



Must have Financial Policies for Small Water Systems

February 4, 2020

Today's Objectives

- Understand the importance of budgeting policies
- Identify necessary reserve funds
- Recognize the need for documented policies/procedures in internal controls
- Gain insight into the necessity of reviewing reports

What Do Policies Do?

- Clarify roles & responsibilities
- Standardize procedures
- Establish consistency
- Set boundaries
- Establish standards of conduct

What Makes A Good Policy?

- Clearly written
- Fair and equitable
- Readily available
- Conforms to state and federal laws



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Planning & Budgeting

Typical Policy (example)

POLICY TITLE: Budget Preparation
POLICY NUMBER: 3020

- **3020.10** An annual budget proposal shall be **prepared** by the General Manager [FINANCE DIRECTOR, or other responsible managing employee].
- **3020.20** Prior to review by the Board of Directors, the Board's Finance Committee shall meet with the General Manager [FINANCE DIRECTOR, or other responsible managing employee] and **review** his/her annual budget proposal.
- **3020.30** The proposed annual budget as reviewed and **amended** by the Finance Committee shall be reviewed by the Board at its regular meeting in [MONTH].
- **3020.40** The proposed annual budget as amended by the Board during its review shall be **adopted** at its regular meeting in [MONTH].

Budget Policies & Procedures

- What is the Process?
- Who Develops the Budget?
- When is the Budget Due?
- Who Approves the Budget?
- What is the Process for Adjusting?
- Operating/Non-Operating Revenue & Costs

Planning and Budget Policies

- Long and Short Term Planning
- Budget Format
- Rate and User Charge Review
- Past Due, Late & Delinquent Billings

System Financial Reserves

- Operating Reserves
- Debt Reserves
- Emergency Reserves
- Short Lived Asset Reserves?
- Capital Improvement Reserves

Capital-Improvements Planning

- Your system started wearing out the day it was turned on.
- What improvements will be needed in the future
- When the improvements will be needed and when they will be undertaken
- How much the improvements will cost
- What financing options are available for the improvements

California Special Districts Association

SAMPLE POLICY HANDBOOK

POLICY TITLE: Fixed-Asset Capitalization

POLICY NUMBER: 3032

3032.1 The purpose of this policy is to provide criteria for determining when assets and associated costs are to be capitalized and depreciated.

3032.2 Single-item purchases with at least an anticipated useful life of five years and exceeding \$5,000 each shall be capitalized as a fixed asset. The purchase of these fixed assets shall be included on the District's statement of net assets and depreciated over the asset's estimated useful life. The purchase of fixed assets for less than \$5,000 shall be expensed.

3032.3 Other expenditures of \$5,000 or more that provide a significant increase in future service potential of a fixed asset shall also be capitalized as part of the existing asset.

3032.3.1 To meet the criteria for a capital expenditure, the purchase should extend the useful life of an asset, increase the quantity of service provided by an asset, or increase the quality of service by an asset.

3032.3.2 Capital expenditures may include the following: additions (enlargements, expansions or extensions of existing assets), replacements and improvements, and rearrangement and/or relocation of an asset.

