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Forest Lakes Mutual Water Company 2022 – 2027 Strategic Plan

February 2022

Acknowledgements

This five-year strategic plan is the culmination of a team effort among and between members of the Forest Lakes community, Forest Lakes Mutual Water Company staff, the Board of Directors, and the Strategic Planning Committee. This document would not have been completed and would not have been as comprehensive without the engagement and input of the stakeholders.

Special thanks must be given to Dawana Cortez, our General Manager, for her command of water rights; rules and regulations; for provision of historical data and information; and for much appreciated assistance in reviewing draft versions of this document.

We would also like to thank Forest Lakes community member Marilyn Gideon for creating historical reference documents that were summarized in the Background section of this Strategic Plan.

Pete Gonda, Chair, Strategic Planning Committee

2022 Board of Directors

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- Pete Gonda, Vice President
- Laurie Dennis, Treasurer
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- Max Mobley
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- Steve Yatson, Board member representative
- Cristina Barauskas, community member
- Henry Burnett, community member and former Board member
- Max Mobley, community member and current/former Board member
- Angela Kelly, community member
- Dave Dondero, community member
- Dawana Cortez, General Manager

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Introduction

This five-year strategic plan establishes the most important priorities of the Forest Lakes Mutual Water Company (FLMWC or Company) and the community it serves. These priorities, and their associated goals and strategies, represent a blueprint for the Company's direction over the next five years. The FLMWC is faced with key financial, operational and environmental challenges and must take steps now and in the future to ensure its long-term sustainability. The priority values, goals and strategies contained in this document will help ensure that the Company addresses these challenges in a meaningful and organized way.

Background

The Forest Lakes Mutual Water Company (FLMWC or Company) is a small and independent shareholder-owned mutual water company incorporated in 1925 that provides water and maintains private roads for 335 shareholders (individual property owners in Forest Lakes own single shares of stock in the Company). The FLMWC is governed by a seven-member elected Board of Directors (BOD or Board) with alternating two-year terms. The Board is vested with the authority to make rules and regulations associated with water conservation and distribution, and for roadway maintenance.

There are currently 327 residential metered water connections in Forest Lakes. In 2004, a moratorium on additional hookups was adopted by the Board. The moratorium was required by state law and will remain in effect until new water sources can be developed that meet demand criteria established by the California Department of Water Resources.

The Company is responsible for maintaining a seasonal fire protection reservoir that can be used for recreational purposes by FLMWC stockholders, their guests and tenants.

From its earliest inhabitants to present day, Forest Lakes has always prided itself on its strong sense of place and community.

Brief History

Forest Lakes and its surrounding area was part of a land grant from the Governor of Mexico to Pierre Sansevain in 1843 (Rancho Rincon). The land grant would not be patented until 1858 after California became a state. In the mid-1850s, after the discovery of gold near the headwaters of what would become known as Gold Gulch, Isaac Graham (who held a nearby land grant, Rancho Zayante) attempted to gain possession of the Rancho Rincon land grant, ultimately gaining ownership of part of the land that encompasses Forest Lakes.

Following his death in 1863, Graham's property was taken over by his lawyer, Edward A. Stanley, who laid the plans for Felton Township, deeded a right-of-way for the San Lorenzo Railroad Company and built a road to Gold Gulch. Stanly's land was leased for the purpose of building steam saw and planning mills for timber production. Rail lines were constructed after the Civil War that included rail stops at Gold Gulch near the present-day Lake that served sawmills owned George Treat and Frederick A. Hihn (Hihn's sawmill was located at the upper end of the Lake).

The Hihn sawmill at Gold Gulch ceased lumbering operations by 1903. Some of the land was leased or sold, with Hihn retaining the majority of the water rights.

Following the end of World War I, the country went through a period of economic growth and the mass production of automobiles provided new opportunities for families to travel together for vacations. In 1921, Highway 17 (then called Glenwood Highway) opened Santa Cruz County to the rest of the state. Land investment companies began promoting the sale of properties in the area as summer vacation home sites to San Francisco Bay and Central Valley residents.

Forest Lakes was begun in this fashion when the Seminary Avenue Land Company (Seminary) based in San Francisco purchased 616 acres of land in Gold Gulch in 1923. In 1924 the land was subdivided, and in January 1925 Seminary's corporate officers formed (incorporated) the Forest Lakes Mutual Water Company. The Hihn family deeded water and road rights to Seminary that were conveyed to the FLMWC.

From this point forward, vacation cabins were constructed in Forest Lakes, first around the Lake area and then into the upper tracts.

Strong Sense of Community

From its inception, Forest Lakes' summer inhabitants maintained a rich tradition of community gathering at the Lake, including nighttime swim parties, nightly bonfires, potlucks, Bingo games and dances (there was a large roofed and lighted dancefloor directly behind the Lake). From Fall to Spring, Forest Lakes was virtually unoccupied, with nearly everyone returning to their peninsula or inland homes.

During the 1950s, as the tract expanded and properties began to change hands, Forest Lakes began evolving from a summer resort to a residential community. Even with this changing demographic, Forest Lakes has retained its sense of place and community.

Demographic Information and Trend Data

The area of Forest Lakes consists of 616 acres in Felton, California situated between Highway 9 and Empire Grade in mixed coastal redwood forest with steep terrain in many areas of the tract. Forest Lakes contains several seasonal creeks and a diversion "lake" for fire protection that is also used for recreational purposes.

