

**Mission Hills Community Services District**

**Financial Statements**

**Year Ended June 30, 2016**

**Mission Hills Community Services District  
Financial Statements  
Year Ended June 30, 2016**

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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, 2016, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

### Management's 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.

**SAN LUIS OBISPO**

1150 Palm Street  
San Luis Obispo, CA 93401  
p 805 544 1441  
f 805 544 4351

**PASO ROBLES**

102 South Vine Street, Ste. A  
Paso Robles, CA 93446  
p 805 237 3995  
f 805 239 9332

**SANTA MARIA**

2222 South Broadway, Ste. A  
Santa Maria, CA 93454  
p 805 922 4010  
f 805 922 4286

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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.

**Opinion**

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, 2016, 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 is presented for purposes of additional analysis and is 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.

**Other Reporting Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, we have also issued our report dated October 14, 2016, 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

**Board of Directors**

**Mission Hills Community Services District**

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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 black 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 14, 2016

**Mission Hills Community Services District**  
**Management's Discussion and Analysis**  
**For the Fiscal Year Ended June 30, 2016**

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, 2016. 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 present information which shows how the District's 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 measure the success of the District's operations during the year and determine whether the District has recovered its costs through user fees and other 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

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Management's Discussion and Analysis  
For the Fiscal Year Ended June 30, 2016  
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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 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**

- Total assets were \$9,368,341 on June 30, 2016.
- Operating revenue was \$1,448,931, which consisted of Water Charges, Wastewater Charges, Street Sweeping Charges, Service Charges and Connection Fees.
- Total Expenses were \$1,773,680, which consisted primarily of Salaries, Benefits, Depreciation, Insurance, Office Expenses, Operating Expenses, Professional Services, Travel, Utilities, Chemicals and Repairs and Maintenance.

**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 \$9,173,856 as of June 30, 2016.

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 MHCS D; consequently, these assets are not available for future spending.

The next largest portion of net position is reserved for future spending. This portion includes cash and investments.

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Management's Discussion and Analysis  
For the Fiscal Year Ended June 30, 2016  
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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, 2016**

|                            | <u>2016</u>         | <u>2015</u>         | <u>% Change</u> |
|----------------------------|---------------------|---------------------|-----------------|
| <b>Assets:</b>             |                     |                     |                 |
| Current assets             | \$ 3,554,665        | \$ 4,235,712        | -16.1%          |
| Capital assets             | 5,813,676           | 5,375,200           | 8.2%            |
| <b>Total assets</b>        | <u>9,368,341</u>    | <u>9,610,912</u>    | -2.5%           |
| <b>Liabilities:</b>        |                     |                     |                 |
| Current liabilities        | 113,053             | 122,930             | -8.0%           |
| Long-term liabilities      | 81,432              | 64,580              | 26.1%           |
| <b>Total liabilities</b>   | <u>194,485</u>      | <u>187,510</u>      | 3.7%            |
| <b>Net Position:</b>       |                     |                     |                 |
| Invested in capital assets | 5,813,676           | 5,375,200           | 8.2%            |
| Unrestricted               | 3,360,180           | 4,048,202           | -17.0%          |
| <b>Total net position</b>  | <u>\$ 9,173,856</u> | <u>\$ 9,423,402</u> | -2.6%           |

The following are significant current fiscal year transactions that have an impact on the Statement of Net Position:

- Current assets decreased primarily due to market losses on investments and capital expenditures.
- Regular straight-line depreciation for the fiscal year ended June 30, 2016 decreased capital assets by \$280,659 offset by capital asset additions of \$720,406.
- Current liabilities have decreased primarily due to a \$17,837 decrease in accrued payroll.
- Long-term liabilities have increased \$16,852 due to an increase in compensated absences.



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Management's Discussion and Analysis  
For the Fiscal Year Ended June 30, 2016  
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**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  
June 30, 2016**

|                                 | <u>2016</u>         | <u>2015</u>         | <u>% Change</u> |
|---------------------------------|---------------------|---------------------|-----------------|
| Operating revenues              | \$ 1,448,931        | \$ 1,488,776        | -2.7%           |
| Nonoperating revenues           | 75,203              | 42,374              | 77.5%           |
| <b>Total revenues</b>           | <b>1,524,134</b>    | <b>1,531,150</b>    | <b>-0.5%</b>    |
| Depreciation expense            | 280,659             | 291,708             | -3.8%           |
| Other operating expenses        | 1,493,021           | 1,391,405           | 7.3%            |
| <b>Total operating expenses</b> | <b>1,773,680</b>    | <b>1,683,113</b>    | <b>5.4%</b>     |
| Change in net position          | (249,546)           | (151,963)           | 64.2%           |
| Beginning net position          | 9,423,402           | 9,575,365           | -1.6%           |
| <b>Ending net position</b>      | <b>\$ 9,173,856</b> | <b>\$ 9,423,402</b> | <b>-2.6%</b>    |

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 \$65,906 and Wastewater revenues were short projections by \$7,243.
- Total operating expenses were \$90,567 higher than last fiscal year, and \$159,668 higher than projected due primarily to increased repair and maintenance costs.

