

Mission Hills Community Services District

Financial Statements

Year Ended June 30, 2010

**Mission Hills Community Services District
Financial Statements
Year Ended June 30, 2010**

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**Mission Hills Community Services District
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2010**

Our Management's Discussion and Analysis of the Mission Hills Community Services District's financial performance provides an overview of the District's financial activities for the year ended June 30, 2010. It should be considered in conjunction with the information within the body of the audited financial statements.

Mission Statement

To efficiently provide safe and dependable drinking water and wastewater treatment services to Mission Hills, Mesa Oaks, The Bluffs, and Lane's End residents. We are committed to providing the best customer service possible.

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

The Statement of Net Assets included all of the District's assets and liabilities, with the difference between the two reported as net assets. The Statement of Net Assets 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 Assets presents information, which shows how the District's net assets 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 Assets 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.

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 Assets by only accounting for transactions that result in cash receipts or cash disbursements.

The government-wide financial statements can be found on pages 10 to 12.

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 13 to 19.

Financial Highlights

- Combined net assets were \$10,588,913 on June 30, 2010. There was a change of \$(542,684) in the General Fund, \$190,637 in the Water Fund, \$165,560 in the Sewer Fund and \$2,442 in the Street Sweeping Fund.
- Combined revenue was \$1,216,990, which consisted of Water Basic Charges, Sewer Basis Charges, Rate Stabilization, Street Sweeping Charges, and various Service Charges.
- Combined Expenses were \$1,421,009, which consisted primarily of Salaries, Benefits, Depreciation, Insurance, Office Expenses, Operating Expenses, Contractual Services, Travel, Utilities, Chemicals and Repairs and Maintenance.

Government-Wide Financial Analysis

Net Assets

Net assets may serve over time as a useful indicator of the District's financial position. Assets exceeded liabilities by \$10,588,913 as of June 30, 2010.

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

The next largest portion of net assets is reserved for future replacement of infrastructure. 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
Condensed Statement of Net Assets
June 30, 2010

	2010	2009	% Change
Assets:			
Current assets	\$ 4,839,119	\$ 5,081,207	-4.8%
Capital assets	<u>5,876,260</u>	<u>5,843,135</u>	0.6%
Total assets	<u>10,715,379</u>	<u>10,924,342</u>	-1.9%
Liabilities:			
Current liabilities	75,225	87,342	-13.9%
Long-term liabilities	<u>51,241</u>	<u>64,042</u>	-20.0%
Total liabilities	<u>126,466</u>	<u>151,384</u>	-16.5%
Net assets:			
Invested in capital assets	5,876,260	5,843,135	0.6%
Unrestricted	<u>4,712,653</u>	<u>4,929,823</u>	-4.4%
Total net assets	<u>\$ 10,588,913</u>	<u>\$ 10,772,958</u>	-1.7%

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

- Current assets have decreased by \$242,088 due primarily to the well construction projects.
- Total liabilities have decreased due to a \$6,003 decrease in accounts payable and a \$4,413 decrease in compensated absences.
- Regular straight-line depreciation for the fiscal year ending June 30, 2010, decreased capital assets by \$286,962.

Revenues, Expenses, and Changes in Net Assets

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 assets.

Table B
Condensed Statement of Revenues, Expenses and Changes in Net Assets
June 30, 2010

	2010	2009	% Change
Operating revenues	\$ 1,216,990	\$ 1,211,992	0.4%
Nonoperating revenues	<u>19,974</u>	<u>140,570</u>	-85.8%
Total revenues	<u>1,236,964</u>	<u>1,352,562</u>	-8.5%
Depreciation expense	286,962	184,764	55.3%
Operating expense	<u>1,134,047</u>	<u>1,150,461</u>	-1.4%
Total expenses	<u>1,421,009</u>	<u>1,335,225</u>	6.4%
Change in net assets	(184,045)	17,337	-1,161.6%
Beginning net assets	<u>10,772,958</u>	<u>10,755,621</u>	1.6%
Ending net assets	<u><u>\$ 10,588,913</u></u>	<u><u>\$ 10,772,958</u></u>	-1.7%

The following are significant current fiscal year transactions that have had an impact on the statement of revenues, expenses and changes in net assets:

- Due to decreasing interest rates, interest income was \$219,867 less than projected and \$93,756 lower than the previous fiscal year.
- Water revenues fell below projections by \$41,018 and Wastewater revenues exceeded projections by \$20,212. This shortfall in the water department could be a product of aging meters and transient population. The district has embarked upon a meter replacement program in order to address this issue.
- Total expenses were \$85,784 greater than last fiscal year, and \$3,438 less than projected.

