

Lake Don Pedro Community Services District

Draft 2016 Budget Preparation Memorandum

May 16, 2016

1 BUDGET OVERVIEW

1.1 PURPOSE

We are pleased to present to the Board of Directors the proposed 2016 Fiscal Year budget assumptions and criteria. Through the Board's public review of the following budgeting criteria, staff can be assured that their effort in developing the actual budget numbers is in alignment with the vision and direction of the Board. Following this Board exercise, the Board's Finance Committee will assist in developing a final budget version to be considered by this Board in June 2016.

The development of the small public agency budget is as much an exercise in public outreach and education as it is in finance and fiscal accountability. Effective special district budgets tie directly to strategic plans and management goals and objectives, are simply presented and easily understood by the average District service customer. The District has seen much confusion over its financial performance, and as we have seen this year, even when you complete \$2 million in infrastructure projects using mostly grant money, there can be misunderstandings and misstatements made within the community. Through these budget processes we attempt to inform the general public of the good work we do at the LDPCSD.

1.2 TRANSPARENCY

To provide a basis of budget understanding, the assumptions, criteria and procedure of budget development is articulated in this memorandum to offer the reader with the background necessary to comprehend the methodology used and performance to budget within the year currently coming to a close; as well as the ability to transition into the upcoming budget year with the information necessary to identify trends, financial red flags, budget influences and other factors. The budgeting exercise is therefore used as a vehicle to increase financial transparency and accountability.

1.3 ACCOUNTABILITY

Budgeting is also a management tool used to continuously refine financial accounting methods to evaluate the impact of delivering various levels of public services. For example, we need to be able to not only quickly recognize when we have underestimated cost for materials and supplies; we should also have the ability to know whether the added expenses could have been avoided by replacing something sooner; such as a pump. We also need to carefully understand the cost for full water system maintenance according to an industry standard, versus the cost to allow equipment to deteriorate without much maintenance, ultimately replacing it sooner than typically required. Throughout the upcoming year, we will be refining our accounting practices to allow for this level of

expense tracking so that in future budgets, we can easily understand the value and cost of our efforts, in each of the major areas of the services we provide.

1.4 SERVICE LEVELS

Special districts are truly the most responsive vehicle in which to respond to a community's service provision needs. In some cases, a district is formed to provide a single public service such as water, and in others such as Lake Don Pedro, a district is formed to serve as a stable entity in the delivery of services that were mandated as a condition of development. Considering these differences, it is important to understand the fact that some of our service levels are fixed by law, and others are at the discretion of the community through its district Board of Directors.

For example, the District provides public, domestic water supply in accordance with various permits issued by the state. These permits are an example of a service in which our actions and service levels are for the most part fixed by others. We have a fiduciary responsibility under the permits to employ the certified staff and work them around the clock if necessary, purchase the monitoring equipment, replace and upgrade infrastructure to standards, perform sampling, purchase materials and supplies and apply the methods necessary to meet the specific operational conditions detailed in these complex permits. Noncompliance with permits results in serious fines issued by the state on a daily basis. Budgetary limitations are not an excuse for noncompliance with permit conditions.

Property or vehicle maintenance is an example of activities where we have the discretion to set service levels. Other than for fire protection and potential liability reduction, there are no state or federal mandates that require us to perform ongoing property maintenance to a specific level; however, lack of maintenance on properties makes for ugly property, and lack of vehicle maintenance is not only ugly, but can shorten the life of a vehicle. Conducting our work in a manner that leaves a "known" *Dangerous and Defective Condition of Public Property* is one of the few instances where a public agency can be held liable for damages determined to be caused by such defects. In either case, the Board has the discretion to allow funding for more or less emphasis on these types of activities based on its priorities.

Although not mandatory, performing property and vehicle maintenance to an established standard will reduce liability to a minimum and maximize the useful life of the property and equipment itself; thereby reducing long term costs. Maintenance to the full industry standard can be extremely expensive for a small community, especially when we perform the services and receive NO form of revenue other than fees and low assessments. This high cost often leads the special district Board to under-fund necessary maintenance work, thus making a conscious decision to perform a lower level of service than required for optimal equipment life. In our case, the District has not fully understood the responsibilities placed on all employees, expecting that all maintenance, repair, upgrades, construction, operations, permit compliance etc. could be completed by our operations staff alone. The Board does have the option to adopt, fund and implement fully compliant industry standard practices; and their approved strategic plan places emphasis in that direction.

