

Mission Hills Community Services District

Financial Statements

Year Ended June 30, 2014

**Mission Hills Community Services District
Financial Statements
Year Ended June 30, 2014**

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Independent Auditors' Report

To the Board of Directors of
Mission Hills Community Services District

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities of Mission Hills Community Services District (the District) as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Managements' Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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**Board of Directors of
Mission Hills Community Services District
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We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities of the Mission Hills Community Services District as of June 30, 2014, and the changes in its net position and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Mission Hills Community Services District's basic financial statements. The schedule of directors are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The schedule of directors has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Board of Directors

Mission Hills Community Services District

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Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 15, 2014, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Mission Hills Community Services District's internal control over financial reporting and compliance.

A handwritten signature in blue ink that reads "GLENN BURDETTE ATTEST CORPORATION". The signature is written in a cursive, slightly slanted style.

Glenn Burdette Attest Corporation
San Luis Obispo, California

October 15, 2014

Mission Hills Community Services District
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2014

Our Management's Discussion and Analysis of the Mission Hills Community Services District's (District) financial performance provides an overview of the District's financial activities for the year ended June 30, 2014. It should be considered in conjunction with the information within the body of the audited financial statements.

Mission Statement

The Mission Hills Community Services District is committed to providing the residents within the District reliable, high quality water and wastewater services in an efficient, cost-effective and environmentally safe manner.

Government-Wide Financial Statements

The government-wide financial statements provide readers with a broad overview of the District's finances, combining the water, sewer, and street sweeping enterprise fund data.

The District's financial statements include four components:

- Statement of Net Position
- Statement of Revenues, Expenses and Changes in Net Position
- Statement of Cash Flows
- Notes to Financial Statements

The Statement of Net Position includes all of the District's assets and liabilities, with the difference between the two reported as net position. The Statement of Net Position provides the basis for evaluating the capital structure of the District and assessing its liquidity and financial flexibility.

The Statement of Revenue, Expenses and Changes in Net Position presents information, which shows how the District's net position changed during the year. All of the year's revenues and expenses are recorded when the underlying transaction occurs, regardless of the timing of the related cash flows. The Statement of Revenue, Expenses and Changes in Net Position measures the success of the District's operations during the year and determines whether the District has recovered its costs through user fees and others charges.

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Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2014**

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The Statement of Cash Flows provides information regarding the District's cash receipts and cash disbursements during the year. This statement reports cash activity in three categories:

- Operating
- Capital and Related Financing
- Investing

This statement differentiates from the Statement of Revenues, Expenses and Changes in Net Position by only accounting for transactions that result in cash receipts or cash disbursements.

The government-wide financial statements can be found on pages 12 to 14.

The Notes to the Financial Statements provide a description of the accounting policies used to prepare the financial statements and present material disclosures required by generally accepted accounting principles that are not otherwise present in the financial statements.

The notes to the financial statements can be found on pages 15 to 22.

Financial Highlights

- Net Position was \$9,798,973 on June 30, 2014.
- Operating revenue was \$1,490,747, which consisted of Water Charges, Wastewater Charges, Street Sweeping Charges and various Service Charges.
- Total expenses were \$1,676,948, which consisted primarily of Salary related expenses, Depreciation, Utilities, Repairs and Maintenance and Profession Services.

Government-Wide Financial Analysis

Net Position

Net Position may serve over time as a useful indicator of the District's financial position. Assets exceeded liabilities by \$9,575,365 as of June 30, 2014.

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Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2014**

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The largest portion of net position reflects investment in capital assets (i.e. land, easements, wells and pumping, mains and distribution systems, buildings and improvements, vehicles, furniture, and equipment). The District uses these capital assets to provide services to the residences of the district; consequently, these assets are not available for future spending.

The remaining balance of net position is unrestricted for future spending. This portion includes cash and investments.

Please see Table A below for a current year to previous year comparison of the districts assets and liabilities.