- The significant change in net assets is due primarily to a 71% decrease in interest income and a 55% increase in depreciation expense. The primary cause for the increase in depreciation expense was the addition of the new wells.

Economic Outlook

Currently the District is constant in both its revenue base and customer base. MHCS D is land locked and unable to experience any large growth in customer base. The general economic trend has been in a negative direction, yet MHCS D has been able to hold rates for both water and waste water constant for the past six years. This has been accomplished through the judicious use of the rate stabilization funds and careful cost controls. The major economic event of this fiscal year was the failure of well #4 and the reduced capacity of well #5. This resulted in a large construction project to replace and upgrade the failed infrastructure.

MHCS D has upgraded its infrastructure by building two new well sites and replacing the aging equipment. The well sites were completed in July 2009 at a cost of approximately \$1.4 million. The meters currently in operation at MHCS D are in excess of 13 years old, while the industry standard for meter life is 10 years. A replacement program was started this fiscal year to replace 10% of the meters with Automatic Meter Reading type meters. This project is anticipated to improve revenue collection as well as reducing the labor cost required to do monthly meter reading.

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.

Principals:

David W. Phillips, CPA
David A. Bryson, CPA
Jeanne A. Potter, CPA
Daniel J. O'Hare, CPA
Kathi Niffenegger, CPA
Fred W. Bogart, CPA
Allen E. Eschenbach, CPA
Michael T. Glaudel, CPA
R. Lance Cowart, CPA
David J. Merlo, CPA



CERTIFIED PUBLIC ACCOUNTANTS
TAX AND BUSINESS ADVISORS

Emeritus:

Fred L. Glenn
Stephen A. Burdette
Bradford M. Hair, CPA

Keith V. Lapp (1932-2008)

Independent Auditors' Report

Board of Directors

Mission Hills Community Services District
Lompoc, California

We have audited the accompanying statement of net assets of Mission Hills Community Services District (the District) as of June 30, 2010, and the related statements of revenues, expenses and changes in net assets and cash flows for the year then ended, which collectively comprise the District's basic financial statements. These financial statements are the responsibility of the District's management. 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, 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*. 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Mission Hills Community Services District as of June 30, 2010, and the changes in its financial position and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 6, 2010, 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* and should be considered in assessing the results of our audit.

Board of Directors
Mission Hills Community Services District
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Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3-7 be presented to supplement the basic financial statements. Such information, although not a 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.

Our audit was made for the purpose of forming opinions on the financial statements that collectively comprise Mission Hills Community Services District's financial statements as a whole. The schedules included in the supplemental information section in the table of contents are presented for purposes of additional analysis and are not a required part of the financial statements. The supplemental information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.



Glenn, Burdette, Phillips & Bryson

Certified Public Accountants

A Professional Corporation

San Luis Obispo, California

October 6, 2010

Mission Hills Community Services District
Statement of Net Assets
June 30, 2010

Assets

Current assets:

Cash and cash equivalents	\$ 4,783,245
Services receivable, net of allowance	23,312
Interest receivable	7,597
Prepays and deposits	24,965
Total current assets	4,839,119

Property and Equipment, net of accumulated depreciation

5,876,260

Total assets

10,715,379

Liabilities

Current liabilities:

Accounts payable and accrued liabilities	24,452
Accrued payroll	3,311
Compensated absences - due within one year	27,563
Customer deposits and advances	19,899
Total current liabilities	75,225

Long-term liabilities:

Compensated absences - due in more than one year	51,241
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Total liabilities

126,466

Net Assets

Invested in capital assets	5,876,260
Unrestricted	4,712,653
Total net assets	\$ 10,588,913

The accompanying notes are an integral part of this financial statement.