In order for the Board to direct the maintenance of all District equipment and infrastructure in accordance with established standards, the system condition assessment must be completed, compared to standards and a thorough Capital Improvement Program (CIP) and maintenance program finalized. Staff is currently working on this plan and expects to have findings before the Board in August 2016. From this evaluation, a financial plan is created to support the CIP and maintenance program, and the Board is then able to make knowledge based decisions on the level of service desired; in particular, whether fully or partially funded.

1.5 2016 BUDGET HIGHLIGHTS:

- The water supply emergency will wrap up and remaining project expenditures will be completed under the USDA grant by September 2016
- No additional unreimbursed well project related expenditures will be budgeted
- We will end the current fiscal year with operating revenue covering operating expenses, and at minimum \$200,000 less transferred from reserves than budgeted
- Operating revenue and expense will be budgeted in balance
- Capital improvement projects will be completed including completion of the Intake Booster #2 and Ranchito Well 1 renovation
- State grant revenue in the amount of \$80,000 to reimburse for grant writing expenses from the 2015/16 fiscal year.

2 2015/16 BUDGET PERFORMANCE

Overall, based on our performance through 10 months of the year (83% roughly), and anticipated water sales and expenses through the rest of the year, we are very much on track to end the budget year with operating revenue over operating expenses by up to \$100,000, which also includes the (non-cash) depreciation expense. Normally, since we do not typically fund depreciation, but we do show the expense on our financial statements throughout the year, our monthly expenses seem higher than actual and the cash value of the depreciation expense shows up in the bank after the close of the year as a cash surplus. Bottom line is that the operating revenue and expense are balancing, but with reduced water consumption, very little revenue remains each year for capital replacement projects.

3 2016/17 BUDGET DISCUSSION

The District's budget is developed for the ensuing calendar year by the CPA and General Manager, with input from the Office and Operations Supervisors typically beginning in the spring of each year. Expenses and revenue through the first six to eight months of the year are closely analyzed and then projected through the end of the fiscal year, June 30. To understand financial trends and identify potential budgeting inaccuracies, the expenses and revenue are then compared to previous years' budgets and actual fiscal year-end figures. These identified trends, as well as areas where we had in previous years budgeted too high or low, are taken into consideration in development of the next fiscal

year's budget. Further, budget criteria are established and assumptions about known changes in expenses and revenue for the next year are forecasted and further guide budget development.

The purpose of this preliminary review of the budget assumptions and criteria is to give the Board the opportunity to better understand what makes up the budget, and why the numbers look the way they do. Explaining what drives the number can be a significant help in relating to the actual numbers once they hit the page. This budget proposal is very simply constructed and presented, due to the relatively stable and very limiting nature of our funding and limited expense fluctuations; therefore, this narrative is very important in understanding the financial condition of the District and where we will be spending the same, more or less money next year. Following are some basic assumptions and criteria used in our budget development:

3.1 SERVICES ASSUMPTIONS

- There will be no changes in the type or extent of the services provided. For example, state mandates will not require a higher level of water conservation than last year, or a higher staffing or certification level.
- No new regulations will be enacted to cause a dramatic change in operation costs
- The Regional Water Use Efficiency (WUE) Project funded by the Department of Water Resources will result in an increase in office and administrative expenses of not to exceed \$30,000, which will be reimbursed under the grant.
- Implementation of the 2016 strategic plan and WUE project will result in impacts as follows:
 - Additional office staff effort and some temporary or contract staffing time to coordinate with the Mariposa County RCD for their work regionally, and our water conservation outreach locally
 - Increased level of public communication and outreach activities for all purposes
 - Development of the Capital Improvement Program (CIP) and maintenance programs in 2016, and including funding recommendations for future years
 - Potential field staff assignment reorganization and modified job responsibilities that may affect future pay
 - Consideration of transition of the temporary office position to regular, with potential increased hours (proposed to be in the budget, but not yet decided if necessary)

3.2 REVENUE FORECASTS (REFER TO CURRENT TREASURER'S REPORT FOR BUDGET AND STATUS)

- There will be no changes in the type of revenue received; ie no new assessments adopted or fees charged
- Both water base rate and sales (consumption) revenue will be consistent with the projected fiscal year end 2016. We are not planning financially on selling more water, or gaining more customers this fiscal year.
- Assessment (standby) revenue will be the same as budgeted in 2015/16
- Customer penalty revenue will be the same as 2015/16
- Property lease revenue from the local internet service providers will be the same plus the small CPI increase per the contracts