The following facts about the FLMWC are interesting to note and contribute to Company's character and uniqueness:

- Largest mutual water company in Santa Cruz County
- Only residential tract in San Lorenzo Valley with a diversion reservoir for fire protection
- Below the average statewide score for small supplier drought/water shortage risk (33 vs. 50)
- Better risk score than two-thirds of the small water suppliers in Santa Cruz County
- Maintains average systemwide water usage at 94 gallons per day per household
- Granite Construction Company is bound by legal restrictions to ensure production of two wells at the Felton Quarry that are operated by Forest Lakes

Since its formation, Forest Lakes has undergone a significant transformation from a community largely consisting of vacation homes to a community of full-time residents. Currently, 91% of all homes within Forest Lakes are occupied year-round (81% owner-occupied and 10% rentals).

This demographic shift has been positive for the community in some respects, i.e., the higher number of full-time residents helps create neighborhood comradery and continuity, and a sense of safety/security.

However, this shift has also resulted in increased service demands that have challenged the Company's ability to keep pace using the budgetary practices and operational systems currently in place. Additional fiscal pressures are apparent, including necessary road/culvert repairs resulting from the winter storms of 2017; the acceleration of aging infrastructure replacements; new realities associated with climate change; and the Company's continual challenge in retaining staff due to the inability to pay market rates.

Trend Analysis and Fiscal Challenges

In conjunction with preparing this strategic plan, available budget data was compiled and analyzed from multiple sources. A number of trends were noted that must be addressed in the future to help ensure the fiscal sustainability of the Company. These include:

- Structural budget deficit that will worsen without corrective action,
- Significant increase in capital project costs over the last 15 years,
- Flat annual assessment fee structure that has become inequitable, and
- Compensation structure that is substantially below what is offered to employees of local water agencies in the region.

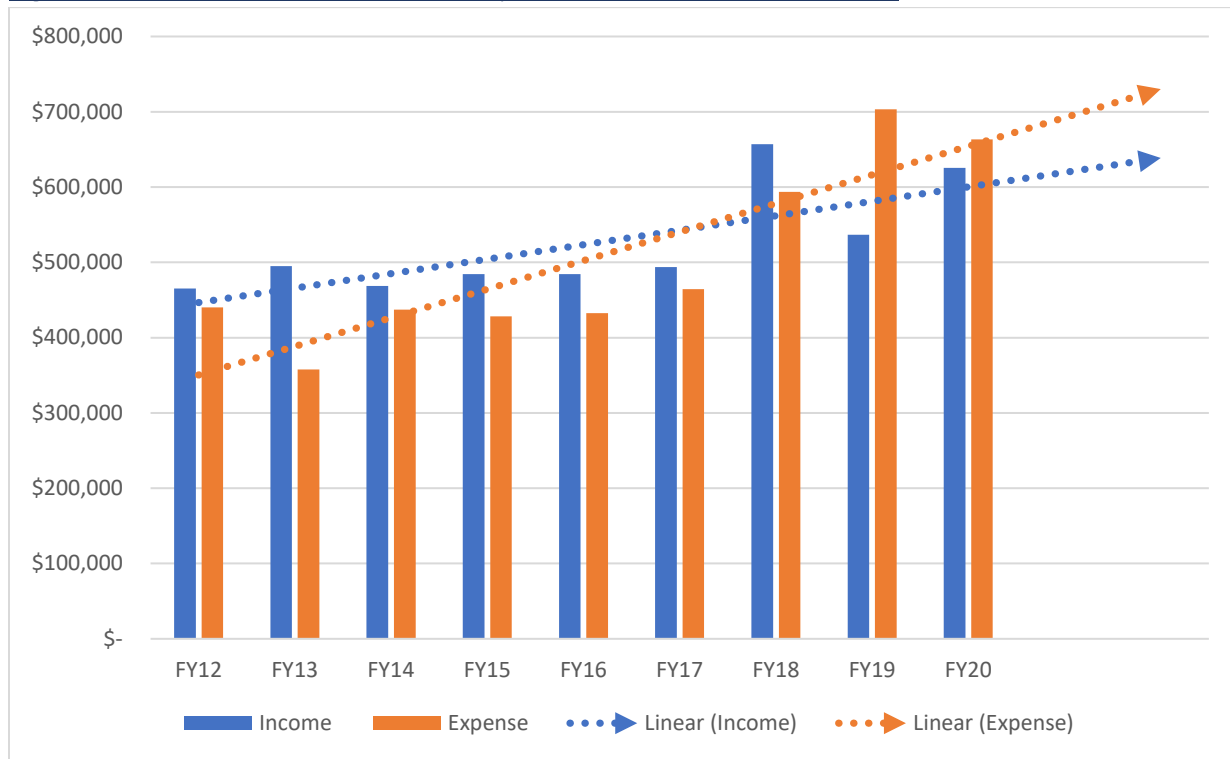
Additionally, steps must be taken to update the Company's budgeting processes and investing idle funds. For example, there is a need to create a separate (multi-year) capital budget. As another example, the Company will evaluate more effective ways of tracking operating expenses to better capture costs associated with providing water system protection, meeting regulatory requirements, and maintaining roads and/or culverts. Lastly, the Company holds its reserve funds in Certificate of Deposit (CD) accounts that do accrue minimal interest income.

Summary information on income and expenses is included below; more detailed information can be found in Appendix 1.

Structural Budget Deficit

Figure 1 below shows actual expenses (capital and operating) between 2012 and 2020. Note that the expense trendline is growing faster than current income. This gap will continue to worsen absent corrective action that will necessarily include raising additional revenue.