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Management's Discussion and Analysis  
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**Economic Outlook**

Currently the District is facing increased costs while the customer base remains constant. MHCS D is land locked and unable to experience any large growth in customer base, although Burton Ranch Homes is tentatively scheduled to begin construction in late 2017. The general economic trend has been in a negative direction due to state mandated water conservation and customer concerns over water use which has caused the income of the District to decrease. Meanwhile, the costs to provide services have increased. This trend of rising costs and decreasing revenues has caused the District to perform a Proposition 218 Engineering and Financial study as required by statute. The results of this study were utilized as a basis for an increase in the water and wastewater rates which was implemented in September 2016.

The major economic events of this fiscal year were the completion of the Sewer Trunk Line Project and replacement of a service truck. The upgrading of the SCADA System has continued this year, and should yield labor saving results. The District was able to obtain a donated video camera system from the City of Lompoc, which will allow the District to perform video inspections of our piping systems, reducing the cost to inspect aging sewer line. The District has experienced unusually high repair and maintenance costs due to the aging of the infrastructure and unanticipated equipment failures. The utilities account has abnormal expenditure due to the long period of time the Natural Gas powered Well 6 was under repair.

Continued regulator action (Notice of Violation) from the California Regional Water Quality Control Board concerning the Waste Water Treatment Plant 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.

MHCS D has continued to upgrade its infrastructure by replacing the water meters. The old meters currently in operation at MHCS D are in excess of 16 years old, while the industry standard for meter life is 10 years. A replacement program was continued this fiscal year to replace the remaining the meters with Automatic Meter Reading type meters. The District has completed 82% 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. The District has completed the following additional projects: replaced the Murphy Panel controlling the function of Well 6 engine and replaced the flow meters throughout the plant. The District continued to utilize the services of H & S Environmental to improve the operations and ensure compliance with the

**Mission Hills Community Services District  
Management's Discussion and Analysis  
For the Fiscal Year Ended June 30, 2016  
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requirements of the Notice of Violation received in December 2010. Mr. Richard Hoffman has completed 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 continues its successful programs of vehicle repair with the County of Santa Barbara as well as the environmentally friendly goat herd.

**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, 2016**

**Assets**

**Current assets:**

|                                       |    |           |
|---------------------------------------|----|-----------|
| Cash and cash equivalents             | \$ | 512,430   |
| Accounts receivable, net of allowance |    | 30,462    |
| Investments                           |    | 2,975,313 |
| Prepays and deposits                  |    | 36,460    |
| Total current assets                  |    | 3,554,665 |

|                                                                |  |                  |
|----------------------------------------------------------------|--|------------------|
| <b>Property and equipment, net of accumulated depreciation</b> |  | <b>5,813,676</b> |
|----------------------------------------------------------------|--|------------------|

|                     |  |                  |
|---------------------|--|------------------|
| <b>Total assets</b> |  | <b>9,368,341</b> |
|---------------------|--|------------------|

**Liabilities**

**Current liabilities:**

|                                          |  |         |
|------------------------------------------|--|---------|
| Accounts payable and accrued liabilities |  | 46,829  |
| Accrued payroll                          |  | 8,955   |
| Compensated absences, current portion    |  | 39,617  |
| Customer deposits and advances           |  | 17,652  |
| Total current liabilities                |  | 113,053 |

**Long-term liabilities:**

|                                              |  |        |
|----------------------------------------------|--|--------|
| Compensated absences, net of current portion |  | 81,432 |
|----------------------------------------------|--|--------|

|                          |  |                |
|--------------------------|--|----------------|
| <b>Total liabilities</b> |  | <b>194,485</b> |
|--------------------------|--|----------------|

**Net Position**

|                                  |  |           |
|----------------------------------|--|-----------|
| Net investment in capital assets |  | 5,813,676 |
| Unrestricted                     |  | 3,360,180 |

|                           |  |                     |
|---------------------------|--|---------------------|
| <b>Total net position</b> |  | <b>\$ 9,173,856</b> |
|---------------------------|--|---------------------|

