

**CITRUS
HEIGHTS
WATER
DISTRICT**



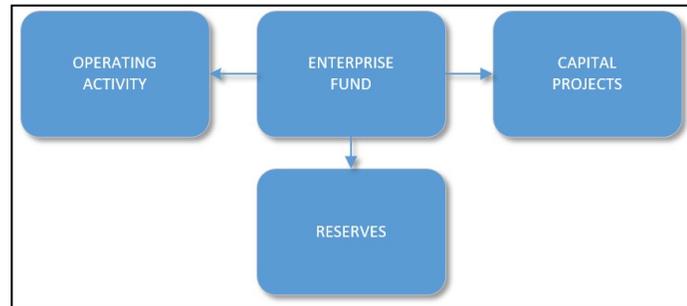
Financial Policies & Goals



Accounting and Budget Structure

Fund Structure

CHWD operates as an enterprise fund with a fiscal year that begins January 1 and ends on December 31. The District operates with one major fund on the accrual basis of accounting. Generally accepted accounting principles (GAAP) require local governments, to use a proprietary-type fund, such as an enterprise fund, to account for business-type activities similar to those found in the private sector. An enterprise fund is one in which the expenditures are supported by fees collected primarily through charging users in exchange for services. CHWD operations are supported almost entirely by fees collected from customers in exchange for providing water service, including providing customer service, continuously working to maintain and repair the District’s infrastructure, and providing a dependable supply of clean, safe water.



CHWD Fund Structure

CHWD’s management is responsible for the establishment and maintenance of the internal control structure that ensures the assets of the District are protected from loss, theft, or misuse. The internal control structure ensures that adequate accounting data is compiled to allow for the preparation of financial statements in conformity with Generally Accepted Accounting Principles (GAAP). CHWD’s internal control structure is designed to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits likely to be derived, and the valuation of costs and benefits requires estimates and judgments by management.

CHWD’s Board annually adopts a budget prior to the new fiscal year. The budget authorizes and provides the basis for reporting and control of financial operations, accountability for CHWD’s enterprise operations, and capital projects. The budget is presented on the accrual basis of accounting, and is consistent with the presentation of CHWD’s Annual Comprehensive Financial Report. As part of the budget process the financial model is updated annually to analyze revenue and expenses along with capital improvements; more information regarding the District’s financial model is provided in the “Financial Model” section. The District defines a balanced budget as one where current revenues are equal to or greater than current expenditures. The District also allows a balanced budget to use reserves to augment current revenues.

Financial Model

The Government Finance Officers Association of the United States and Canada (GFOA) recommends that government agencies complete a forecast of revenues and expenditures that extends several years into the future. The GFOA considers this to be a best practice of the budget preparation process.

In 2013, the District partnered with NBS Government Finance Group to develop a 10-year financial model. This model was first used to develop the 2014 Annual Budget. A financial model takes into account past revenues and expenditures, revenues and expenditures projected for the current and future years, economic and demographic trends, as well as expected cash flows, and produces an estimate on the financial position of the District based on these variables.

The financial model can be used to determine the appropriate service rates needed to achieve a desired financial result. This type of budgeting, commonly referred to as priority-based budgeting, is used to clearly define goals, set priorities, and deliver the best possible value to ratepayers.

In 2019, the District updated its financial model, with Raftelis Financial Consultants (Raftelis). This model was further refined in 2020 with IB Consulting. As years pass, it is a best practice to update the assumptions and factors in a financial model, as assumptions used in prior models may no longer apply. In addition to updating assumptions, CHWD desired to reevaluate its rate structure and ensure a rate allocation ratio of 65% fixed to 35% variable income. The final goal of the model update was to evaluate the current rate schedule and ascertain whether a recalibration of the rates was necessary.

As a result, the District determined that the fixed portion of the rate needed a recalibration in order to ensure that costs allocated to meters of different sizes accurately reflected the demand and usage each meter size placed on the District's water system.

The rebuild of the financial model was presented to the Board of Directors at the August 2019 Board Meeting, which included a rate calibration component.

Five Year Forecast

Table 2 illustrates the District's five-year forecast of revenues and expenditures for 2022 through 2026. The forecast includes assumptions of 4% growth in rate revenue, increased operating costs based on the Consumer Price Index (CPI) 10-Year Average for San Francisco, and increased construction costs based on the Engineering News Record Construction Cost Index (ENR CCI) 5-Year average for San Francisco.

Primary goals for this forecast include building the Water Main Replacement Reserve in order to soften the financial impact of commencing the main replacement plan charted by the Project 2030 Study, maintaining designated reserves at healthy levels, and construction of the District's seventh groundwater well.