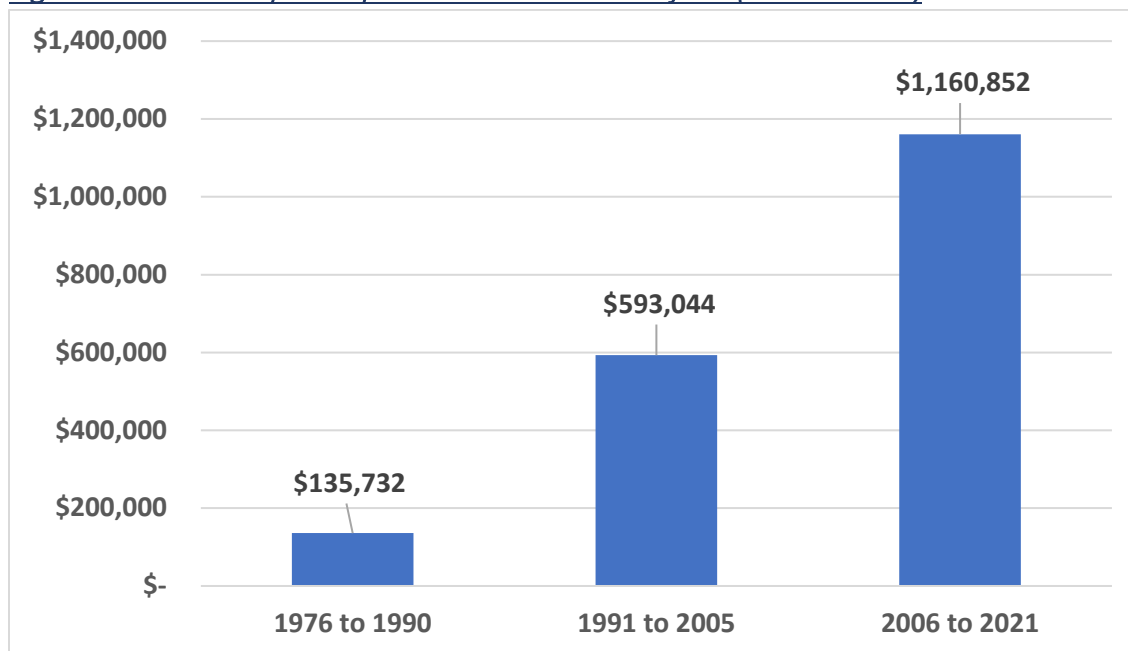
Figure 1. FLMWC Actual Income and Expenses Between 2012 and 2020



Significant Increase in Capital Costs

Figure 2 below shows the growth in capital expenses in approximate 15-year increments over a 46-year period. Since 1976 a total of nearly \$1.9 million (uninflated dollars) has been spent maintaining the FLMWC water and roadway infrastructure.

Figure 2. FLMWC Capital Expense Increases – All Projects (1976 to 2021)



This trend reflects the fact that the FLMWC infrastructure is aging, and in years past there was a tendency to defer maintenance or to limit maintenance to “band-aid” fixes that now require longer-term solutions at greater cost.

Inequitable Flat Annual Assessment Structure

Throughout its history, FLMWC has assessed shareholders a flat annual fee, as opposed to the more traditional model that includes a fixed fee component and a variable rate based on water consumption. In reviewing records kept since 1997, the flat assessment has increased by 230%, from \$620 to \$2,044. More than 20% of this increase has happened over the last five years.

During this timeframe, average systemwide water use has remained constant at approximately 94 gallons per day per household, while substantial assessment increases unrelated to actual water usage have been implemented. The rate of these increases over the past five years, a cumulative total of 48.4%, has become inequitable for those shareholders who use less water than others (see Table 1 in Appendix 1).

Inadequate Compensation Structure

In 2021, a compensation study was completed by the Human Resources (HR) Committee that reviewed hourly pay rates for regional water service providers such as San Lorenzo Valley Water District and Scotts Valley Water District, among others. The study concluded that FLMWC hourly pay rates are approximately 40% below market.

Impact of State Regulations

As a mutual water company in California, Forest Lakes must comply with numerous and ever-changing state mandates and regulations that relate to water capacity and quality. It is important that shareholders understand the level of regulation by the state and how this can impact our independence, i.e., the state can require the Company to merge with another entity.

Environmental Concerns

Like other similar service providers, Forest Lakes has been forced to confront the effects of a changing climate. Long-term drought conditions and worsening fire patterns require the Company and community residents to become more diligent in conserving water and more vigilant in hardening homes and infrastructure for fire protection.

As a testament to the community’s commitment to safety, Forest Lakes became certified as a Firewise Community in 2021, largely due to the collaborative efforts of volunteer shareholders.

Important Operational Considerations

The FLMWC is a small operation consisting of a General Manager, three Water System Operators/Maintenance Workers (one serving as lead), a part time Water Operations Manager and a part time Office Assistant. Forest Lakes staff members are dedicated to their mission and the community they serve, and it is important that the company finds ways to sustainably increase compensation and improve employee retention. For example, since 2014 the operations “division” consisting of the three operators has turned over three times, with most of the turnover attributable to better compensation packages offered by other water providers in the area.

History of Volunteerism

Woven into the rich history of Forest Lakes is the fact that the community has greatly benefitted from dedicated volunteers who serve as Board members, Committee members, emergency management coordinators, subject matter experts, maintenance workers, community engagers, recreational/social event coordinators and local historians!

As the community's demographic continues to evolve, it is essential that this level of dedication continue so that the Company's staff members can focus on their mission, to ensure that staff's efforts are supported to the best possible extent, and perhaps most importantly, to maintain our sense of place and community.

Five-year Strategic Plan (2022 to 2027)

The remainder of this document is focused on the Company's strategic plan which lays out a road map for the Forest Lakes Mutual Water Company to follow in pursuit of its vision for the future – to maintain its independence as a small, shareholder owned mutual road and water company.