Mission Hills Community Services District
Statement of Revenues, Expenses and Changes in Net Assets
Year Ended June 30, 2010

Operating revenues:	
Service charges	\$ 1,193,690
Late charges and other revenue	<u>23,300</u>
Total operating revenues	<u>1,216,990</u>
Operating expenses:	
Chemicals	26,574
Contractual services	48,272
Depreciation	286,962
Directors' fees	8,400
Engineering services	11,218
Government charges	25,880
Insurance	23,906
Memberships and dues	8,271
Miscellaneous expense	8,989
Office expense	35,275
Operating supplies	7,727
Professional services	49,544
Repairs and maintenance	65,661
Research and monitoring	10,366
Safety expense	2,836
Salaries, benefits and payroll taxes	650,080
Travel and meetings	11,621
Utilities	127,231
Vehicle expense	<u>12,196</u>
Total operating expenses	<u>1,421,009</u>
Operating loss	<u>(204,019)</u>
Nonoperating revenues:	
Unrealized loss on investments	(4,571)
Interest income	38,709
Loss on disposition of property and equipment	<u>(14,164)</u>
Total nonoperating revenues	<u>19,974</u>
Change in net assets	<u>(184,045)</u>
Net assets at beginning of year, as previously stated	10,724,104
Prior year restatement	<u>48,854</u>
Net assets at beginning of year, restated	<u>10,772,958</u>
Net assets at end of year	<u>\$ 10,588,913</u>

The accompanying notes are an integral part of this financial statement.

Mission Hills Community Services District
Statement of Cash Flows
Year Ended June 30, 2010

Cash flows from operating activities:		
Cash received from customers	\$ 1,205,711	
Cash payments to suppliers for goods and services	(497,116)	
Cash payments to employees for services	<u>(665,064)</u>	
Net cash provided by operating activities		\$ 43,531
Cash flows from capital and related financing activities:		
Purchases of property and equipment	(338,250)	
Proceeds from sale of property and equipment	<u>4,000</u>	
Net cash used in capital and financing activities		(334,250)
Cash flows from investing activities:		
Unrealized loss on investments	(4,571)	
Interest on cash and cash equivalents	<u>50,440</u>	
Net cash provided by investing activities		<u>45,869</u>
Net decrease in cash		(244,850)
Cash and cash equivalents - beginning of year		<u>5,028,095</u>
Cash and cash equivalents - end of year		<u>\$ 4,783,245</u>
Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss		\$ (204,019)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	\$ 286,962	
Changes in operating assets and liabilities:		
Accounts receivable	(12,557)	
Prepays and deposits	(1,937)	
Accounts payable and accrued liabilities	(11,212)	
Accrued payroll	(10,571)	
Compensated absences	(4,413)	
Customer deposits	<u>1,278</u>	
Total adjustments		<u>247,550</u>
Net cash used in operating activities		<u>\$ 43,531</u>

The accompanying notes are an integral part of this financial statement.

Mission Hills Community Services District
Notes to Financial Statements
June 30, 2010

Note 1: Summary of Significant Accounting Policies

The Reporting Entity

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 operates under a Board of Directors – Manager form of government.

The District is a political subdivision of the State of California. The District's financial statements are presented in accordance with *Governmental Accounting Standards*. These standards establish criteria for determining the District's activities and functions that should be included in the financial statements of a governmental unit.

For financial reporting purposes, the District would include in this report all funds of all agencies and boards that are controlled by, or dependent upon, the District's legislative body. The criteria of control is determined on the basis of financial interdependency, governing authority, designation of management, ability to significantly influence operations, and accountability for fiscal matters.

Basis of Presentation

For financial reporting purposes, the District is considered a special-purpose government engaged only in business-type activities. 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.

