a basis on which to evaluate the bank's ongoing performance.

### Computing the Cost of Banking Services

Banks price their services primarily in two ways:

- **Direct payment:** The bank prices each service offered, and the municipality reimburses the bank periodically for charges incurred during that period.
- **Compensating balances:** The bank provides particular services in return for the municipality's maintaining a specified, minimum balance in a non-interest bearing account.

### Compensating Balances

Ch. 44 §53F expressly permits a municipal treasurer to enter into a formal "compensating balance" agreement with a banking institution, so long as the agreement complies with the following requirements.

- The agreement may include only those types of services prescribed by the Commissioner of Revenue.
- Each agreement must include the total amount that must be required to be on deposit at all times and, if this amount may vary from time to time, the agreement must specify a minimum total amount that must be on deposit at any time.

## **Procuring Banking Services**

- The agreement must be approved by the town meeting, in towns, and by the mayor and council, in cities.
- The treasurer must submit an annual report of all compensating balances to the Inspector General and local officials.

See Guidelines issued by Division of Local Services on website, [www.mass.gov/dls](http://www.mass.gov/dls) and in Addendum at end of manual.

## Procuring Banking Services

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## **Appendix I**

### **A. Introduction**

Laws are enacted at each level of government (federal, state, and local). The intent of all enacted laws is to impose certain regulations on the manner by which a community is governed. While it is not necessary for a treasurer to be able to quote specific laws verbatim, it is important that each treasurer have a general understanding of the intent and the important points of each statute. Since treasurers are faced with the responsibility of making daily decisions which are consistent with the provisions of the Massachusetts General Laws, the treasurer should be knowledgeable about finding current laws and court decisions.

A municipal treasurer is elected or appointed for a term of a year or more. From the time that a treasurer takes office, it is his/her primary responsibility as custodian of a community's assets to exercise due care in the management of such assets. Management of assets begins at the point of ownership (usually receipt) through the exchange of the asset for goods or services or other assets. Management includes functions of investing and converting, accounting for, and reporting on all of the community's assets. There are municipal laws which have been enacted throughout the levels of government concerning asset management. In order to carry out his or her responsibilities to the people in the community, the treasurer must have knowledge of these laws and be in compliance with them.

### **B. What are Municipal Laws?**

Governments are regulated by a body of laws referred to as municipal laws. Municipal laws include not only the laws of the state, but also the laws of the city or town, which are called ordinances and bylaws. By definition, a bylaw is a local law or a municipal statute of a city or town. A municipal ordinance is a law or rule, enacted or adopted by a municipal corporation for the proper conduct of its affairs or the government of its inhabitants.

On the state level, municipal laws are found in the *Massachusetts General Laws Annotated*, which can be found in most libraries and municipal offices. Pamphlets which are located inside the back cover update the laws through the latest completed legislative session. State law may also be researched by using the website, [www.mass.gov/legis](http://www.mass.gov/legis), and clicking on the various topics available. Current legislation, and an index of the general laws is available and legislators are listed. This is an invaluable resource as it is always being updated. The intent of certain Massachusetts Annotated Laws has been clarified by decisions of the Supreme Judicial Court of Massachusetts and the Appeals Court of Massachusetts. The context of each court case may be found in either of two sets of references. These references, which may be found in all law libraries, are the *Massachusetts Decisions* and the *Massachusetts Edition of the North Eastern Reporter*.

At the local level, municipal ordinances and bylaws are usually printed and are available to the public. The city or town clerk has on file certified copies of bylaws or ordinances that have been passed by the appropriate governing bodies. Town bylaws also need the approval of the attorney general. They must be provided by the Town Clerk sixty days after Town Meeting enactment.

Cities and towns also sponsor legislation on behalf of their particular community which is acted upon by the state legislature. All pieces of legislation which are favorably acted upon can be found in the hardcover blue books entitled the *Acts and Resolves* which are published each year, or in *West's Legislative Services* paperback series which is printed during each legislative session as a number of acts are passed. In both publications, the acts relative to a particular community can be found by looking under the name of the town in the index.

### **C. Locating and Researching Municipal Laws**

The most common municipal law references are the *Annotated General Laws of Massachusetts*. These hardcovered "Green Books," as they are referred to, contain all of the Massachusetts General Laws, amended through the most recent legislative session. The last volumes include a master index which is organized by subject and indicates the applicable legal reference(s) by chapter, section, and clause. See paragraph above for references on line at the Massachusetts government website.