The Board of Directors and Company staff will use this plan to guide decision making and measure its impact across the five key priorities established by the Board and shown below in Figure 3.

The Plan contains goals and strategies that the Company will evaluate and endeavor to implement over the next five years and will serve as a living document that can be monitored for progress and updated every five years. It is important to note that many of the strategies contained in this document are already in process.

Why Do Strategic Planning?

Strategic planning is an effective way to establish an entity's mission and organize its operational priorities. Strategic planning can:

- Provide direction to an organization.
- Align people in the organization and community toward a common purpose and shared goals.
- Create opportunities to evaluate outdated information, explore new ways of doing business and address areas of concern.

What work has taken place so far?

A strategic planning committee was created prior to the COVID-19 pandemic and several meetings were held. During the pre-pandemic timeframe, the Board and strategic planning committee took part in priority-setting exercises to develop the five key priorities. Additionally, the committee chair and general manager met on several occasions to refine and make comments on the outline of values, goals and strategies.

Work on the strategic plan was temporarily halted during the pandemic, with efforts resuming in 2021. During 2021, several community meetings were held to discuss the five key priorities and generate ideas about goals and strategies. Finally, this document was distributed to shareholders for review and comment before a final draft was considered and ultimately adopted by the Board.

Five Key Priority Values Adopted by the Board of Directors

The five most important priorities adopted by the Board are shown below.



Priority Value 1: Safeguard Forest Lakes' Independence as a small shareholder-owned mutual road and water company.

Goal A: Increase community awareness of external factors that can negatively impact Forest Lakes' independence.

Strategies for Goal A:

1. Develop and periodically update informational bulletins for shareholders that explain how state regulations and mandates can impact our independence.
2. Monitor proposed legislation and regulations and develop advocacy principles to help guide communication with state officials.

Goal B: Identify and protect critical infrastructure components needed for operational continuity.

Strategies for Goal B:

1. Prioritize infrastructure components that must be maintained to ensure business continuity and protect Forest Lakes from external factors. This may include coordination and/or contracting with outside entities.
2. Adopt a three to five-year capital improvement plan based on risk of failure and necessity for operational continuity.
3. Evaluate contingency plan option(s) in the event new regulations or other factors necessitate consolidation with another water system.

Priority Value 2: Assure the operational business continuity of the FLMWC.

Goal C: Ensure that administrative, managerial and operational procedures are documented in writing and kept up to date.

Strategies for Goal C:

1. Ensure that procedural manuals for running FLMWC (administrative, bookkeeping, water and road operations and regulatory reporting) are kept up to date.
2. Develop and maintain water system operations matrix by priority and frequency.
3. Identify key operational areas in need of redundancy and create backup/contingency plans in order of priority.
4. Evaluate methods for modernizing and streamlining administrative processes and systems.

Goal D: Ensure that the FLMWC plans for Board and employee succession.

Strategies for Goal D:

1. Develop succession plans for Forest Lakes operations staff and general manager.
2. Develop and implement an outreach plan to continually recruit Board members.

Goal E: Implement ways to increase employee retention.

Strategies for Goal E:

1. Ensure that training programs for staff are up to date, adequately funded and relevant to essential job functions.
2. Develop periodic compensation studies using benchmark water agencies.
3. Implement a competitive pay/benefits structure that is fiscally sustainable.
4. Research incentive-based alternatives with legal counsel that could potentially include revenue-sharing, bonuses based on budget savings, etc.
5. Analyze the FLMWC organizational structure to determine if staffing levels are adequate or whether there are outsourcing opportunities and evaluate implementation options.

Priority Value 3: Ensure the short and long-term fiscal stability and sustainability of the FLMWC.

Goal F: Identify additional business revenue opportunities that are equity based and adequately recover the cost-of-service provision.

Strategies for Goal F:

1. Evaluate and implement as feasible an annual assessment/rate structure that is proportionately based on the fixed cost component required by state law and a use-based component.
2. Identify and implement an appropriate index to apply to annual assessments to limit fluctuations and promote consistency for shareholder financial planning.
3. Identify and implement at least two new revenue sources.
4. Explore opportunities for privately funded monetary endowments or in-kind contributions.
5. Research options for evaluating road use/vehicle counts for apportioning road maintenance costs.
6. Research options for investing idle funds, adopt a prudent investment policy and diversify the Company's investment portfolio.

Goal G: Prudently manage ongoing capital and operating expenses.

Strategies for Goal G:

1. Carefully consider the ongoing and/or replacement costs associated with new equipment and operational expenses.
2. Eliminate the structural budget deficit.
3. Implement a three to five-year capital improvement program based on planned, priority improvements.
4. Establish a separate budget for capital expenses.
5. Evaluate different budgeting methods and implement those that result in more effective tracking capabilities and maximize state funding opportunities.
6. Secure grant funding for infrastructure improvements.
7. Research opportunities to assess shareholders and/or allocate expenses by risk factors.
8. Evaluate adoption of service charges for non-shareholder (non-Forest Lakes residents) use of private roads.

Priority Value 4: Maintain our sense of community.

Goal H: Maximize volunteer participation for coordinating community and social events.

Strategies for Goal H:

1. Establish a volunteer coordinator and task with creating volunteer database.
2. Seek out volunteers to help coordinate assistance for and communication to shareholders during emergencies/weather events.
3. Seek out volunteers to consistently coordinate community events such as BBQs, movie nights, fireside chats for storytelling, music shows and neighborhood walks.

Goal I: Promote Forest Lakes history and identity.