Basis of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned and expenses are recognized when incurred. The District follows private-sector standards of accounting and financial reporting issued prior to December 1, 1989 to the extent those standards don't conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds subject to this same limitation. The District has elected not to follow subsequent private-sector guidance.

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.

Mission Hills Community Services District

Notes to Financial Statements

June 30, 2010

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Note 1: Summary of Significant Accounting Policies (Continued)

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 demand deposits in banks and in the Santa Barbara County and Local Agency Investment Fund pooled investment account to be cash and cash equivalents.

Services and Interest Receivable

The District's services receivable is 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 totally uncollectible. At June 30, 2010, the allowance for uncollectible services receivable was \$42,896.

Interest receivable represents interest due to the District for the quarter ended June 30, 2010 from Santa Barbara County and the Local Agency Investment Fund.

Prepays and Deposits

Payments made to vendors for services that will benefit any period beyond June 30, 2010 are recorded as prepaid expenses or deposits. Prepaid expenses and deposits at June 30, 2010 totaled \$24,965.

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

Mission Hills Community Services District

Notes to Financial Statements

June 30, 2010

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Note 1: Summary of Significant Accounting Policies (Continued)

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.

Subsequent Events

Subsequent events have been evaluated through October 6, 2010, which is the date the financial statements were available to be issued.

Note 2: Cash and Cash Equivalents

District cash at June 30, 2010, consisted of the following:

Deposits	
Cash in bank	\$ 178,178

The Board has established certain restrictions on cash for purposes including replacement, emergency and development reserves. Total cash restricted due to board designation at June 30, 2010 was \$3,590,029.

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 Federal Deposit Insurance Corporation. 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.

District investments at June 30, 2010, consisted of the following:

Pooled Investment Funds:	
Cash in Santa Barbara County Treasury	\$ 1,315,421
Cash in Local Agency Investment Fund (LAIF)	<u>3,289,646</u>
	<u>\$ 4,605,067</u>

Cash in County Treasury

The District maintains a portion of its cash in the Santa Barbara County Treasury, an external investment pool. The County pools these funds with those of other governmental entities in the county and invests the cash. These pooled funds are carried at fair value. Interest is earned based on average daily balance and is deposited quarterly into the

Mission Hills Community Services District

Notes to Financial Statements

June 30, 2010

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Note 2: Cash and Cash Equivalents (Continued)

participating funds. Any investment gains and losses are proportionately shared by all funds in the pool. The County is restricted by the California Government Code to invest in obligations issued by the United States Treasury; obligations, participations, or other instruments of or issued by a federal agency or a United States government sponsored enterprise; obligations of State and local agencies of this State; bankers acceptances; commercial paper; negotiable certificates of deposit; repurchase agreements; medium-term corporate notes; as well as other investments established by the California Government Code. The County'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.

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.

Interest Rate Risk

The District does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk

The District investment policy allows the District to have monies invested in the Santa Barbara County pooled investment fund and the LAIF. Both the Santa Barbara County Treasury pooled investment fund and the LAIF are unrated.

Concentration of Credit Risk

The risk that an issuer of an investment may not fulfill its obligation to the holder of the investment is called credit risk. The investment policy of the District allows the District to maintain an operating account at a commercial bank, maintaining approximately one month's average expenditures in the account. District funds not specified for deposit or investment elsewhere are held in various accounts with the Santa Barbara County Treasurer's office. The policy also directs the District to establish and maintain an account with LAIF and provides guidelines for allocation of funds. At June 30, 2010, the District's investment in the Santa Barbara County Treasury represents 29% and the LAIF represents 71% of the total amount invested in pooled investment funds.

Mission Hills Community Services District
Notes to Financial Statements
June 30, 2010
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Note 3: Property and Equipment

Property and equipment activity for the year ended June 30, 2010, was as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Land	\$ 431,163	\$	\$	\$ 431,163
Plant and equipment	7,773,689	1,500,130	(219,041)	9,054,778
Construction in progress	1,161,283		(1,161,283)	-
	<u>9,366,135</u>	<u>1,500,130</u>	<u>(1,380,324)</u>	<u>9,485,941</u>
Less accumulated depreciation	(3,522,939)	(286,962)	200,220	(3,609,681)
Property and equipment, net	<u>\$ 5,843,196</u>	<u>\$ 1,213,168</u>	<u>\$ (1,180,104)</u>	<u>\$ 5,876,260</u>

Total depreciation expense for the year ended June 30, 2010, was \$286,962.

