



# DLS

DIVISION OF LOCAL SERVICES  
MA DEPARTMENT OF REVENUE

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**To:** Mayor Nicole LaChapelle

**From:** Melinda Ordway, Senior Project Manager, Technical Assistance Bureau  
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**Date:** December 18, 2019

**Re:** Enterprise Fund Best Practices

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## INTRODUCTION

The Division of Local Services Technical Assistance Bureau (TAB) conducted a review of the indirect cost allocation for the water, sewer, and wastewater consolidated enterprise fund at the request of Easthampton's mayor. By obtaining an independent review, the mayor sought to ensure that the city's shared costs from the general fund are reasonable and follow best business practices.

For the review, TAB staff met with Mayor Nicole LaChapelle, City Auditor Valerie Bernier, and Treasurer Jennifer Gallant. TAB examined such documents as the tax rate recapitulation sheet, the annual budgets, the city's formal Enterprise Fund Indirect Cost Policy, detailed cost allocation spreadsheets, and other financial documents.

## SUMMARY

Water, sewer, and wastewater are three of seven divisions under the day-to-day management of the department of public works (DPW) director who reports to a three-member board of public works appointed by the mayor.

- The Sewer Division is responsible for maintenance and repair of the City's Sanitary Sewer System which consists of 100 miles of pipe and are also responsible for the Storm Drainage System consisting of different size and types of pipe and thousands of manholes and catch basins.
- The Water Division is responsible for the pumping and distribution of potable water as well as maintenance of 100 miles of water main, 800 fire hydrants and 5,500 water meters.
- The Wastewater Treatment Plant is responsible for the treatment of sanitary sewerage.

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To account for these major services separate from the general fund into a business-like model funded by receipts, Easthampton adopted M.G.L. c. 53F½. This distinction is purely for accounting purposes, and organizationally an enterprise fund is just another department providing a service. Thus, the enterprise fund participates in employee benefits and insurances and receives support from associated administrative services provided by other town departments, and these comes at a cost. Since the enterprise fund has a revenue stream distinct from the general fund, these costs are not accounted for in the general fund budget. The purpose of an indirect cost policy is to direct some portion of enterprise revenues to the general fund to cover these indirect costs. The policy should explicitly identify the indirect costs being allocated, making a distinction between them and the enterprise fund's' direct costs.

Easthampton has a formal policy agreement dated June 24, 2014 that is signed by the then mayor and board of public works chairperson. The policy identifies departments providing support and indirect expenses and provides the methodology used in developing the cost allocation. The qualifying costs include salaries, expenses, employee benefits, insurances, retirement, Medicare, other post-employment benefits (OPEB), and debt. Annually as a part of the budget process, the city auditor calculates the indirect cost allocations, reviews them with the mayor and public works director, and presents them to city council for approval. Because of the city's financial management system, it is a longstanding practice the city auditor applies the budgeted assessments to the enterprise fund at the beginning of the fiscal year and may make adjustments at the end, if warranted.

Generally, we found the indirect cost allocations are transparent, reasonable, and defensible, which are formalized in a written agreement and easily replicated. However, we have three recommendations for the city.

1. Remove In lieu of Taxes – In the written policy, qualifying costs include in lieu of taxes on property and buildings. However in the last sentence of the agreement, it states that the indirect costs for property tax loss are not charged to the enterprise fund. We recommend removing this cost for the simple reason the city does not charge taxed on its own property and therefore there is no loss of taxes to be recouped.
2. Review the Identified Costs Annually – As time passes, the city may make changes to its operations, add or eliminate staffing, or functions are reorganized. A prime example is the recent changes in the finance department with the elimination of the finance director's position and the separation of the treasurer's and collector's jobs. City officials should review all identified costs and allocation methodology to ensure both are current and accurate.

3. Report City Council Votes Appropriately on the Tax Recap and Schedule A-2 – As reported in the budget and voted by council, only direct expenditures are budgeted in the enterprise fund and the indirect costs are appropriated in the general fund (and subsequently reported on the Schedule A, yearend report of actual revenues and expenditures). Council approves the budget by major categories (e.g., general government, public works, unclassified, and debt). When each major category is voted, dollar amounts to be transferred in from the enterprise fund for indirect costs are included. As such, the direct enterprise costs should be reported in column F (from Enterprise Funds) on the tax recap page 4 and in section 2a of Schedule 2-A, Enterprise Funds. The indirect costs are reported in section 2b of Schedule 2-A and included with amounts in column B (from Raise and Appropriate). Together, they will equal the total enterprise estimated receipts listed under IIIb (3) on page 2 of the tax recap. The separation of these costs corresponding to the appropriations made is designed to be able to tie the figures back to the budget and ensure they are not duplicated.

## **ADDITIONAL INFORMATION**

During the discussion with city officials, two additional inquiries were raised regarding the city's payroll function and how best to handle cannabis receipts.

**Payroll Function** Attached is a grid (Human Resources (HR) and Payroll Duties) contrasting the primary functions of a human resources department and a payroll department to highlight key points to consider. While the functions of the two departments overlap, they have separate responsibilities with divergent focuses and priorities. Human resources by definition serve the employee, whereas payroll is a fully financial function. By maintaining them as two departments, they provide a best practice check and balance.