*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, 2016**

|                                                |                            |
|------------------------------------------------|----------------------------|
| <b>Operating revenues:</b>                     |                            |
| Service charges                                | \$ 1,395,220               |
| Late charges and other revenue                 | 53,711                     |
| Total operating revenues                       | <u>1,448,931</u>           |
| <br><b>Operating expenses:</b>                 |                            |
| Chemicals                                      | 62,307                     |
| Contractual services                           | 63,527                     |
| Depreciation                                   | 280,659                    |
| Directors' fees                                | 12,300                     |
| Engineering services                           | 49,637                     |
| Government charges                             | 23,476                     |
| Insurance                                      | 51,113                     |
| Memberships and dues                           | 10,012                     |
| Office expense                                 | 16,373                     |
| Operating supplies                             | 10,881                     |
| Printing and publications                      | 5,781                      |
| Professional services                          | 75,236                     |
| Repairs and maintenance                        | 160,682                    |
| Research and monitoring                        | 22,584                     |
| Safety expense                                 | 6,665                      |
| Salaries, benefits and payroll taxes           | 707,280                    |
| Travel and meetings                            | 16,524                     |
| Utilities                                      | 174,657                    |
| Vehicle expense                                | 23,986                     |
| Total operating expenses                       | <u>1,773,680</u>           |
| Operating loss                                 | <u>(324,749)</u>           |
| <br><b>Nonoperating revenues and expenses:</b> |                            |
| Investment loss, net                           | (65,512)                   |
| Interest income                                | 138,085                    |
| Gain on disposition of property and equipment  | 2,630                      |
| Total nonoperating revenues and expenses       | <u>75,203</u>              |
| Decrease in net position                       | (249,546)                  |
| <b>Net position - beginning of year</b>        | <u>9,423,402</u>           |
| <b>Net position - end of year</b>              | <u><u>\$ 9,173,856</u></u> |

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

**Mission Hills Community Services District**  
**Statement of Cash Flows**  
**Year Ended June 30, 2016**

|                                                                                   |              |                           |
|-----------------------------------------------------------------------------------|--------------|---------------------------|
| <b>Cash flows from operating activities:</b>                                      |              |                           |
| Cash received from customers                                                      | \$ 1,442,235 |                           |
| Cash payments to suppliers for goods and services                                 | (773,561)    |                           |
| Cash payments to employees for services                                           | (711,011)    |                           |
| Net cash used in operating activities                                             |              | \$ (42,337)               |
| <b>Cash flows from capital and related financing activities:</b>                  |              |                           |
| Purchases of property and equipment                                               | (720,405)    |                           |
| Proceeds from sale of property and equipment                                      | 3,900        |                           |
| Net cash used in capital and financing activities                                 |              | (716,505)                 |
| <b>Cash flows from investing activities:</b>                                      |              |                           |
| Proceeds from sale of investments                                                 | 461,327      |                           |
| Investment income                                                                 | 138,085      |                           |
| Net cash provided by investing activities                                         |              | 599,412                   |
| Net decrease in cash                                                              |              | (159,430)                 |
| <b>Cash and cash equivalents - beginning of year</b>                              |              | <u>671,860</u>            |
| <b>Cash and cash equivalents - end of year</b>                                    |              | <u><u>\$ 512,430</u></u>  |
| <b>Reconciliation of operating loss to net cash used in operating activities:</b> |              |                           |
| Operating loss                                                                    |              | (324,749)                 |
| Adjustments to reconcile operating loss to net cash used in operating activities: |              |                           |
| Depreciation                                                                      | 280,659      |                           |
| Changes in operating assets and liabilities:                                      |              |                           |
| Accounts receivable, net of allowance                                             | (1,156)      |                           |
| Prepays and deposits                                                              | (4,066)      |                           |
| Accounts payable and accrued liabilities                                          | 16,246       |                           |
| Accrued payroll                                                                   | (17,837)     |                           |
| Compensated absences                                                              | 14,106       |                           |
| Customer deposits and advances                                                    | (5,540)      |                           |
| Total adjustments                                                                 |              | <u>282,412</u>            |
| Net cash used in operating activities                                             |              | <u><u>\$ (42,337)</u></u> |
| <b>Supplemental disclosures of cash flow information:</b>                         |              |                           |
| Noncash transactions:                                                             |              |                           |
| Decrease in fair value of investments                                             |              | \$ 65,512                 |

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

**Mission Hills Community Services District**  
**Notes to Financial Statements**  
**June 30, 2016**

**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, 2016**

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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, 2016, the allowance for uncollectible services receivable was \$42,596.

**Prepays and Deposits**

Payments made to vendors for services that will benefit any period beyond June 30, 2016 are recorded as prepaid expenses or deposits.

**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, 2016**

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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, 2016, have been evaluated through October 14, 2016, 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**

Cash and cash equivalents at June 30, 2016, consisted of the following:

|                                             |                          |
|---------------------------------------------|--------------------------|
| Cash in bank                                | \$ 511,410               |
| Cash in Local Agency Investment Fund (LAIF) | <u>1,020</u>             |
|                                             | <u><u>\$ 512,430</u></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, 2016**

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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.