Note 4: Long-Term Liabilities - Compensated Absences

Long-term liabilities activity for the year ended June 30, 2010, was as follows:

	<u>Balance June 30, 2009</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance June 30, 2010</u>	<u>Current Portion</u>
Compensated absences	\$ 83,217	\$ 32,828	\$ (37,241)	\$ 78,804	\$ 27,563

Note 5: 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, 2010, were as follows:

Water charges	\$ 705,536
Wastewater charges	472,738
Street sweeping charges	<u>15,416</u>
Total	<u>\$ 1,193,690</u>

Mission Hills Community Services District

Notes to Financial Statements

June 30, 2010

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Note 6: 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 6.2% social security taxes in lieu of paying into social security and those contributions will be matched 100% by the District. 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 \$32,746 for the year ended June 30, 2010. Contributions by plan members were \$37,909 for the year ended June 30, 2010.

Note 7: 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 agency's 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, 2010
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Note 7: Risk Management (Continued)

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

	<u>September 30, 2009 *</u>
Total assets	\$ 124,067,027
Total liabilities	83,993,363
Net assets	<u>\$ 40,073,664</u>
Total operating revenues	\$ 21,082,354
Total nonoperating revenues	6,294,982
Total operating expenses	<u>(25,663,970)</u>
Net increase in net assets	<u>\$ 1,713,366</u>

* Latest information available.

Note 8: Prior Year Restatement

A prior year restatement was recorded in these financial statements as a result of the District's physical inventory of property and equipment. Assets were discovered that had been disposed of in prior periods, but never removed from the property and equipment sub ledger. The net impact of this adjustment was a decrease to net assets of \$108,997, a decrease to plant and equipment of \$785,673 and a decrease to accumulated depreciation of \$676,676.

In addition, it was determined that a wastewater line that had been put in by a developer and transferred over to the District for maintenance, was never capitalized on the financial statements. The net impact of this adjustment was an increase to net assets of \$157,851, an increase to plant and equipment of \$170,650 and an increase to accumulated depreciation of \$12,799.

The net impact of these adjustments on the financial statements was an increase to net assets of \$48,854, a decrease to plant and equipment of \$615,023 and a decrease to accumulated depreciation of \$663,877.

Principals:

David W. Phillips, CPA
David A. Bryson, CPA
Jeanne A. Potter, CPA
Daniel J. O'Hare, CPA
Kathi Niffenegger, CPA
Fred W. Bogart, CPA
Allen E. Eschenbach, CPA
Michael T. Glaudel, CPA
R. Lance Cowart, CPA
David J. Merlo, CPA



CERTIFIED PUBLIC ACCOUNTANTS
TAX AND BUSINESS ADVISORS

Emeritus:

Fred L. Glenn
Stephen A. Burdette
Bradford M. Hair, CPA

Keith V. Lapp (1932-2008)

**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***

Board of Directors

Mission Hills Community Services District
Lompoc, California

We have audited the financial statements of Mission Hills Community Services District as of and for the year ended June 30, 2010, and have issued our report thereon dated October 6, 2010. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Mission Hills Community Services District's (the District's) internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

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 misstatements 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 in internal control over financial reporting, described in the accompanying schedule of findings and recommendations at item 10.1, to be a material weakness.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We consider the deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and recommendations at item 10.2 and 10.3, to be significant deficiencies. *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.

Board of Directors
Mission Hills Community Services District
Page 2

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*.

This report is intended solely for the information and use of management, the Board of Directors, others within the entity, the County of Santa Barbara and the California State Controller's Office and is not intended to be and should not be used by anyone other than these specified parties.