A significant conclusion to draw from the forecast is that operational costs are projected to keep rising due to inflation, while construction costs are projected to rise due to increased materials costs caused by large-scale regional construction. In order to maintain policy-defined reserve targets, these growing costs will need to be addressed by the District.

	2020	2021	2022	2023	2024	2025	2026
	Actual	Projected	Proposed	Projected	Projected	Projected	Projected
<u>Revenues</u>							
Water Sales	16,908,986	16,807,101	16,874,305	17,541,305	18,234,305	18,955,305	19,705,305
Connection and Other Fees	2,294,771	831,963	982,901	982,901	982,901	982,901	982,901
Project 2030 Designated Charge	-	-	1,374,099	1,374,099	1,374,099	1,374,099	1,374,099
Investment and Other Income	216,845	89,081	193,000	193,000	193,000	193,000	193,000
Total Revenues	19,420,602	17,728,144	19,424,305	20,091,305	20,784,305	21,505,305	22,255,305
<u>Expenses</u>							
Salaries and Benefits	4,850,319	5,233,360	5,971,747	6,278,251	6,481,599	6,691,047	6,906,778
Water Purchases	3,444,647	3,241,422	3,135,754	3,675,000	3,675,000	3,675,000	3,675,000
Contracted Services	2,199,992	1,447,674	1,982,770	344,086	354,475	365,178	376,205
Other Operating Costs	1,968,341	1,922,675	2,456,203	4,124,223	4,178,103	4,237,422	4,297,268
Debt Service	610,000	95,000	100,000	183,922	244,431	249,431	254,431
Transfers to Reserves	1,200,000	-	1,374,099	1,374,099	1,374,099	1,374,099	1,374,099
Total Expenses	14,273,299	11,940,131	15,020,573	15,979,582	16,307,707	16,592,177	16,883,781
Operating Income before Capital Outlay	5,147,303	5,788,014	4,403,732	4,111,723	4,476,598	4,913,128	5,371,524
Capital Outlay	3,203,785	3,100,000	8,690,939	5,103,650	6,554,240	7,047,664	6,635,008
Beginning Net Position	12,870,096	16,013,614	18,701,628	15,788,520	16,170,692	15,467,150	14,706,712
Operating Revenues	19,420,602	17,728,144	19,424,305	20,091,305	20,784,305	21,505,305	22,255,305
Operating Expenses	(13,073,299)	(11,940,131)	(13,646,474)	(14,605,483)	(14,933,608)	(15,218,078)	(15,509,682)
Capital Outlay	(3,203,785)	(3,100,000)	(8,690,939)	(5,103,650)	(6,554,240)	(7,047,664)	(6,635,008)
Ending Net Position	16,013,614	18,701,628	15,788,520	16,170,692	15,467,150	14,706,712	14,817,327

Table 2

Budget Process

The District's budget process begins with its Strategic Planning meeting, typically held in June of the preceding year. The Board adopted the current Strategic Plan in August 2021. Using the 10-year financial model, the Administrative Services department

prepares the District’s revenue budget, with the input of department managers and supervisors throughout CHWD. The Engineering and Operations department review the 30-year capital improvement plan, and short-term needs to produce the annual capital budget.

Using the goals and objectives identified by members of the Board of Directors, CHWD leadership, and vested members of the community, each department prepares a draft operating budget, which is then reviewed by the General Manager. Once draft budgets are completed, they are presented to the Board in August or September in a study session, along with any recommended rate adjustments.

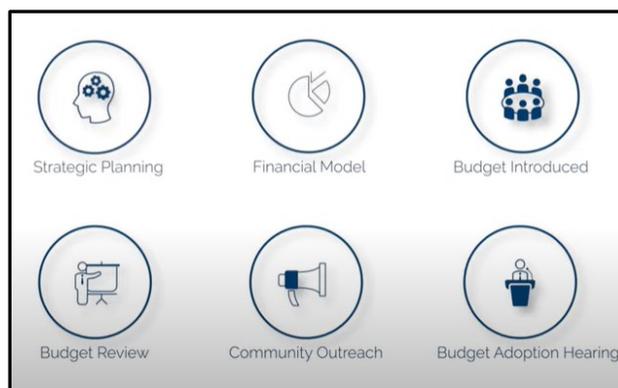
The Board then provides direction to District staff. This can either be a request for revision, or authorization to proceed with the budget process. Once the Board gives the authorization to proceed, staff will finalize the budget and, if necessary, issue a notice to its customers, pursuant to California Proposition 218 (Prop 218) including the maximum rate adjustment that the Board will consider at a scheduled public hearing. The Board then approves the budget in a public hearing held in November or December.