Strategies for Goal I:

1. Create an outreach program for new residents with the support from existing residents.

2. Solicit bios from new and longer-term residents and post on website.
3. Update the welcome packet that is sent out to new shareholders.
4. Evaluate the concept of branding and whether to create a brand or branded items for Forest Lakes.
5. Explore the establishment of an ice cream truck route.

Goal J: Improve social media and web presence to focus on community information sharing and volunteer participation.

Strategies for Goal J:

1. Explore establishing linkages between the Forest Lakes website and community media sites to share pertinent information.
2. Enlist volunteers to develop social media strategies, design new Forest Lakes webpages and maintain content.
3. Create new “owner’s manual” or include information in welcome packet about fir/other tree hazards, gray water, culvert clearing, scotch broom and ivy removal, etc.
4. Leverage virtual community meetings to enlist volunteer support and obtain input/ideas about new ways of communicating and staying in touch.

Priority Value 5: Promote and maintain environmental management practices that facilitate water conservation and minimize threats to life and property.

Goal K: Minimize risks to Forest Lakes road and water infrastructure.

Strategies for Goal K:

1. Continue to identify critical infrastructure most susceptible to failure or beyond its useful life and prioritize replacement.
2. Create inventory of hazards on Forest Lakes and shareholder property and target priority areas for mitigation based on risk factors.
3. Explore and implement partnerships with contractors to mitigate hazards, i.e., Douglas Fir removal for timber harvest.

4. Explore grant funding opportunities for residents for hazard mitigation on shareholder properties.
5. Leverage neighborhood and shareholder abilities and professional expertise to maintain properties.

Goal L: Create and maintain Communication and Evacuation Plans for use during emergencies.

Strategies for Goal L:

1. Coordinate efforts with the Fire Prevention Committee and/or consolidate safety-related committees to maximize effectiveness.
2. Establish a Safety Committee and staff with volunteers to draft Emergency Communication and Evacuation Plans for wide-scale emergency events that expand on the current plan in use for water emergencies.
3. Create and maintain essential phone/email/text trees/door-to-door to activate volunteers for needed tasks such as traffic control.
4. Establish communications with adjacent non-Forest Lakes property owners to leverage resources and develop methods/options for evacuating residents in the event of a wide-scale emergency.

Goal M: Ensure access to water supply during and after natural disasters.

Strategies for Goal M:

1. Develop systemwide and zonal contingency plans to maintain operations during emergency events.
2. Identify Board members and/or trusted volunteers who live near Company infrastructure and train them on assessing/monitoring systems during an emergency if staff members are unable to access such facilities.
3. Maintain strong policies that discourage and limit shareholder use of water during emergencies and assess substantial penalties for excessive use.

Goal N: Assess tract perimeter to identify opportunities to create fire breaks and emergency access routes.

Strategies for Goal N:

1. Establish emergency access routes where current Rights-of-Way exist.

2. Raise community awareness of techniques to help protect homes from natural disasters.
3. Maintain Firewise Community status.

Conclusion

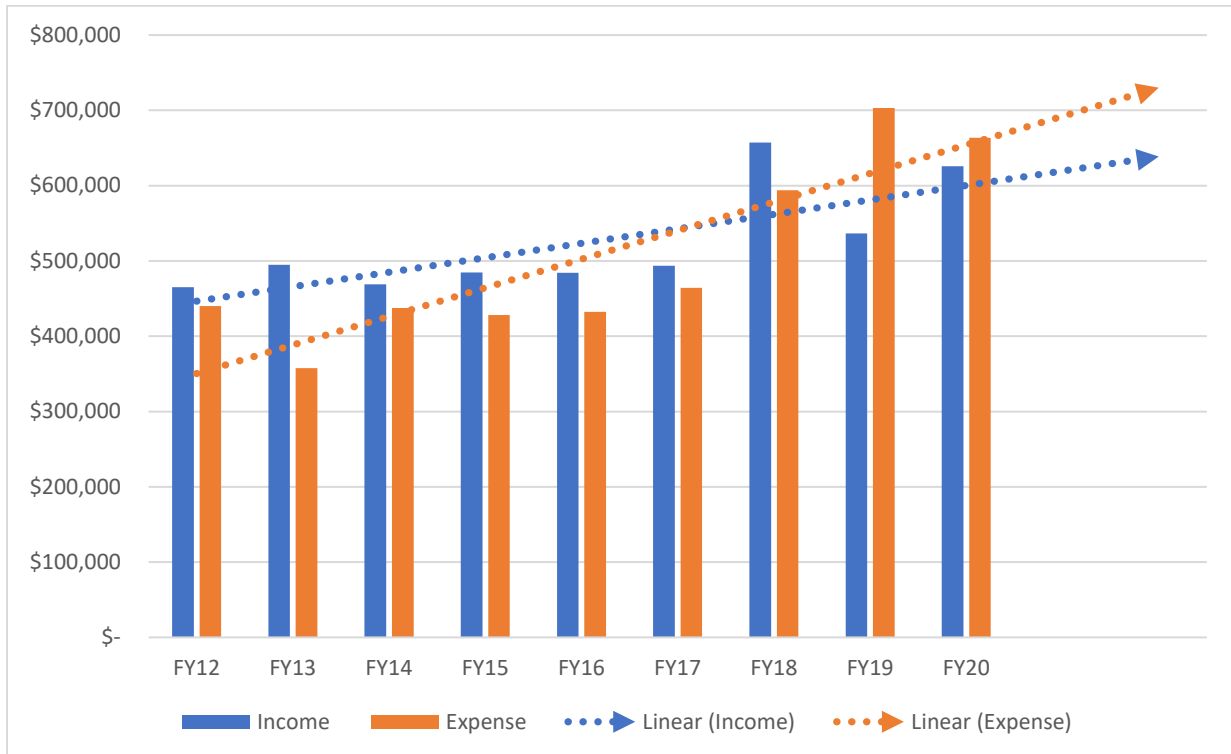
The Forest Lakes Mutual Water Company, and the community it serves, takes pride in its sense of place and status as a small non-profit mutual water company that is separate and independent from larger water systems in the region. This independence, however attractive and desirable, is fragile and vulnerable to external actions such as state regulatory mandates and natural disasters. As such, the FLMWC must be diligent in its efforts to maintain fiscal and operational viability. This five-year strategic plan is an important step that charts a course for the Company's long-term stability and sustainability.