Glenn, Burdette, Phillips & Bryson
Certified Public Accountants
A Professional Corporation
San Luis Obispo, California

October 6, 2010

Mission Hills Community Services District
Schedule of Findings and Recommendations
Year Ended June 30, 2010

Finding 10.01 – Physical Tracking and Reconciliation of Property and Equipment (Material Weakness)

During the year ended June 30, 2010, the Mission Hills Community Services District (the District) performed a physical inventory and reconciliation of their property and equipment listings. Assets were discovered that had been disposed of in prior periods, but never removed from the property and equipment sub ledger. A prior year restatement was recorded in the accompanying financial statements based on errors identified during the physical inventory and reconciliation. The net impact of this adjustment was a decrease to net assets of \$108,997, a decrease to plant and equipment of \$785,673 and a decrease to accumulated depreciation of \$676,676.

In addition, a Board member identified a wastewater addition, put in by a developer and transferred to the District in October 2005 that was never capitalized on the District's financial records. The estimated cost of this asset was \$170,650 and the unrecorded associated depreciation was \$12,799. The net impact of this adjustment was \$157,851.

The net financial statement impact of both adjustments was an increase to net assets of \$48,854 and was recorded as a prior year restatement.

Recommendation: We recommend that the District perform physical observations of all property and equipment at least annually and at any time there are major repairs or other significant work on any system. When the physical observations are done, all assets that have not been capitalized and all assets that have been disposed of should be recorded appropriately and in a timely manner. This will result in more accurate property and equipment listings as well as proper recording of depreciation.

Finding 10.02 – Investment Policy (Significant Deficiency)

The District has an investment policy, Board of Directors Resolution #111, established in November 1992, which directs the District on the investment of District funds. While the District does maintain all of the accounts outlined in the policy, they are not maintaining appropriate balances in the accounts. The District maintained a balance in their operational depository account at June 30, 2010, that was higher than one month's average expenditures as defined in the policy. In addition, there was no control in place to review that the appropriate funds were maintained in the Santa Barbara County and Local Agency Investment Fund as outlined in the policy. When this issue was brought to the attention of management in the previous year, the operational account balance was reduced to be more in-line with the policy, but no other changes were made or reviews performed.

Recommendation: We recommend that cash and investment accounts be reviewed on a monthly basis to ensure the District is complying with their stated investment policy and that appropriate transfers be made to comply with the policy. We also recommend that the board review the investment policy annual and periodically make necessary changes to the policy to ensure that it is still providing the intended results of safeguarding the cash and investments of the District.

Finding 10.03 – Restricted Reserves (Significant Deficiency)

The Board passed Board of Directors Resolution #102 in November 1991, titled “Depreciation, Restricted Reserves, Allocation of Interest Income” that details, among other things, the reserves that should be set up by the District on a regular basis to ensure there will be proper cash assets available to replace systems as required. These reserves include: replacement reserves, established at least quarterly; development reserves, established when connection fees are received from developers; and emergency reserves, established annually. The policy also describes how interest on these funds should be allocated.

At June 30, 2010, there were some investment funds set aside in Board restricted accounts, however, management has not been reviewing these reserves in accordance with the policy. Management was made aware of this issue in the previous year and a decision was made to prioritize the property and equipment physical observation before assessing the needs of the restricted reserves, believing that they needed to have a proper accounting of their assets before establishing the reserves.

Recommendation: We recommend that the Board review the existing reserve requirements and determine the appropriate level of required reserves, setting these aside in restricted accounts. We also recommend that they establish a policy for reviewing and setting these reserves and follow it going forward. The policy should include a methodology for establishing the reserves, the required frequency of review, and an annual evaluation, documented in the Board of Director minutes, of existing reserves.