**Table A
Statement of Net Position
June 30, 2014 and 2013**

	<u>2014</u>	<u>2013</u>	<u>% Change</u>
Assets:			
Current assets	\$ 4,299,743	\$ 4,101,478	4.8%
Capital assets	<u>5,529,174</u>	<u>5,751,541</u>	-3.9%
Total assets	<u>9,828,917</u>	<u>9,853,019</u>	-0.2%
Liabilities:			
Current liabilities	196,571	77,843	152.5%
Long-term liabilities	<u>56,981</u>	<u>62,010</u>	-8.1%
Total liabilities	<u>253,552</u>	<u>139,853</u>	81.3%
Net position:			
Net investment in capital assets	5,529,174	5,751,541	-3.9%
Unrestricted	<u>4,046,191</u>	<u>3,961,625</u>	2.1%
Total net position	<u>\$ 9,575,365</u>	<u>\$ 9,713,166</u>	-1.4%

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Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2014**

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The following are significant current fiscal year transactions that have an impact on the statement of net position:

- Total liabilities have increased due to an \$89,441 increase in accounts payable and a \$21,234 increase in accrued payroll. Long-term liabilities have decreased \$5,029 due to a decreased in accrued vacation/sick leave.
- Regular straight-line depreciation for the fiscal year ending June 30, 2014 decreased capital assets by \$295,908.

Revenues, Expenses, and Changes in Net Position

The District's financial position results from operating activities, investment activities, the acquisition and disposal of capital assets, and the depreciation of capital assets. Please see Table B below for a current year to previous year comparison of the districts revenues, expenses and changes in net position.

**Table B
Statement of Revenues, Expenses and Changes in Net Position
Years ended June 30, 2014 and 2013**

	<u>2014</u>	<u>2013</u>	<u>% Change</u>
Operating revenues	\$ 1,490,747	\$ 1,524,512	-2.2%
Nonoperating revenues	48,400	6,533	640.9%
Total revenues	<u>1,539,147</u>	<u>1,531,045</u>	0.5%
Depreciation expense	295,908	301,379	-1.8%
Operating expense	<u>1,381,040</u>	<u>1,393,984</u>	-0.9%
Total expenses	<u>1,676,948</u>	<u>1,695,363</u>	-1.1%
Change in net position	(137,801)	(164,318)	-16.1%
Beginning net position	<u>9,713,166</u>	<u>9,877,484</u>	-1.7%
Ending net position	<u>\$ 9,575,365</u>	<u>\$ 9,713,166</u>	-1.4%

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Management's Discussion and Analysis
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The following are significant current fiscal year transactions that have had an impact on the Statement of Revenues, Expenses and Changes in net Position:

- Water revenues fell short of projections by \$73,290 and Wastewater revenues were over projections by \$48,219.
- Total expenses were \$18,415 lower than last fiscal year, and \$179,641 higher than projected.

Economic Outlook

Currently the District is increasing its revenue base while the customer base remains constant. The District is land locked and unable to experience any large growth in customer base, although Summit View Homes is tentatively scheduled to begin construction in 2015 (42 Homes). The general economic trend has been in a slightly positive direction, causing the cost to provide services to increase. This has allowed the District to increase the water and wastewater rates 3.4% in the current year.

The major economic events of this fiscal year were the removal and repair of the filter material in the Granulated Activated Charcoal Water Filter and the continued regulatory action from the California Regional Water Quality Control Board concerning the Waste Water Treatment Plant stemming from the Notice of Violation (NOV) from December 2010 . This has resulted in large ongoing maintenance costs to replace and upgrade the failed infrastructure, as well as increased legal fees required in order to respond to the requirements of the Regional Water Quality Control Board. These increased funding requirements have caused the District to reevaluate all expenditures in order to reduce costs to an absolute minimum. The District was able to recover \$61,426 from our insurance carriers for claims in both this fiscal year and previous fiscal years.

The District has continued to upgrade its infrastructure by replacing the angle drive for Well #6 and removed and replaced failed laterals in the water treatment plant. The water meters currently in operation at the District are in excess of 15 years old, while the industry standard for meter life is 10 years. A replacement program was continued this fiscal year to replace 15% of the meters with Automatic Meter Reading type meters. The District has completed 73.4% of the replacement program to date. This project is anticipated to improve revenue collection as well as reducing the labor cost required to do monthly meter reading.