It is often true that a treasurer can look up a statute or statutes in this manner and satisfy a question of how a certain problem should be handled. However, there are instances in which legal citations are vague and do not clear up the problem. When this happens, the treasurer should look at the end of the section where there are listings of court cases which have been tried before the Massachusetts Supreme Court and Appeals Court. A description of each decision is included in the Notes of Decisions.

Numbers and letters following the case name are "citations" to a case. They are shorthand keys to the books known as "reporters" which contain the cases. For example, the citation:

Board of Health of North Adams v. Mayor of North Adams

368 Mass. 554, 334 NE 2d 34 (1975)

tells where the case can be found. "368 Mass. 554" means that the case is located in Volume 368 of the *Massachusetts Reports* on page 554. "334 NE 2d 34" means that the case is also located on page 34 of the *North Eastern Reporter*, second edition, Volume 334. The case year is 1975. In the citation:

Commonwealth v. Hudson 315 Mass. 335, 339-341, 52 NE 2d

566 (1943)

"315 Mass. 335, 339-341" means that this case can be found in Volume 315 of the *Massachusetts Reports* on page 335, and that pages 339 through 341 should be noted with special interest. Most cases are only reported in one or two reporters. Opening notes usually summarize the decision, but they may be misleading. It is important always to read the entire decision.

If the case does not have citation numbers, it may still be located by checking the year of the case and then the index of the yearly reporter. Citations of Supreme Court cases are usually listed under the appropriate statute in the *Annotated General Laws of Massachusetts*. There is also an index in the *U.S. Supreme Court Digest* that lists cases by name.

The *Annotated General Laws of Massachusetts*, the *Massachusetts Reports*, and the *North Eastern Reporter* can be found in law libraries located in law schools, in federal, state, and city court houses, and in state offices.

**INSTRUCTIONS**  
**HOW TO DETERMINE YOUR MINIMUM PERFORMANCE BOND**  
**AMOUNT USING THE BOND AMOUNT SCHEDULE**

To calculate your minimum bond amount, you must first determine the amount of money from all sources which you expect to handle during the year for which you must obtain a bond. The fiscal items which must be considered by the respective officials include the following:

**Treasurer**

1. Retirement funds
2. Trust funds
3. Stabilization funds (if any)
4. Net amount to be raised by taxation
5. Total estimated receipts
6. Bond proceeds

**Clerk**

1. City/town monies (licenses, permits, fees, etc.)
2. State monies (hunting and fishing licenses, etc.)
3. County monies (dog licenses when applicable, etc.)

**Collector**

1. Net amount to be raised by taxation
2. Uncollected real estate and personal property taxes for current fiscal year
3. Uncollected real estate and personal property taxes for prior fiscal years
4. If a city/town collector, the amount of revenue collected from all sources other than taxes

After determining the amount of money you handle, identify that amount in Column I of the BOND AMOUNT SCHEDULE. The corresponding amount in Column II is the minimum amount in which you must obtain a performance bond.

**Assistant Treasurer or Collector**

The amount of the bond of an assistant treasurer or collector shall be set at one quarter (1/4) of the amount of the bond of the appointing treasurer or collector.

**Deputy Tax Collector**

The amount of the bond of a deputy collector shall be set by the appointing collector. However, this amount shall be at least \$6,500.

**NOTE: IT IS IMPORTANT TO REMEMBER THAT THE COMMISSIONER OF REVENUE SETS MINIMUM BOND AMOUNTS. THE CHIEF EXECUTIVE OFFICER OF A MUNICIPALITY CAN AT HIS DISCRETION INCREASE THESE AMOUNTS.**

**PER COMMISSIONER OF REVENUE**

## PERFORMANCE BOND AMOUNT SCHEDULE

This schedule identifies the minimum amount for which each municipal official must obtain a bond. As a municipal official you must determine the amount of money from all sources that you will handle in the fiscal year. Identify that amount in Column I. The corresponding amount in Column II is the amount for which you must obtain a performance bond. For assistance in using this schedule, consult the instruction sheet provided by the Department of Revenue.

<b>Column I</b> <b>Amount of Money Handled</b>	<b>Column II</b> <b>Minimum Bond Required</b>
\$30,000 or less	\$6,500
30,001-100,000	15,000
100,001-500,000	35,000
500,001-1,000,000	65,000
1,000,001-2,000,000	80,000
2,000,001-5,000,000	100,000
5,000,001-10,000,000	120,000
10,000,001-25,000,000	150,000
25,000,001-50,000,000	200,000
50,000,001-100,000,000	250,000
100,000,001-200,000,000	300,000
Amounts over 200,000,000	300,000 plus 100,000 for each add'l 100,000,000 (Round to nearest 100,000,000.)

PER COMMISSIONER OF REVENUE