Supplemental Information

**Mission Hills Community Services District
Schedule of Directors
June 30, 2010**

G. Bruce Nix	President
Cathy Schlottmann	Vice President
Susan Warnstrom	Finance Officer
James Mac Kenzie	Alternate Finance Officer
Kenneth Hyman	Director

Mission Hills Community Services District
Combining Statement of Net Assets (Deficit)
June 30, 2010

	<u>General Fund</u>	<u>Water Fund</u>	<u>Wastewater Fund</u>	<u>Street Sweeping Fund</u>	<u>Total</u>
Assets					
Current assets:					
Cash and cash equivalents	\$ 744,606	\$ 2,235,507	\$ 1,799,574	\$ 3,558	\$ 4,783,245
Services receivable, net of allowance		8,739	14,259	314	23,312
Interest receivable	1,324	3,150	3,123		7,597
Prepays and deposits	19,868	3,427	1,670		24,965
Total current assets	<u>765,798</u>	<u>2,250,823</u>	<u>1,818,626</u>	<u>3,872</u>	<u>4,839,119</u>
Property and equipment, net of accumulated depreciation	<u>247,553</u>	<u>3,662,222</u>	<u>1,966,485</u>		<u>5,876,260</u>
Total assets	<u>1,013,351</u>	<u>5,913,045</u>	<u>3,785,111</u>	<u>3,872</u>	<u>10,715,379</u>
Liabilities					
Current liabilities:					
Accounts payable and accrued liabilities	7,787	11,367	4,236	1,062	24,452
Accrued payroll	2,162	829	320		3,311
Compensated absences - due within one year	18,586	7,625	1,352		27,563
Customer deposits	14,716	5,183			19,899
Total current liabilities	<u>43,251</u>	<u>25,004</u>	<u>5,908</u>	<u>1,062</u>	<u>75,225</u>
Long-term liabilities:					
Compensated absences - due in more than one year	<u>34,552</u>	<u>14,175</u>	<u>2,514</u>		<u>51,241</u>
Total liabilities	<u>77,803</u>	<u>39,179</u>	<u>8,422</u>	<u>1,062</u>	<u>126,466</u>
Net Assets					
Invested in capital assets	247,553	3,662,223	1,966,484		5,876,260
Unrestricted	<u>(679,425)</u>	<u>1,836,254</u>	<u>3,532,615</u>	<u>23,209</u>	<u>4,712,653</u>
Total net assets (deficit)	<u>\$ (431,872)</u>	<u>\$ 5,498,477</u>	<u>\$ 5,499,099</u>	<u>\$ 23,209</u>	<u>\$ 10,588,913</u>

Mission Hills Community Services District
Combining Statement of Revenues,
Expenses and Changes in Net Assets
Year Ended June 30, 2010

	General Fund	Water Fund	Wastewater Fund	Street Sweeping Fund	Total
Operating revenues:					
Service charges	\$	\$ 705,536	\$ 472,738	\$ 15,416	\$ 1,193,690
Late charges and other revenue	23,300				23,300
Total operating revenues	<u>23,300</u>	<u>705,536</u>	<u>472,738</u>	<u>15,416</u>	<u>1,216,990</u>
Operating expenses:					
Chemicals		15,518	11,056		26,574
Contractual services	16,945	16,686	1,667	12,974	48,272
Depreciation	30,661	191,062	65,239		286,962
Directors' fees	8,400				8,400
Engineering services	1,260	2,513	7,445		11,218
Government charges	2,320	19,680	3,880		25,880
Insurance	23,906				23,906
Memberships and dues	6,181	1,834	256		8,271
Miscellaneous expense	8,989				8,989
Office expense	33,136	1,194	945		35,275
Operating supplies	2,143	4,427	1,157		7,727
Professional services	49,544				49,544
Repairs and maintenance	1,640	36,776	27,245		65,661
Research and monitoring		6,232	4,134		10,366
Safety expense	48	1,344	1,444		2,836
Salaries, benefits and payroll taxes	385,775	133,127	131,178		650,080
Travel and meetings	9,151	1,842	628		11,621
Utilities	7,872	78,388	40,971		127,231
Vehicle expense	1,108	7,355	3,733		12,196
Total operating expenses	<u>589,079</u>	<u>517,978</u>	<u>300,978</u>	<u>12,974</u>	<u>1,421,009</u>
Operating income (loss)	<u>(565,779)</u>	<u>187,558</u>	<u>171,760</u>	<u>2,442</u>	<u>(204,019)</u>
Nonoperating revenues:					
Unrealized loss on investments	(4,571)				(4,571)
Interest income	27,115	3,079	8,515		38,709
Gain (loss) on disposal of property and equipment	551		(14,715)		(14,164)
Total nonoperating revenues	<u>23,095</u>	<u>3,079</u>	<u>(6,200)</u>		<u>19,974</u>
Change in net assets	<u>(542,684)</u>	<u>190,637</u>	<u>165,560</u>	<u>2,442</u>	<u>(184,045)</u>
Net assets at beginning of year, as previously stated	151,273	5,316,595	5,235,469	20,767	10,724,104
Prior year restatement	(40,461)	(8,755)	98,070		48,854
Net assets at beginning of year, restated	<u>110,812</u>	<u>5,307,840</u>	<u>5,333,539</u>	<u>20,767</u>	<u>10,772,958</u>
Net assets (deficit) at end of year	<u>\$ (431,872)</u>	<u>\$ 5,498,477</u>	<u>\$ 5,499,099</u>	<u>\$ 23,209</u>	<u>\$ 10,588,913</u>