**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: Investments**

At June 30, 2016, investments comprised the following:

|                         |                     |
|-------------------------|---------------------|
| Investments             |                     |
| Fixed income securities | <u>\$ 2,975,313</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.

**Mission Hills Community Services District**

**Notes to Financial Statements**

**June 30, 2016**

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**Note 4: Investments (Continued)**

*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, 2016, 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.

*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.

*Investment Fair Values:*

The District categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The District's investments are all classified in Level 1 of the fair value hierarchy, which values investments at the unadjusted quoted prices for identical assets in active markets that the District has the ability to access.

**Mission Hills Community Services District**

**Notes to Financial Statements**

**June 30, 2016**

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**Note 5: Property and Equipment**

At June 30, 2016, property and equipment consisted of the following:

|                               | <u>Balance</u><br><u>June 30, 2015</u> | <u>Increases</u>  | <u>Decreases</u>   | <u>Balance</u><br><u>June 30, 2016</u> |
|-------------------------------|----------------------------------------|-------------------|--------------------|----------------------------------------|
| Land                          | \$ 431,163                             | \$                | \$                 | \$ 431,163                             |
| Plant and equipment           | 9,696,630                              | 800,428           | (66,532)           | 10,430,526                             |
| Construction in progress      | 86,446                                 | 6,423             | (86,446)           | 6,423                                  |
|                               | 10,214,239                             | 806,851           | (152,978)          | 10,868,112                             |
| Less accumulated depreciation | (4,839,039)                            | (280,659)         | 65,262             | (5,054,436)                            |
| Property and equipment, net   | <u>\$ 5,375,200</u>                    | <u>\$ 526,192</u> | <u>\$ (87,716)</u> | <u>\$ 5,813,676</u>                    |

**Note 6: Long-Term Liabilities - Compensated Absences**

At June 30, 2016, long-term liabilities consisted of the following:

|                      | <u>Balance</u><br><u>June 30, 2015</u> | <u>Additions</u> | <u>Reductions</u>  | <u>Balance</u><br><u>June 30, 2016</u> | <u>Current</u><br><u>Portion</u> |
|----------------------|----------------------------------------|------------------|--------------------|----------------------------------------|----------------------------------|
| Compensated absences | <u>\$ 106,943</u>                      | <u>\$ 49,130</u> | <u>\$ (35,024)</u> | <u>\$ 121,049</u>                      | <u>\$ 39,617</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, 2016, were as follows:

|                         |                     |
|-------------------------|---------------------|
| Water charges           | \$ 863,849          |
| Wastewater charges      | 513,256             |
| Street sweeping charges | <u>18,115</u>       |
| Total                   | <u>\$ 1,395,220</u> |

**Mission Hills Community Services District**

**Notes to Financial Statements**

**June 30, 2016**

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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. Total District contributions were \$36,696 for the year ended June 30, 2016. Contributions by plan members were \$56,217 for the year ended June 30, 2016.

**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, 2016**

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**Note 9: Risk Management (Continued)**

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

|                              |    |                      |
|------------------------------|----|----------------------|
| Total assets                 | \$ | 195,400,750          |
| Total liabilities            |    | <u>114,466,932</u>   |
| Net assets                   | \$ | <u>80,933,818</u>    |
| <br>                         |    |                      |
| Total operating revenues     | \$ | 157,661,735          |
| Total nonoperating revenues  |    | 2,738,962            |
| Total operating expenses     |    | <u>(164,195,428)</u> |
| <br>                         |    |                      |
| Net decrease in net position | \$ | <u>(3,794,731)</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 received correspondence from the RWQCB dated September 2, 2016, Update on Violations from 2015 and 2016-Nitrogen, Chloride, Total Dissolved Solids, Order No. 97-035. The District and the RWQCB are in constant communication in order to correct the deficiencies noted. A technical report is due in November 2016 to support correction of the Notice of Violation. The RWQCB has not indicated any change to the possibility of imposing monetary fines. 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, 2016, 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 14, 2016.

**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 at 16.01 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



Glenn Burdette Attest Corporation  
San Luis Obispo, California

October 14, 2016



**Mission Hills Community Services District**  
**Schedule of Findings and Recommendations**  
**Year Ended June 30, 2016**

**Finding 16.01: 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 General Manager and District Accountant.

*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, 2016**

|                  |                           |
|------------------|---------------------------|
| Danny Hayes      | President                 |
| Tim Naughton     | Vice President            |
| Walt Fasold      | Finance Officer           |
| Bruce Nix        | Alternate Finance Officer |
| James Mac Kenzie | Director                  |

*See independent auditors' report.*