3032.4 Expenditures for normal repairs and maintenance shall not be considered as capital expenditures.

3032.5 Depreciation will be computed over the estimated useful lives of the assets as follows:



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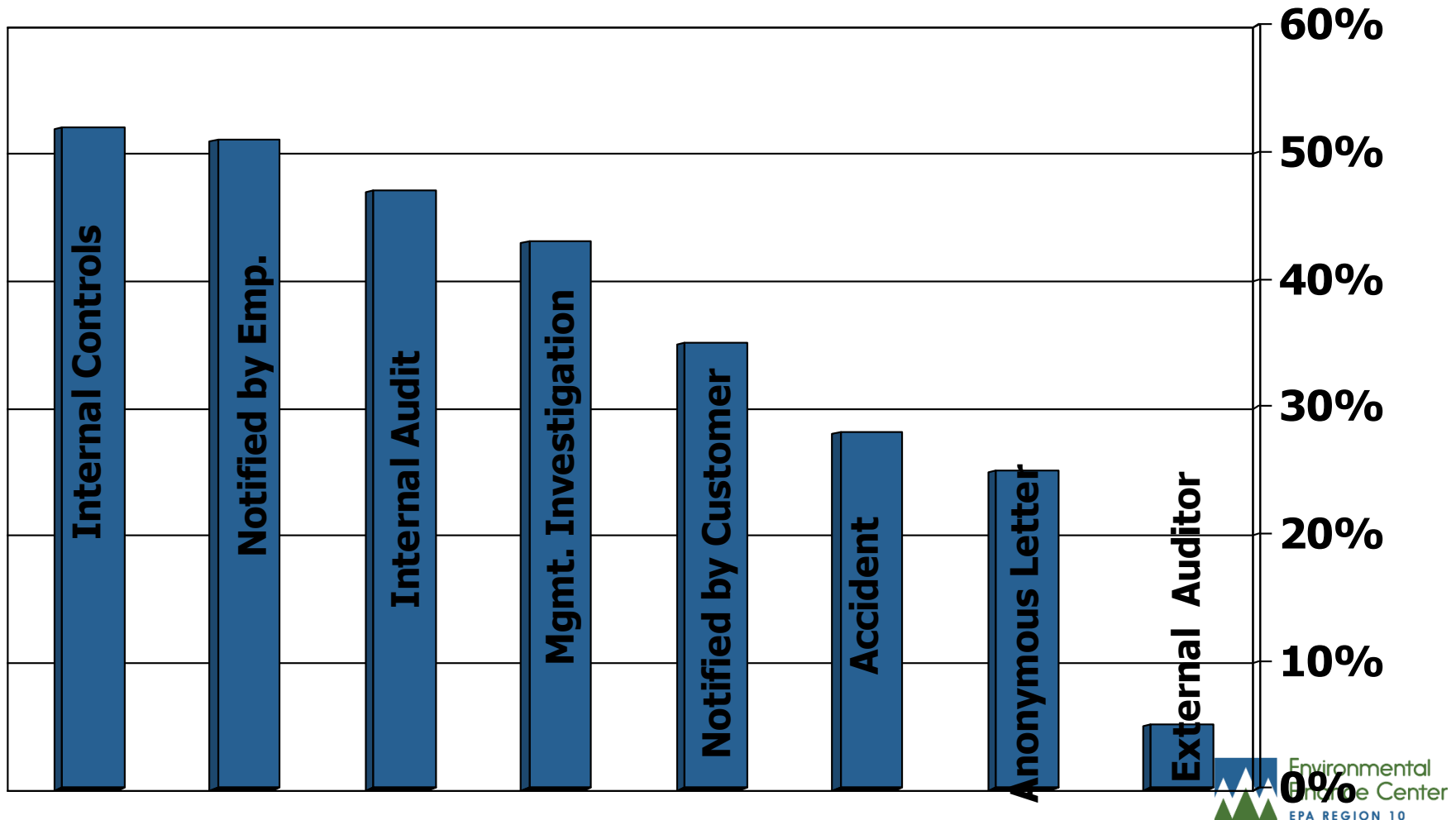


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Internal Controls

How is Fraud Discovered?



Elements of Internal Control

- Control Environment
- Risk Assessment
- Control Activities
- Information & Communication Systems
- Monitoring

What Control Elements Would Apply?

First: Is there a problem with this?

Utility gets a good deal on cell phones if they order 6 cell phones. They only need 5 so General Manager takes one home for his daughter to use.

What Control Elements Would Apply?

First: Is there a problem with this?

Due to lack of sufficient revenue, governing board votes to discontinue employee retirement fund.

The bookkeeper and staff are advised and the utility stops paying the provider without any notification.