Budget Amendments

During the course of a year, it may be necessary to amend line items in the operating or capital budgets, or to transfer budgeted dollars between operating budget accounts, between capital projects, or between capital and operating budgets. Budgetary control rests with the General Manager up to the limits prescribed in CHWD’s Purchasing Policy. When the amount exceeds the General Manager’s authority, budgetary control rests with the Board of Directors, and Board approval is required for any budget transfers.

Budget Controls

The budget is monitored regularly by the Administrative Services department using budget-to-actual reports for both operating and capital budgets, as well as through the use of purchase orders for large purchases. Budget reports are also reviewed by the General Manager and executive team. These reports are submitted monthly to the Board of Directors.



CHWD’s Budget Process

Budget Calendar

Item	Start	Due Date
Strategic Planning	5/26/2021	5/26/2021
Regional Rate Survey	6/25/2021	8/1/2021
Create CIP List of Projects for 2022 and Financial Plan Term	7/15/2021	7/16/2021
GM to Review O&M Budget	8/13/2021	8/15/2021
Create detail CIP sheets for 2022	8/17/2021	9/30/2021
Financial Model Update to Board	9/15/2021	9/15/2021
BOD Budget and Rate Meeting	9/09/2021	9/09/2021
Final adjustments to budgets & Rate Model	9/30/2021	9/30/2011
Public Outreach	Late Sept to Late Oct	Oct to Early Nov
Present Misc. Charges and Fees to BOD	10/20/2021	10/20/2021
Revisions to detail budgets and rates per BOD direction	10/21/2021	10/24/2021
Present final budgets and rates to BOD @ Public Hearing	11/10/2021	11/10/2021
Preparation / distribution of final budget binders / 2022 rate schedule	12/1/2021	12/27/2021

Table 3

Financial Policies

The CHWD financial policies include many of the District's financial management practices that are used for operational and strategic decision making. These policies also allow the Board of Directors and community stakeholders to monitor how effectively the District is managing its financial responsibilities, as well as providing a means for holding the District fiscally accountable. These policies are reviewed annually to incorporate minor changes to existing policy, or major shifts in financial priorities at the discretion of the Board of Directors. The financial policies underwent a comprehensive review and update during 2020, which was approved at the May 8, 2020 Board of Directors meeting.

Basis of Presentation - Fund Accounting: The basic financial statements of the Citrus Heights Water District (District) are prepared in conformity with generally accepted accounting principles as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The District is accounted for as an enterprise fund and applies all applicable GASB pronouncements in its accounting and reporting. The more significant of the District's accounting policies are described below.

Investment Policy: The Board has adopted an investment policy that conforms to state law, CHWD's ordinances and resolutions, prudent money management, and the "prudent person" standards. The objectives of the Investment Policy are safety, liquidity, and then yield. Currently, funds are invested in various securities as authorized by CHWD's Investment Policy, with most of the District's funds invested in California's Local Agency Investment Fund (LAIF).

Reserves Policies: The District has eleven Reserve accounts with supported policies to balance ongoing operations to capital improvement programs. These funds are allocated to the maintenance, repair, replacement, or improvement of water system infrastructure. Adequate reserves, along with sound financial policies, provide financial flexibility to counter unanticipated expenditures or revenue fluctuations.

Basis of Accounting: The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. The enterprise fund type is accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets, deferred outflows, liabilities, and deferred inflows associated with the operation of this fund are included on the balance sheet. Net position is segregated into amounts invested in capital assets, net of related debt, amounts restricted and amounts unrestricted. Enterprise fund type operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total position.

The District uses the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

When such funds are received they are recorded as unearned revenue until earned. Earned but unbilled water services are accrued as revenue.

Water lines are constructed by private developers and then dedicated to the District, which is then responsible for their future maintenance lines are recorded as capital contributions when they pass inspection by the District, and are capitalized as donated pipelines at acquisition cost.

Operating revenues and expenses consist of those revenues and expenses that result from the ongoing principal operations of the District. Operating revenues consist primarily of charges for services. Non-operating revenues and expenses consist of those revenues and expenses that are related to financing and investing types of activities and result from non-exchange transactions or ancillary activities.

When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, then unrestricted resources as they are needed.

Use of Estimates: The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.



Customer Outreach at a Community Event

Fair Value Measurements: Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The District categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The fair value hierarchy categorizes the inputs to valuation techniques used to measure fair value into three levels based on the extent to which inputs used in measuring fair value are observable in the market.

