ACCOUNTING APPROACH (VER 1.0)

What is it? *The accounting approach refers to how the regional entity will keep track of its revenues, expenses, assets, and liabilities (i.e. its accounting system) in a manner appropriate for its obligation and right to serve. It also informs how the entity will report its financial status for public accountability.*

How it Fits in the Regional Plan? *The guiding principles state that the entity will: manage (but not own) existing capacity, own the future water production assets, and establish wholesale rates for the region's water production needs. It follows that the regional entity's managerial and governance decisions will require timely knowledge of accounting information. Because the entity will consist of existing and new assets with different asset owners, the question of how to account for all the entity's costs poses challenges.*

A PROPOSED STARTING POINT FOR DISCUSSIONS:

The overall accounting framework should facilitate the decision making and reporting needs of the regional entity. Timely accounting information is a basic need for any organization and, in this case, the accounting framework also supports the regional entity's wholesale rate setting responsibility. However, choosing a framework is complicated by the fact that existing assets, per the guiding principles, will not be owned by the regional entity.

There are two general themes for potentially handling the accounting framework:

- Framework A: Accounting predominately handled by original asset owners with new assets handled by regional entity
- Framework B: Accounting predominately handled by regional entity for both new and old assets through system of dual record keeping.

The group should work to some overall agreement as to whether the regional entity's accounting will resemble something more of a Framework "A" or "B".

Both frameworks attempt to address the issue of separate asset ownership. Under Framework A, the system of transactions originate more from the current owners, and the system of accounts is such that the owners account for their existing assets and related expenses. Under Framework B, transactions originate more from the regional entity and requires duplicate record keeping to accomplish this. As a result, the rate setting influence under Framework A rests more with the asset owners while under Framework B it rests more with the regional entity.

Account Type	Framework A	Framework B
Summary of Differences	All accounting data for existing assets/liabilities and operational cost are held by the current owners. Any costs incurred for regional water production, including capital recovery, is invoiced to the regional entity. Owners create a "rate" or invoice for the use of their assets and resources, and charge those costs to regional entity.	Existing accounting data is duplicated by the regional entity (does not convey ownership). Accounts for existing water production facilities are then kept by both owners and regional entity. Regional entity creates a wholesale rate from its own accounting records, collects all revenue, and pays all related expenses including any contractual payments to owners for use of existing facilities.
Existing Assets	Accounted for by existing owners only.	Owners and the regional entity would reconcile asset records at the start, and the regional entity would then maintain its own asset accounting. Records would be kept by both the existing owners and the regional entity.
New Assets	Depends on capitalization approach selected. Contributory Approach: portion (or shares) of new assets recorded by owners/members. Enterprise Approach: regional entity records all new assets/members.	Depends on capitalization approach selected. Contributory Approach: portions (or shares) of new assets recorded by owners/members. Enterprise Approach: regional entity records all new assets/members.
Existing Liabilities	Accounted for by existing owners only.	Owners and regional entity reconcile outstanding debts at the start, and the regional entity would then amortize the debts shown on its books as "amounts owed to other governments". Both owners and regional entity keep accounting records.
New Liabilities	Depends on capitalization approach selected. Contributory Approach: recorded by owners / members. Enterprise Approach: recorded by regional entity only.	Depends on capitalization approach selected. Contributory Approach: recorded by owners / members. Enterprise Approach: recorded by regional entity only.
Expenses	Any costs associated with water production would be recorded by owners as operating expense.	Regional entity awards an operating contract and pays invoices to the operator for expenses incurred.
Revenues	Payments received from the regional entity for services, expenses, debt service, etc. would be recorded as revenue by the existing owner(s).	Regional entity records all wholesale revenue.

Overall, Framework A potentially simplifies the process of ensuring fairness in compensating existing asset owners. Meanwhile, Framework B potentially simplifies the process of informing decision making of the regional entity's board and seems to be more consistent with the criteria for separate reporting entity (see below discussion).

Neither framework necessarily impacts operating and capital cost recovery frameworks; these will still have to be worked out separately. It instead focuses on where the accounting information comes from.

THINGS TO CONSIDER:

Regional Entity as "Separate Reporting Entity"

An important question here is whether the proposed regional entity would meet the criteria as a separate entity for financial reporting purposes, or would instead be a component unit of one or more of the members. Separate reporting entities exhibit certain attributes that make them independent from other government organizations, whereas component units do not share those attributes.

The Government Accounting Standards Boards (GASB) Statement 14 describes the attributes that determine the financial reporting status of government organizations, including organizations like the proposed regional entity. Under these rules (GASB 14, Par. 21), a member would be financially accountable for the proposed regional water entity if at least one of the two below conditions exist:

- A member appoints a voting majority of the entity's governing body *and:* (i) it is able to impose its will on the entity; *or* (ii) there is potential for the entity to provide the member with financial benefits, or impose financial burdens on the member.
- The entity is fiscally dependent on one or more of the members.

The below table steps through the key considerations and summarizes the information from GASB's publications (note: this table is not authoritative; it is summarized and meant to help with discussion only). For local reference, the WRA reports as a separate entity per its 2016 audit.

Attribute	Conditions for Attribute to be True
1 - Regional entity is fiscally independent from the members	Must have all three of these authorities: a) Determine its budget without another member having authority to modify that budget. b) Levy taxes or set rates without approval by another government (i.e. member). c) Issue debt without approval of another government (i.e. member) If the answer is "no" to any of these, then the entity is fiscally dependent and classified as a component unit. If the answer is "yes" for all of these, then the entity is fiscally independent and the following additional characteristics should be considered.
2- Member(s) appoint a majority to the entity's Board.	If any member has the ability to appoint a majority of Board seats, then the regional entity is a component unit of that member only if one of the following 2 conditions (2A and/or 2B) are also true.
2a - Member(s) can impose its will on the entity	A member has the ability to impose its will on the regional entity if it can exercise any one of the following: a. Remove appointed members of the governing body at will b. Modify or approve the entity's budget c. Modify of approve the rate or fees affecting revenues d. Veto, overrule, or modify decisions of the Board e. Appoint, hire, reassign, or dismiss persons responsible for the day-to-day operations of the entity. Entity is a component unit if any of the above are true, in addition to the same member having the ability to appoint a majority of the board seats.
2b – Member receives financial benefits or burdens from the entity	Financial benefits or burdens exist when any one of these conditions exists: a. The member is legally entitled to access the regional entity's resources (financial resources). b. Member is legally obligated to finance deficits of the regional entity c. Member is obligated in some manner for the entity's debts

Attribute	Conditions for Attribute to be True
	Entity is a component unit if any of these conditions are true, in addition to the same member having the ability to appoint a majority of the board seats.

Handling existing assets and related costs

Accounting is complicated by the fact that the regional entity does not own any of the existing assets. This is stated in the Guiding Principles. The majority of existing assets are held by Des Moines Water Works (DMWW). In contrast, this is not the case for the WRA: it owns all the regional wastewater assets and accounts for everything within its own systems. By having a full accounting of all assets, liabilities, revenues, and expenses, the WRA can more easily make informed management and governance decisions. This information also can help establish rates for its own services that achieve full operating and capital cost recovery.

Therefore, the challenge for the regional entity is how to ensure it has access to complete financial data to inform its own decision making processes without ownership of the assets themselves. In addition, is the ability of the regional entity to function as a separate reporting entity – if that is indeed the intent – limited if the great majority of its assets and other costs are being accounted for by one (or more) of its members?