Mission Hills Community Services District
Combining Statement of Cash Flows
Year Ended June 30, 2010

	<u>General Fund</u>	<u>Water Fund</u>	<u>Wastewater Fund</u>	<u>Street Sweeping Fund</u>	<u>Total</u>
Cash flows from operating activities:					
Cash received from customers	\$ 23,666	\$ 704,592	\$ 462,243	\$ 15,210	\$ 1,205,711
Cash payments to suppliers for goods and services	(181,771)	(197,495)	(104,761)	(13,089)	(497,116)
Cash payments to employees for services	(387,345)	(122,855)	(154,864)		(665,064)
Net cash provided by (used in) operating activities	<u>(545,450)</u>	<u>384,242</u>	<u>202,618</u>	<u>2,121</u>	<u>43,531</u>
Cash flows from capital and related financing activities:					
Purchases of property and equipment	(41,298)	(296,952)			(338,250)
Proceeds from sale of property and equipment	4,000				4,000
Net cash used in capital and related financing activities	<u>(37,298)</u>	<u>(296,952)</u>			<u>(334,250)</u>
Cash flows from investing activities:					
Unrealized gain on investments	(4,571)				(4,571)
Interest on cash and cash equivalents	30,004	8,406	11,991	39	50,440
Net cash provided by investing activities	<u>25,433</u>	<u>8,406</u>	<u>11,991</u>	<u>39</u>	<u>45,869</u>
Net increase (decrease) in cash	(557,315)	95,696	214,609	2,160	(244,850)
Cash and cash equivalents - beginning of year	<u>810,727</u>	<u>2,139,306</u>	<u>2,074,504</u>	<u>3,558</u>	<u>5,028,095</u>
Cash and cash equivalents - end of year	<u>\$ 253,412</u>	<u>\$ 2,235,002</u>	<u>\$ 2,289,113</u>	<u>\$ 5,718</u>	<u>\$ 4,783,245</u>
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities:					
Operating income (loss)	\$ (565,779)	\$ 187,558	\$ 171,760	\$ 2,442	\$ (204,019)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:					
Depreciation	30,661	191,062	65,239		286,962
Changes in operating assets and liabilities:					-
Accounts receivable		(1,856)	(10,495)	(206)	(12,557)
Prepays and deposits	(484)	(1,177)	(276)		(1,937)
Accounts payable and accrued liabilities	(8,644)	(2,529)	76	(115)	(11,212)
Accrued payroll	(5,726)	(1,878)	(2,967)		(10,571)
Compensated absences	4,156	12,150	(20,719)		(4,413)
Customer deposits	366	912			1,278
Total adjustments	<u>20,329</u>	<u>196,684</u>	<u>30,858</u>	<u>(321)</u>	<u>247,550</u>
Net cash provided by (used in) operating activities	<u>\$ (545,450)</u>	<u>\$ 384,242</u>	<u>\$ 202,618</u>	<u>\$ 2,121</u>	<u>\$ 43,531</u>