**Cannabis Receipts** Easthampton has more than one establishment in the city and asked about best practice on handling the revenues received. As a new revenue stream, there is no guarantee on the volume of sales that occur in the community and what the impact will be as establishments open in surrounding communities. To this inquiry, we have attached two Division of Local Services' documents, Local Finance Opinion (LFO) 2018-3, Money from Marijuana Establishments and Medical Marijuana Treatment Centers, and Informational Guideline Release (IGR) No. 17-20, Stabilization Funds.

A municipality may (1) impose a local excise on the retail sales of marijuana for adult use and (2) negotiate impact fees or other payments under a community host or other agreement with a marijuana establishment or medical marijuana treatment center in connection with its siting and operation in the municipality. These are general receipts that should be credited to the general fund (G.L. c. 44 § 53) and can only be spent after appropriation. However, the city may use a local acceptance option to dedicate all, or a portion of at least 25%, of the collections of the excise on retail sales of marijuana or payments from a community host and other agreement payments to a general or special purpose stabilization fund established under G.L. c. 40 § 5B. If included as estimated receipts, significant fluctuations could impact balancing the annual operating budget. Alternatively, opting to dedicate the revenues to one or more stabilization funds would assist in the city in building its reserves for future capital projects, acquisitions, and one-time expenditures.

## Human Resource (HR) and Payroll Duties

Function	HR	Payroll	Comments
General	<p>Employee focus</p> <ul style="list-style-type: none"> <li>▪ Employee relations</li> <li>▪ Paperwork</li> <li>▪ Alphabet soup</li> </ul>	<p>Financial focus</p> <ul style="list-style-type: none"> <li>▪ Compensating employees</li> <li>▪ Reconciliations</li> <li>▪ Subject to financial audit</li> </ul>	<p>The two offices have divergent priorities Best practice is to maintain segregation of duties</p>
New hires	<p>Hire new employees:</p> <ul style="list-style-type: none"> <li>▪ Collect personnel data</li> <li>▪ Conduct onboarding</li> <li>▪ Solicit benefit enrollments</li> </ul>	<p>Enter new hire payroll data:</p> <ul style="list-style-type: none"> <li>▪ Dates</li> <li>▪ Classification or bargaining unit</li> <li>▪ Wages</li> <li>▪ Benefit selections</li> <li>▪ Tax withholding</li> <li>▪ Bank data</li> </ul>	<p>Information gathered by HR, verified and entered into employee record by payroll</p>
Ongoing	<ul style="list-style-type: none"> <li>▪ Maintain master employee database</li> <li>▪ Provide all employee forms</li> <li>▪ Create and update job descriptions</li> </ul>	<p>Verify and process employee information related to payroll</p> <ul style="list-style-type: none"> <li>▪ Updates based on information received from HR</li> </ul>	<p>Information gathered by HR, verified and entered into employee record by payroll</p>
Compensation	<ul style="list-style-type: none"> <li>▪ Establish classification and wage structures</li> <li>▪ Manage personnel action forms for changes</li> </ul>	<ul style="list-style-type: none"> <li>▪ Prepare cyclical payroll based on employee classification or bargaining agreement and timesheet data</li> <li>▪ Process pay adjustments and additional wages and stipends based on authorized personnel action forms</li> </ul>	<p>Information processed by payroll based on guidelines established in HR</p> <p>HR initiated changes verified by payroll</p>
Benefits	<p>Manage:</p> <ul style="list-style-type: none"> <li>▪ Benefit administration</li> <li>▪ Open enrollment</li> <li>▪ Benefit selections and changes</li> </ul>	<ul style="list-style-type: none"> <li>▪ Update employee payroll record with changes</li> <li>▪ Monitor leave accruals and balances</li> <li>▪ Process withholdings</li> </ul>	<p>HR creates and manages the paperwork</p> <p>Payroll verifies HR paperwork and enters into payroll system</p>

Function	HR	Payroll	Comments
Compliance and Reporting	Monitor that internal practices and activities comply with external governmental requirements: <ul style="list-style-type: none"> <li>▪ Antidiscrimination</li> <li>▪ Wage and hours (FLSA)</li> <li>▪ Benefits and Leave</li> <li>▪ Immigration</li> <li>▪ Safety</li> </ul>	Internal: <ul style="list-style-type: none"> <li>▪ Ensure employee payment data complies with current classification or bargaining unit</li> </ul> External: <ul style="list-style-type: none"> <li>▪ Ensure payroll activities comply with federal, state, and local laws</li> <li>▪ Remit federal and state taxes</li> <li>▪ Prepare and remit quarterly and year-end reporting</li> </ul>	HR requires constant and consistent communication with employees  Payroll is driven by financial activity and reporting deadlines
Financial		<ul style="list-style-type: none"> <li>▪ Fund payroll and associated town charges</li> <li>▪ Reconcile payroll and withholdings with accounting officer</li> <li>▪ Prepare withholding warrant</li> <li>▪ Manage relationships with financial institutions</li> </ul>	No HR role
Confidentiality	Must maintain complete confidentiality of employee files	Public has access to certain payroll information: <ul style="list-style-type: none"> <li>▪ Gross wages</li> <li>▪ Employee contract information</li> <li>▪ Negotiated benefits</li> </ul>	Different regulations for employee data