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Management's Discussion and Analysis
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The District has completed the following additional projects: leak detection program throughout the entire District. The District continued to utilize the services of H & S Environmental to improve the operations and ensure compliance with the requirements of the NOV. Mr. Richard Hoffman has been contracted to produce an extensive report of District operations and any possible effects the District may have had to the underlying aquifer. This action will be of great importance when addressing issues listed in the current outstanding NOV. The District has replaced the corrosion inhibitor utilized within the water distribution system, greatly improving the Lead and Copper sampling results. The District continues negotiations with Chevron Oil Company in order to provide two alternate well sites required for future use.

Contacting the District

This financial report is designed to provide the District's customers and other interested parties with an overview of the District's financial operations and financial condition. Questions concerning any of the information in this report or requests for additional information should be addressed to the General Manager, Mission Hills Community Services District, 1550 Burton Mesa Boulevard, Lompoc, CA 93436.

Mission Hills Community Services District
Statement of Net Position
June 30, 2014

Assets

Current assets:

Cash and cash equivalents	\$ 1,010,715
Accounts receivable, net of allowance	35,662
Investments	3,226,541
Prepays and deposits	26,825
Total current assets	4,299,743

Property and equipment, net of accumulated depreciation	5,529,174
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Total assets	9,828,917
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Liabilities

Current liabilities:

Accounts payable and accrued liabilities	108,209
Accrued payroll	21,421
Compensated absences, current portion	40,897
Customer deposits and advances	26,044
Total current liabilities	196,571

Long-term liabilities:

Compensated absences, net of current portion	56,981
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Total liabilities	253,552
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Net Position

Net investment in capital assets	5,529,174
Unrestricted	4,046,191

Total net position	\$ 9,575,365
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See independent auditors' report.

The accompanying notes are an integral part of these financial statements.

Mission Hills Community Services District
Statement of Revenues, Expenses and Changes in Net Position
Year Ended June 30, 2014

Operating revenues:	
Service charges	\$ 1,450,120
Late charges and other revenue	40,627
Total operating revenues	<u>1,490,747</u>
 Operating expenses:	
Chemicals	53,702
Contractual services	48,717
Depreciation	295,908
Directors' fees	7,375
Engineering services	43,293
Government charges	27,935
Insurance	17,136
Memberships and dues	8,765
Office expense	16,978
Operating supplies	7,144
Printing and publications	3,432
Professional services	63,449
Repairs and maintenance	150,165
Research and monitoring	14,877
Safety expense	5,430
Salaries, benefits and payroll taxes	697,805
Travel and meetings	16,694
Utilities	172,236
Vehicle expense	25,907
Total operating expenses	<u>1,676,948</u>
Operating loss	<u>(186,201)</u>
 Nonoperating revenues and (expenses):	
Unrealized loss on investments	(83,988)
Interest income	98,243
Insurance Reimbursement	48,487
Loss on disposition of property and equipment	(14,342)
Total nonoperating revenues and (expenses)	<u>48,400</u>
Decrease in net position	(137,801)
Net position - beginning of year	<u>9,713,166</u>
Net position - end of year	<u>\$ 9,575,365</u>

See independent auditors' report.

The accompanying notes are an integral part of these financial statements.

Mission Hills Community Services District
Statement of Cash Flows
Year Ended June 30, 2014

Cash flows from operating activities:		
Cash received from customers	\$ 1,498,651	
Cash payments to suppliers for goods and services	(593,874)	
Cash payments to employees for services	<u>(679,839)</u>	
Net cash provided by operating activities		\$ 224,938
Cash flows from capital and related financing activities:		
Purchases of property and equipment	(87,883)	
Proceeds from insurance settlement	<u>48,487</u>	
Net cash used in capital and financing activities		(39,396)
Cash flows from investing activities:		
Purchase of investments	(3,310,529)	
Investment income	<u>98,243</u>	
Net cash used in investing activities		<u>(3,212,286)</u>
Net decrease in cash		(3,026,744)
Cash and cash equivalents - beginning of year		<u>4,037,459</u>
Cash and cash equivalents - end of year		<u><u>\$ 1,010,715</u></u>
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss		(186,201)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	295,908	
Changes in operating assets and liabilities:		
Accounts receivable, net of allowance	1,612	
Prepays and deposits	(80)	
Accounts payable and accrued liabilities	89,441	
Accrued payroll	21,234	
Compensated absences	(3,268)	
Customer deposits and advances	<u>6,292</u>	
Total adjustments		<u>411,139</u>
Net cash provided by operating activities		<u><u>\$ 224,938</u></u>
Supplemental disclosures of cash flow information:		
Decrease in fair value of investments		\$ 89,369

See independent auditors' report.