What Control Elements Would Apply?

First: Is there a problem with this?

A detailed budget for the upcoming fiscal year is developed. The governing body approves it. The budget is filed for reference when the next year's budget is prepared.

What Control Elements Would Apply?

First: Is there a problem with this?

The bookkeeper enters new vendors in the accounting software, opens mail, enters vendor invoices, cuts checks and mails payments.

What Control Elements Would Apply?

First: Is there a problem with this?

The utility management and bookkeeper document accounting procedures. The procedures are filed in a binder. They will be used for SOPs in case a new bookkeeper is someday hired.

Control Activities

- Segregation of duties
- Physical controls
- Performance Reviews
- Information Processing Controls

Reconciliation procedures

- How are billings, receipts, and payments reconciled with ledgers and accounts of the system?
- How are daily and monthly financial transaction reports reconciled with bank statements?
- How are cash transactions and petty-cash funds reconciled, by whom, and how often?

What Policy/Procedure Could Prevent This?

The operator is building a new bathroom in his personal residence. He or she orders materials through the utility where they work. They are paid by the utility as equipment repairs and maintenance.

What Policy/Procedure Could Prevent This?

One of the maintenance staff routinely takes a two hour lunch and leaves work an hour early. The payroll clerk does not know this and cuts his paychecks for the full amount he was supposed to have worked, costing the utility thousands of dollars annually.

What Policy/Procedure Could Prevent This?

The bookkeeper enters time records for payroll, calculates payroll and issues the payroll checks. He/she feels that they are not adequately paid for the hard work they do so they add \$500 per month to their pay.

What Policy/Procedure Could Prevent This?

The bookkeeper opens a personal bank account under the name, “Valley Chemicals”. He/she then creates a “phantom” vendor account in the utility books. Every month they mails an invoice to the utility, writes a check for the invoice and deposits the check in the personal account opened under this name.

Difficulties in Implementing Internal Controls in Small Systems

- Limited Staff
- Significant number of cash transactions
- Complex accounting rules
- Regulatory focus
- Less resources to support accounting function

Question to the Group

How can internal controls be implemented in a very small utility?

When Problems Happen

Encourage the utility to:

- Have a plan and *make sure everyone knows that they do!*
- Act quickly and fairly
- Document everything
- Use outsiders to investigate
- Corrective Actions
- Find out where the system broke down



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Financial Statements

Financial Reporting

Financial Statements

- Which Ones?
- Who Produces?
- How Often?
- Timeline?
- Who Reviews?

Standard financial statements

- The Statement of Financial Position (sometimes called the balance sheet) shows the system's net worth—how much the system is worth at a particular point in time.
- The Statement of Activity (or income statement) shows the results of operations over a period of time—how much revenue the system has earned vs. the amount of expense it has incurred.

Standard financial statements

- The cash-flow statement breaks down all of the financial transactions of the system in terms of how they affect the flow of cash.
- Budget Comparison Report compares actual costs to budgeted costs

Budget Comparison Report

- If you don't know how much money your spending compared to how much you budgeted, you could be in trouble.
- A Budget Comparison Report or Budget Statement is a written report of revenues and expenses presented at each monthly Board meeting.

Additional Reports for Board Review

- Bank Reconciliation
- Check Register/Cash Disbursement log
- Customer Aged Billing Report
- Customer Billing adjustment report
- Aged Accounts Payable Report

To be reviewed, preferably by board treasurer, to provide appropriate 'checks & balances' to confirm numbers

Other Financial Reporting

- IRS Reporting
- Payroll Tax Reports
- Sales-Tax Reports
- Worker's Compensation Reports
- Funder Financial Reports



Resources

Technical Assistance

RCAC provides technical assistance to communities wanting to evaluate their systems of internal controls.



Community involvement and ownership is critical.

Recommendations of the technical assistance provider are worthless if they are never implemented.

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