- State grant revenue in the amount of \$80,000 will be received to reimburse for grant writing expenses from the 2015/16 fiscal year

3.3 EXPENSE ASSUMPTIONS AND CRITERIA (REFER TO CURRENT TREASURER'S REPORT FOR BUDGET AND STATUS)

The 2016/17 fiscal year budget is being prepared using the following assumptions regarding expenses:

- Increase all positions and all step levels of the Salary Scale by the published 2015 CPI
- Included step increases for regular employees that will be due in 2016/17 based on LDPCSD policy and assuming performance expectations are met
- Allow for increase in hours of the Office Clerk and transition to a regular position
- Health insurance is calculated based on 2016 rates and an estimated 10% increase in January 2017
- Workers Compensation is estimated based on 2015 rates
- Office Clerk position calculated at 70% to 80% full time and transitioning to regular position, so benefit costs may apply
- Assume one additional operator achieves a Grade II state certification and associated pay and responsibilities
- Staffing levels in the field stay the same as 2015/16 with three full time equivalent employees
- PG&E power bills will remain high at Intake due to lowering lake levels and use of the barge pumps
- Well #1 power budgeted as 2015/16, operating full time to meet the demand of customers located outside the MID Place of Use
- Emergency Wells power budgeted at \$2000 each to rotate operation and reduce Intake pumping costs
- Vehicle repair and maintenance will be increased to \$20,000 per year consistent with the expenditures expected this year, unless vehicle replacement schedule adopted and vehicles replaced; in which case the vehicle cost is reduced and lease/purchase payments increased.
- Repair and maintenance distribution expense will be increased to \$75,000 (up from the projected \$65,000 at June 30) assuming we will implement the maintenance plan and continue to use some form of contracted labor for specialty or time consuming work that reduces our ability to perform critical or overly technical work
- \$106,000 will be budgeted for completion of the final technology work required to close out the 2012 office fire project including hardware, software upgrades, asset management software, installation and programming. A \$32,000 office fire reimbursement item is budgeted in revenue to offset a portion of the expense.
- Purchased water expense will be budgeted conservatively at the midpoint between the projected year end this year, and the amount budgeted for 2015/16 below which we will certainly fall considerably due to well operation and conservation.

3.4 CAPITAL EXPENSES

Revenue and Expense for each of the following are being developed if applicable.

- 3.4.1 **Emergency Well Project Completion** – All remaining construction costs are grant funded
- 3.4.2 **Ranchito Well #1 Renovation Project**
- 3.4.3 **Replace one major piece of equipment or vehicle**
- 3.4.4 **Intake Booster Pump and Control Renovation Project** – Pump and motor for booster already purchased and in stock. Engineering completed for project and prepared for bid.
- 3.4.5 **Water Service Line Replacement Project** – DWR grant funded
- 3.4.6 **Regional Water Use Efficiency Project** – DWR grant funded, program administration by the Mariposa County RCD

3.5 PENDING BOARD INPUT

Staff seeks input from the Board on the following areas, needs and opportunities that have been discussed:

3.5.1 Funding for specific reserves such as:

- **Rate stabilization** (primarily drought related costs and revenue loss)
- **Contingency**
- **Drought Emergency** (new water supply and demand management programs)
- **Capital Equipment Reserve** – although it would not be prudent to self fund all infrastructure projects without taking on any debt when money costs are low, we need enough funding in reserve for such items as a Vehicle/Equipment Replacement Program, and for upfront planning and design costs for major infrastructure projects, to get them shovel ready. A reserve for future system expansion is also required, in which we will deposit a portion of all connection fees in the future.

3.5.2 Funding for a vehicle replacement program

For the same \$20,000 annually we expect to pay to keep our existing fleet up and running, not including the cost of staff time, labor and lost productivity, we can replace \$90,000 to \$100,000 in equipment on a five year rotation keeping vehicle maintenance to only annual maintenance and oil changes; which can be done by one person in house in a day or two per year.

3.5.3 Funding of the GASB 45 debt as detailed in the Actuarial Valuation

3.5.4 Depreciation funding as a cash item