The accompanying notes are an integral part of these financial statements.

Mission Hills Community Services District
Notes to Financial Statements
June 30, 2014

Note 1: Nature of Business

The Mission Hills Community Services District (the District) began operations in November of 1979, under the authorization of Section 61000, et. seq., of the Government Code of the State of California, for the purpose of providing water and wastewater disposal services. Prior to the formation of the District, these services were provided by Park Water Company. The District is a political subdivision of the State of California and operates under a Board of Directors – Manager form of government.

Note 2: Summary of Significant Accounting Policies

Basis of Presentation

For financial reporting purposes, the District is considered a special-purpose government engaged only in business-type activities. The accompanying financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB). Under the accrual basis, revenues are recognized when earned and expenses are recognized when incurred.

The principal operating revenues of the District are sewer and water usage charges and other related income. Interest income is considered non-operating revenue. When both restricted and unrestricted revenues are available for an expense, the District's policy is to use restricted revenues first, and then unrestricted fees as they are needed.

Budgets and Budgetary Accounting

An annual budget is adopted by the Board of Directors at the start of each fiscal year. Any changes or revisions to that budget throughout the year must be approved by the Board of Directors.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Cash and Cash Equivalents

The District considers all unrestricted highly-liquid investments with an initial maturity of three months or less to be cash equivalents for purposes of the Statement of Cash Flows. Cash equivalents held by brokers at year-end pending long-term reinvestment are considered investments.

Mission Hills Community Services District

Notes to Financial Statements

June 30, 2014

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Note 2: Summary of Significant Accounting Policies (Continued)

Investments

Investments are reported at fair value. Marketable securities' fair values are based on quoted market prices from independent sources. Short-term investments consist of equity securities, open-ended mutual funds, certificates of deposit and U.S. government and municipal obligations with an original maturity date of one year or less, and U.S. government and municipal obligations with a maturity date of one year or less.

Investment income consists of realized and unrealized gains and losses on investments, interest and dividends. The amounts are presented net of investment management and custodian fees.

Services and Interest Receivable

The District's accounts receivable is primarily comprised of water, wastewater, and street sweeping fees billed on a monthly basis. Customer receivables are written off in full when the receivable is deemed uncollectible. The allowance for uncollectible services is based on prior experience and management's analysis of possible bad debts. At June 30, 2014, the allowance for uncollectible services receivable was \$42,627.

Prepays and Deposits

Payments made to vendors for services that will benefit any period beyond June 30, 2014 are recorded as prepaid expenses or deposits. Prepaid expenses and deposits at June 30, 2014 was \$26,825.

Property and Equipment

Depreciation is provided for on a straight-line basis over the estimated useful lives of the assets. The estimated useful lives of the assets are as follows:

Office furniture and fixtures	5-15 years
Machinery and equipment	2-25 years
Supply distribution system	10-75 years
Building and improvements	10- 40 years
Treatment collection system	10-100 years
Vehicles	7 years

All purchased fixed assets are valued at historical cost. Donated fixed assets were recorded at their estimated net book value when the District was formed. Other donated fixed assets are valued at their estimated fair value on the date received. It is the policy of the District to capitalize assets that have a unit cost of more than \$5,000.

Mission Hills Community Services District

Notes to Financial Statements

June 30, 2014

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Note 2: Summary of Significant Accounting Policies (Continued)

Net Position

The District's net position is required to be classified for accounting and reporting purposes into the following net position categories:

- Net investment in capital assets includes capital assets net of accumulated depreciation and amortization, deferred outflows of resources, less the outstanding principal balances of debt attributable to the acquisition, construction, or improvement of those assets.
- Restricted consists of net position which is restricted as to use by the terms and conditions of agreements with outside parties, governmental regulations, laws, or other restrictions which the District cannot unilaterally alter. The District does not have any assets in this category.
- Unrestricted consists of all other categories of net position. Unrestricted may be designated for use by management of the District. These designations limit the area of operations for which expenditures of net position may be made and require that unrestricted net position be used to support future operations in these areas.