Appendix 1: Figures and Tables Showing Trend Data

Structural Budget Deficit

Figure 1 below shows actual expenses (capital and operating) between 2012 and 2020. Note that the expense trendline is growing faster than current income. This gap will continue to worsen absent corrective action that will necessarily include raising additional revenue.

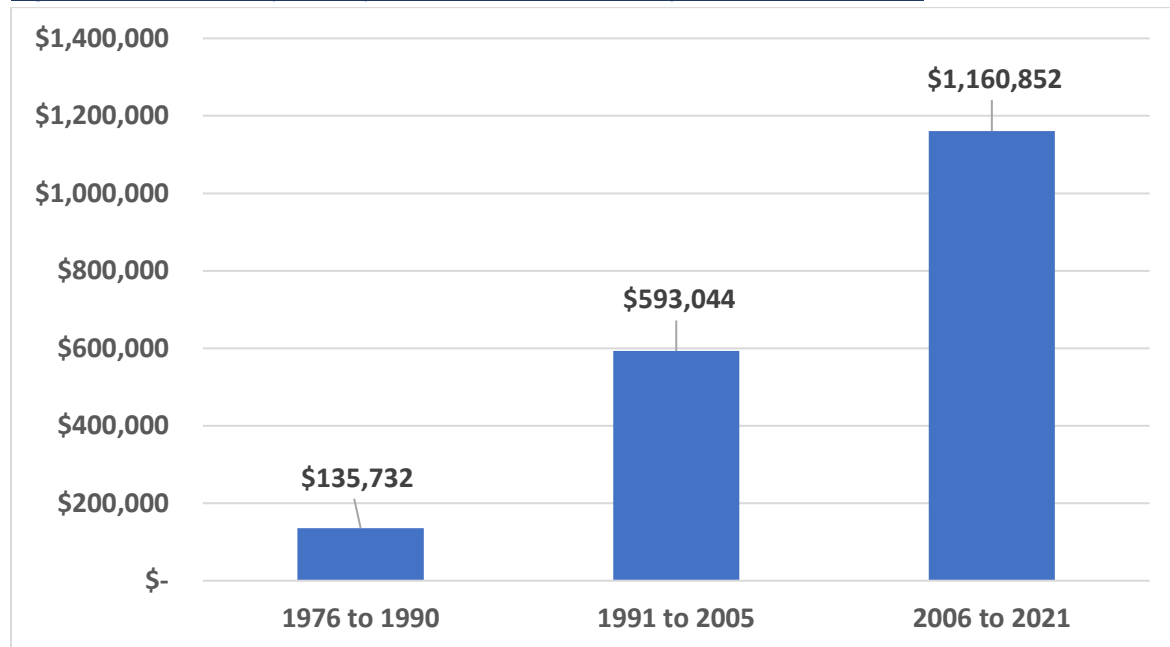
Figure 1. FLMWC Actual Income and Expenses Between 2012 and 2020



Significant Increase in Capital Costs

Figure 2 below shows the growth in capital expenses in approximate 15-year increments over a 46-year period. Since 1976 a total of nearly \$1.9 million (uninflated dollars) has been spent maintaining the FLMWC water and roadway infrastructure. (See Figure 4 below for a more detailed breakdown by capital expense type.)

Figure 2. FLMWC Capital Expense Increases – All Projects (1976 to 2021)