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 inputs are inputs - other than quoted prices included within level 1 - that are observable for an asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable inputs for an asset or liability.

If the fair value of an asset or liability is measured using inputs from more than one level of the fair value hierarchy, the measurement is considered to be based on the lowest priority level input that is significant to the entire measurement.

Cash and Cash Equivalents: For purposes of the statement of cash flows, the District considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents. Cash and cash equivalents held include bank deposits and restricted and unrestricted investments in money market mutual funds and LAIF.

Restricted Assets: Certain proceeds of the District's long-term debt are classified as restricted investments on the balance sheet because their use is limited by applicable debt covenants.

Investments: Investments are stated at their fair value, which represents the quoted or stated market value. Investments that are not traded on a market, such as investments in external pools, are valued based on the stated fair value as represented by the external pool.

Inventory: Inventory consists primarily of materials used in the construction and maintenance of the water distribution facilities and is valued on a first-in, first-out basis.

Prepaid Assets: Prepaid assets consist primarily of insurance, maintenance agreements and other prepaid assets.

Capital Assets: Capital assets are tangible, personal property with a value of at least \$5,000 and a useful life of more than two years; any addition to the District's infrastructure for conveyance, treatment, pumping, or production of water with a value greater than \$15,000 and a useful life of more than two years; or any construction project, building, land, or improvement upon land with a value greater than \$15,000

and a useful life greater than two years. Capital assets are recorded at historical cost. Donated capital assets, works for art and similar items, and capital assets received in a service concession arrangement are reported at acquisition value rather than fair value. Self-constructed assets are recorded based on the amount of direct labor, material, and certain overhead charged to the asset construction calculated using the straight-line method, using the estimated useful lives in *Table 3*.

Description	Useful Life
Pipeline and Infrastructure	20 - 40 years
Equipment and Machinery	5 - 10 years
Buildings	15 - 40 years
Well Improvements	40 years
Donated Pipelines	40 years
Improvements	40 years

Table 4

Bond Premiums and Bond Issuance Costs: Bond premiums are deferred and amortized over the lives of the bonds. Long-term liabilities are reported net of the applicable bond premiums. Bond issuance costs are recognized as an expense in the period incurred.

Debt Management

CHWD funds capital improvement requirements primarily on a pay-as-you-go basis. However, there have been instances when the District has issued debt to fund significant capital projects. The District's debt instruments are secured by net revenues derived from the operation of the water system. The District may not issue or incur any new debt obligations that are superior to the installment or parity obligations under existing debt covenants. The District has no legal debt limit, and no immediate plans to issue debt for 2022.

Outstanding Debt Obligations

2010 Certificates of Participation: In 2010, the District issued \$5,155,000 of Revenue Certificates of Participation (Certificates) with an interest rate of 4.00%. These 2010 Certificates were issued to retire the 2000 Certificates of Participation, which were issued to finance certain capital improvements to the District's water system. The District is required to collect rates and charges from its water system that will be sufficient to yield net revenues equal to 110% of debt service payments on any future

debt issued, and to deposit the net revenues in a revenue fund pledged for such future debt service payments. Annual principal payments, ranging from \$450,000 to \$545,000 are due on September 28 through September 28, 2020 and semi-annual interest payments, ranging from \$10,900 to \$59,600 are due on March 28 and September 28 through September 28, 2020.

Repayment of the 2010 Certificates of Participation was completed in September 2020, which is reflected in the reduction of debt service from \$740,388 in 2020 to \$174,088 in 2021, as shown on *Table 4*.

2012 Revenue Refunding Bonds: In April 2012, the District issued \$2,275,000 of Revenue Refunding Bonds with interest rates ranging from 3.00% to 5.25%. These 2012 Revenue Refunding Bonds were issued to retire the 2003 Certificates of Participation, which were issued to finance the cost of certain capital improvements to the District’s water system. The District is required to collect rates and charges from its water system that will be sufficient to yield net revenues equal to 110% of debt service payments on any future debt issued, and to deposit the net revenues in a revenue fund pledged for such future debt service payments. Annual principal payments, ranging from \$70,000 to \$160,000 are due on February 1 through February 1, 2033, and semi-annual interest payments, ranging from \$4,200 to \$48,600 are due on February 1 and August 1, through February 1, 2033.

Debt Service Schedule

Year	Series 2010		Series 2012B		Total Payment
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	
2020	545,000	21,800	90,000	83,588	740,388
2021			95,000	79,088	174,088
2022			100,000	74,338	174,338
2023			105,000	69,338	174,338

Table 5