The District has adopted a policy of utilizing restricted, expendable funds, when available, prior to unrestricted funds.

Subsequent Events

Events subsequent to June 30, 2014, have been evaluated through October 15, 2014, which is the date the financial statements were available to be issued. Management did not identify any subsequent events that required disclosure.

Note 3: Cash and Cash Equivalents

District cash at June 30, 2014, consisted of the following:

Deposits	
Cash in bank	<u>\$ 927,946</u>

Custodial Credit Risk-Deposits

Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. The District does not have a formal deposit policy for custodial credit risk in addition to the California Government Code collateral requirements. Cash balances held in bank are insured up to \$250,000 by the National Credit Union Association. All deposits held by financial institutions are fully insured or collateralized with securities, held by pledging financial institutions' trust departments in the District's name.

Mission Hills Community Services District

Notes to Financial Statements

June 30, 2014

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Note 3: Cash and Cash Equivalents (Continued)

The Board has recommended certain restrictions on cash for purposes including capital replacement, emergency and operating reserves.

District pooled investments at June 30, 2014, consisted of the following:

Pooled Investment Funds:	
Cash in Local Agency Investment Fund (LAIF)	<u>\$ 82,769</u>

Local Agency Investment Fund (LAIF)

The District maintained investments with the State of California Local Agency Investment Fund (LAIF). The LAIF is an external investment pool sponsored by the State of California. These pooled funds approximate fair value. The administration of the LAIF is provided by the California State Treasurer and regulatory oversight is provided by the Pooled Money Investment Board and the Local Investment Advisory Board. State statutes, bond resolutions, and LAIF investment policy resolutions allow investments in United States government securities, negotiable certificates of deposit, bankers' acceptances, commercial paper, corporate bonds, bank notes, mortgage loans and notes, other debt securities, repurchase agreements, reverse repurchase agreements, equity securities, real estate, mutual funds and other investments. The LAIF's report discloses the required information in accordance with Governmental Accounting Standards Board Statements No. 3 and 40. Pooled investments are not required to be categorized by risk category.

Note 4: Property and Equipment

At June 30, 2014, property and equipment consisted of the following:

	<u>Balance</u> <u>June 30, 2013</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance</u> <u>June 30, 2014</u>
Land	\$ 431,163	\$	\$	\$ 431,163
Plant and equipment	9,625,502	87,882	(48,211)	9,665,173
	10,056,665	87,882	(48,211)	10,096,336
Less accumulated depreciation	(4,305,124)	(295,907)	33,869	(4,567,162)
Property and equipment, net	<u>\$ 5,751,541</u>	<u>\$ (208,025)</u>	<u>\$ (14,342)</u>	<u>\$ 5,529,174</u>

Mission Hills Community Services District

Notes to Financial Statements

June 30, 2014

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Note 5: Investments

At June 30, 2014, investments comprised the following:

Investments	
Fixed income securities	<u>\$ 3,226,541</u>

Investment Policies

The District’s Board of Directors (Board) oversees the management of its investments and establishes investment policy. The Board has delegated the implementation of the investment policy to staff. The Board advises on investment guidelines and selection of investment managers. The District prohibits investments that jeopardize the safety of principal concept, while maintaining a market rate of return and providing sufficient liquidity to enable the District to meet its cash flow requirements.

Investment Risk Factors

Interest Rate Risk:

Interest rate risk is the risk that fixed income securities will decline because of rising interest rates. The District manages interest rate risk by maintaining large coupons with short durations within its portfolio. This practice is utilized to assist the District with a positive total return.

Credit Risk:

Fixed income securities are subject to credit risk, which is the chance that a bond issue will fail to pay interest or principal in a timely manner, or that negative perceptions of the issuer’s ability to make these payments will cause security prices to decline. The District maintains policies to manage credit risk which include requiring minimum credit ratings issued by nationally recognized statistical rating organizations, including Standard and Poor’s or Moody’s Investor Services, for certain investments.