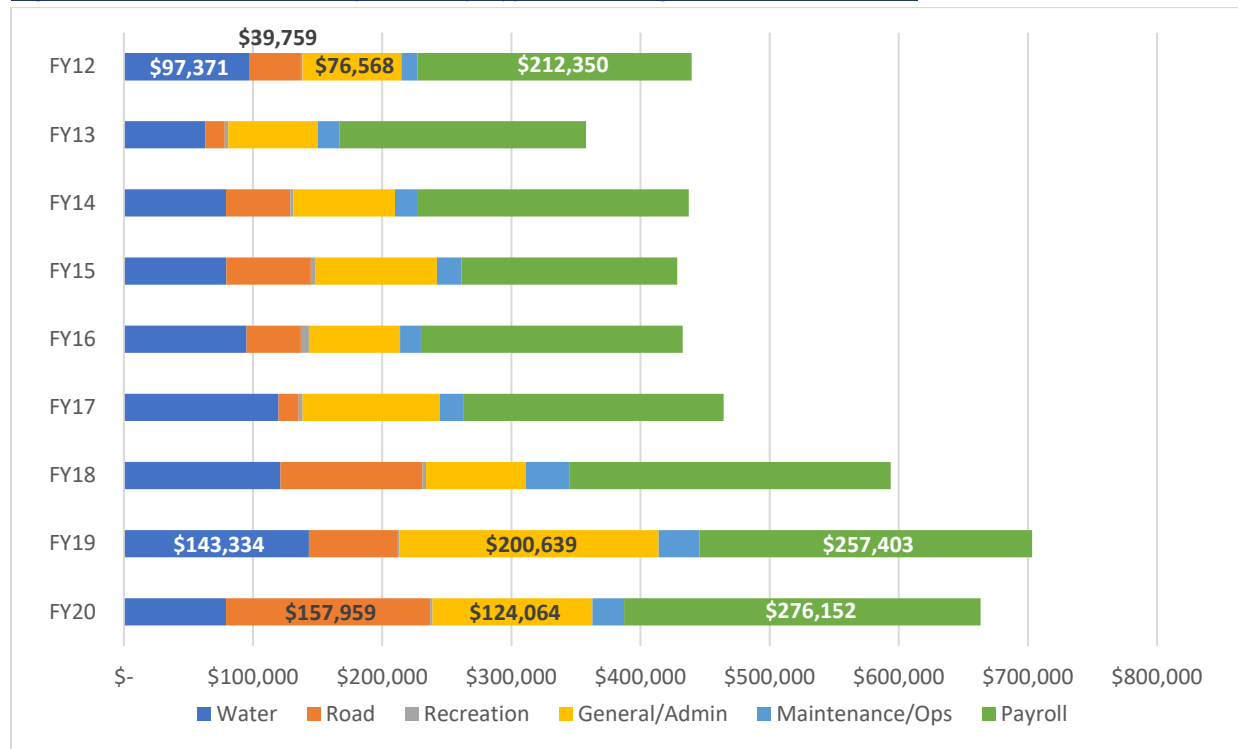


Actual Expenses by Type

Figure 3 below shows actual expenses by type over the last nine years. During this timeframe, actual expenses for road maintenance increased substantially by nearly 300% and general administrative expenses increased by 62%.

While actual payroll costs increased by 30%, a smaller increase by comparison to the road and general administrative categories, payroll constitutes the largest percentage of the total budget (an average of 44%) and will continue to grow as salary and benefit adjustments are made to bring Company compensation more in line with other water agencies in the area.

Figure 3. FLMWC Actual Expenses by Type (All Categories) 2012 to 2020



Actual Capital Expenses by Type

Figure 4 below shows actual capital expenses by type over the last 45 years, in groupings of 14-to-15-year timeframes. This is a companion graphic to Figure 2 that provides greater detail.

Figure 4. FLMWC Actual Capital Expenses by Type – 1976 to 2021

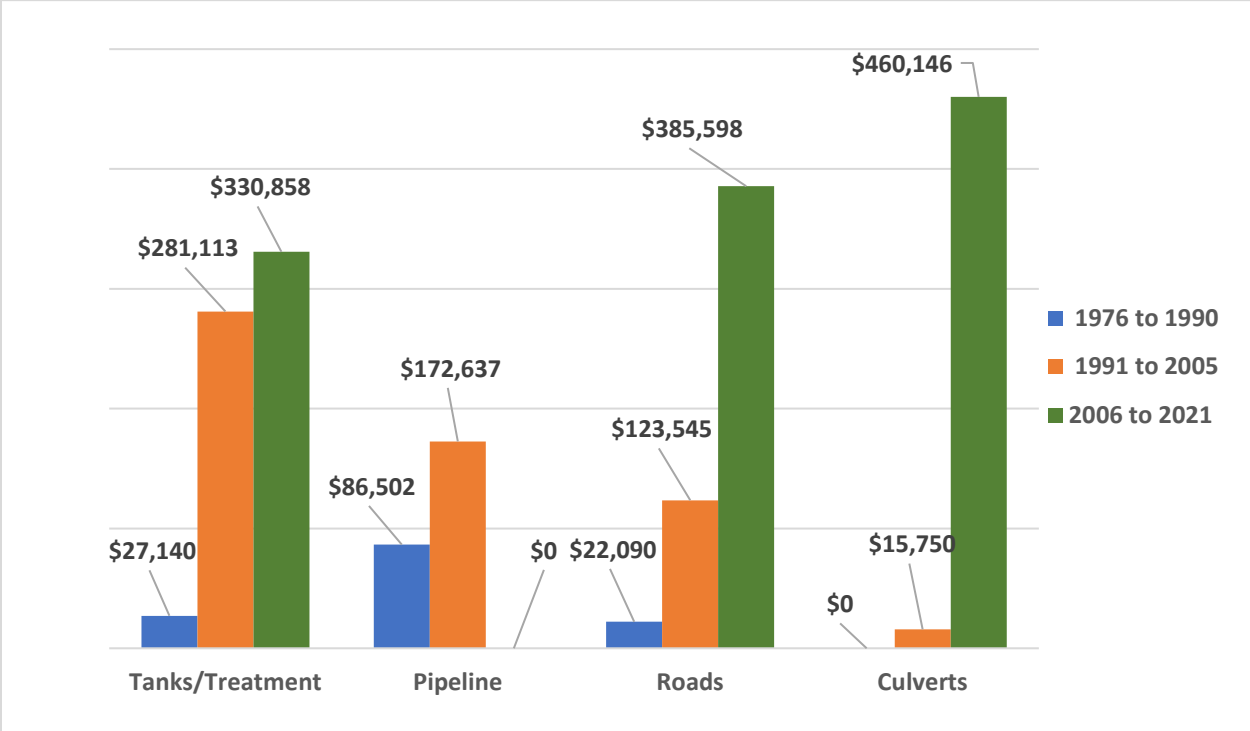


Figure 5 below shows the variances in budget to actual expenses between 2012 and 2020, providing insight into the Company’s historical method of one-year budgeting that has relied on under spending in certain expense categories (or deferring maintenance) in order to compensate for unplanned costs in other categories.