Concentration of Credit Risk:

Concentration of credit risk is the risk associated with a lack of diversification, such as having substantial investments in a few individual issuers; thereby exposing the organization to greater risks resulting from adverse conditions or developments. GASB requires disclosure of investments in any one individual issuer that represent 5% or more of total investments. At June 30, 2014, the District had no investments that exceeded this threshold.

Custodial Risk:

Custodial risk is the risk that in the event of the failure of the custodian, the investments may not be returned. Substantially all of the District’s investments are issued, registered or held in the name of the District by custodian banks and brokers, as its agent.

Mission Hills Community Services District

Notes to Financial Statements

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Note 5: Investments (Continued)

Equity Securities Risk:

Equities are subject to both unsystematic and systematic risk. Unsystematic risk is the risk of a price change due to the unique circumstances of a specific security or group of related securities. Equity securities are also subject to systematic risk or market risk. Systematic risk recognizes that equity securities, as an asset class, can change in value as a result of such factors as inflation, exchanges rates, political instability, war, economic conditions and interest rates. This type of risk is not specific to a particular company or industry and cannot be substantially mitigated by diversification. The District does not have any equity securities at this time, but is not prohibited by their investment policy to invest in equity securities.

Note 6: Long-Term Liabilities - Compensated Absences

At June 30, 2014, long-term liabilities consisted of the following:

	Balance			Balance	Current
	June 30, 2013	Additions	Reductions	June 30, 2014	Portion
Compensated absences	<u>\$ 101,146</u>	<u>\$ 45,959</u>	<u>\$ (49,227)</u>	<u>\$ 97,878</u>	<u>\$ 40,897</u>

Note 7: Service Revenues

The operations of the District are primarily funded through the collection of service fees for connection fees, water, wastewater, and street sweeping services provided for by the District. Revenues earned by type during the year ended June 30, 2014, were as follows:

Water charges	\$ 933,729
Wastewater charges	498,397
Street sweeping charges	<u>17,994</u>
Total	<u>\$ 1,450,120</u>

Mission Hills Community Services District

Notes to Financial Statements

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Note 8: Employee Benefit Plan

The District is currently participating in a FTJ FundChoice governmental eligible 457 plan administered by Bayhill Advisors, Inc. effective January 1, 2007. The Mission Hills CSD 457 Plan is a defined contribution plan and covers all employees of the District. Employees elect to contribute a portion of their salary to the plan with no limitations other than those legally imposed. An employee can also elect to contribute their social security taxes in lieu of paying into social security and the District contributes the employer portion as well. All other District contributions are discretionary and all contributions are vested 100% immediately. Assets are held separately from the District's funds. The total pension expense was \$38,890 for the year ended June 30, 2014. Contributions by plan members were \$57,185 for the year ended June 30, 2014.

Note 9: Risk Management

The District is a member of the Association of California Water Agencies Joint Powers Insurance Authority (ACWA/JPIA), which was organized for the purpose of providing general liability, automobile, errors and omission, and property loss insurance coverage to water agencies. The ACWA/JPIA is financed through premium charges to each member. The ACWA/JPIA does not meet the reporting entity criteria and is therefore not included in the accompanying financial statements.

The ACWA/JPIA is administered by a board of directors, consisting of one member of each participating water agency. In addition, the water agencies' board members and staff are eligible to participate on the various committees and subcommittees of the ACWA/JPIA. The board is responsible for establishing premium rates and making budgeting decisions.

Coverage under current policies provide for the District to pay for the first \$2,500 of property loss for buildings, personal property, fixed equipment, and mobile equipment and the agency to pay for the next \$497,500. There is a \$1,000 deductible for licensed vehicles. The auto and general liability program has no deductible. Property losses are limited to the value of the property as assessed by the ACWA/JPIA. The ACWA/JPIA is self-insured for the first \$500,000. Claims over the self-insured amounts are covered by a group purchased commercial insurance policy. Each member district is assessed a premium in accordance with the JPIA agreement, creating the ACWA/JPIA.