Table 1 below provides a 25-year history of annual assessments. Similarly, this table demonstrates the Company’s traditional budgeting method of establishing assessments in annual increments that can be tied to under/overspending variability seen in Figure 5. Across the 25-year timeframe, there were no assessment increases nearly half of the time, while in nine of the remaining years the annual assessment was increased by at least 6% (with a high of more than 26% in 2002 and increases between 9.8% and 20% in five of these years).

Finally, due to the actual expense trend shown in Figure 1, annual assessments are increasing at a faster/higher rate than in the past to address the structural budget gap between income and expenses. As previously noted, the pace of annual (flat) assessment increases has resulted in an inequitable fee structure that will be evaluated as part of this strategic plan.

Taken together, these variances underscore the need for more measured and predictable income and expense streams based on annual assumed inflation adjustments and planned capital improvements.

Figure 5. FLMWC Budget to Actual Variances by Expense Category – 2012 to 2020

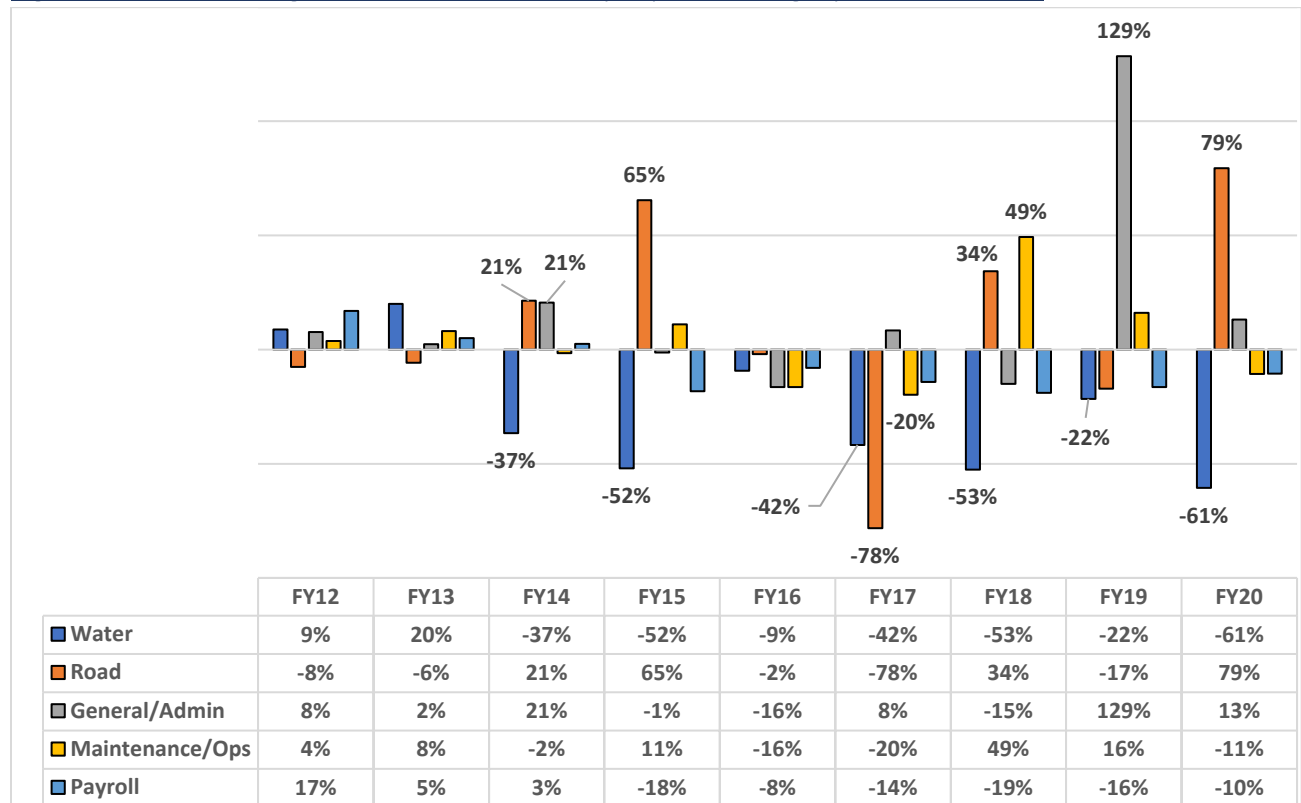


Table 1. Annual Assessments 1997 to 2021

Year	Annual Assessment	% Increase	5-year % Increase	10-year % Increase
1997	\$ 620	0.0%	12.9%	54.8%
1998	\$ 700	12.9%		
1999	\$ 700	0.0%		
2000	\$ 700	0.0%		
2001	\$ 700	0.0%		
2002	\$ 885	26.4%	37.1%	
2003	\$ 885	0.0%		
2004	\$ 940	6.2%		
2005	\$ 960	2.1%		
2006	\$ 960	0.0%		
2007	\$ 1,070	11.5%	32.8%	43.4%
2008	\$ 1,175	9.8%		
2009	\$ 1,175	0.0%		
2010	\$ 1,175	0.0%		
2011	\$ 1,275	8.5%		
2012	\$ 1,325	3.9%	8.0%	
2013	\$ 1,325	0.0%		
2014	\$ 1,325	0.0%		
2015	\$ 1,377	3.9%		
2016	\$ 1,377	0.0%		
2017	\$ 1,422	3.3%	48.4%	
2018	\$ 1,521	7.0%		
2019	\$ 1,521	0.0%		
2020	\$ 1,825	20.0%		
2021	\$ 2,044	12.0%		

Average annual increase	5.1%
Median annual increase	2.1%
25-year cumulative increase	230%