Mission Hills Community Services District
Notes to Financial Statements
June 30, 2014
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Note 9: Risk Management (Continued)

Condensed financial information of the ACWA/JPIA was as follows:

	<u>September 30, 2013</u>
Total assets	\$ 194,823,604
Total liabilities	<u>100,307,836</u>
Net assets	<u><u>\$ 94,515,768</u></u>
Total operating revenues	\$ 140,290,060
Total nonoperating revenues	162,348
Net assets acquired from merger	-
Total operating expenses	<u>(133,299,974)</u>
Net increase in net position	<u><u>\$ 7,152,434</u></u>

* Latest information available.

Note 10: Commitments and Contingencies

On December 2, 2010, the District received a Notice of Violations from the Regional Water Quality Control Board (RWQCB) for alleged non-compliances associated with its Waste Discharge Requirement Order 97-035 for the Wastewater Treatment Plant. The Notice of Violations required the District to take immediate actions necessary to ensure compliance with Order No. 97-035 and to submit a report addressing the violations described in the Notice of Violations. The Notice of Violations states that the District may be subject to civil liability of up to \$1,000 per day for each day in which the violation occurs.

The District submitted a Corrective Action Plan and Implementation Schedule to the RWQCB on February 28, 2011. The District has substantially followed up with the RWQCB updating them on the status of the District's efforts made consistent with its Corrective Action Plan, which has been completed. The District is still awaiting a formal written response from the RWQCB. As such there is no estimate of the potential financial impact to the District and nothing has been recorded for this potential contingency in these financial statements. The District estimates that the potential liability will not be significant, but it could be material to these financial statements.

From time to time, in the normal course of operations, the District may become involved in litigation for which the District has insurance coverage. Management does not believe this will result in a material impact to the financial statements.

**Report on Internal Control Over Financial Reporting and on Compliance
and Other Matters Based on an Audit of Financial Statements Performed
in Accordance with *Government Auditing Standards***

To the Board of Directors of
Mission Hills Community Services District

We have audited, in accordance with the auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States and the State Controller's *Minimum Audit Requirements for California Special Districts*, the business-type activities of Mission Hills Community Services District, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise Mission Hills Community Services District's basic financial statements and have issued our report thereon dated October 15, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Mission Hills Community Services District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Mission Hills Community Services District's internal control. Accordingly, we do not express an opinion on the effectiveness of Mission Hills Community Services District's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and recommendations, we identified a deficiency in internal control that we consider to be a material weakness.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatement on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying schedule of findings and recommendations as 14.01 to be a material weakness.

Board of Directors

Mission Hills Community Services District

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A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Mission Hills Community Services District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose

A handwritten signature in blue ink that reads "GLENN BURDETTE ATTEST CORPORATION". The signature is written in a cursive, slightly slanted style.

Glenn Burdette Attest Corporation
San Luis Obispo, California

October 15, 2014

**Mission Hills Community Services District
Schedule of Findings and Recommendations
Year Ended June 30, 2014**

Finding 14.01: Inadequate Segregation of Duties (Material Weakness)

Criteria:

There are generally four phases for an accounting process or operation: authorization, custody, record keeping and reconciliation. A well-designed system of internal control contemplates the allocation of duties among personnel such that each of these four functions would be performed by a different person.

Condition:

During our audit, we noticed that, due to the small size of the District staff, many of these duties are being performed by the same individuals and that the majority of the employees have access to the cash drawer.

Management has informed us that based upon the size of the District, they believe the cost to employ a sufficient number of employees with sufficient education and training to accomplish this would be cost prohibitive. While the District does not have all four phases of their accounting processes segregated, they have designed their controls to limit the potential of a material misstatement by having mitigating controls in place to detect any material misstatements that might occur. This includes detail oversight review of the trial balance on a monthly basis by both the District Manager and District Bookkeeper.

Effect:

The effect on the District of not fully segregating these functions could be to have a misappropriation of assets, although the District has mitigated the impact by the controls discussed above.

Recommendation:

We recommend that the District continue to evaluate the assignment of responsibilities and authority in the accounting department and segregate duties to the best of their ability given the size of the District and the resources available.

Supplemental Information

**Mission Hills Community Services District
Schedule of Directors
June 30, 2014**

Walter Fasold	President
Danny Hayes	Vice President
Tim Naughton	Finance Officer
James Mac Kenzie	Alternate Finance Officer
Bernard Jones	Director