

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

AUDITED FINANCIAL STATEMENTS

June 30, 2011

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

AUDITED FINANCIAL STATEMENTS

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Rio Linda/Elverta Community Water District
Rio Linda, California

We have audited the accompanying basic financial statements of the Rio Linda/Elverta Community Water District (the District) as of June 30, 2011 and 2010 and for the years then ended, as listed in the table of contents. 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 audits.

Except as discussed in the following paragraphs, 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 basic 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.

The District has not adopted Governmental Accounting Standards Board Statement (GASBS) No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, and accordingly has not recorded a liability for post-employment benefits. Accounting principles generally accepted in the United States of America require the liability to be recorded as of June 30, 2010, which would decrease net assets and increase expenses of the District. The amount by which this departure would affect the net assets and expenses of the District is not readily determinable. Disclosures required by generally accepted accounting principles related to the post-employment benefits and related liability has also been omitted.

In addition, the District did not perform a physical inventory at June 30, 2011 and 2010 and, accordingly, has not adjusted the inventory balance since June 30, 2009. We were unable to satisfy ourselves about the inventory quantities by means of other audit procedures.

The District has disclosed that there have been allegations of fraud and that investigations by outside organizations are being performed. The outcome of these investigations is not known.

The accompanying financial statements have been prepared assuming that the District will continue as a going concern. As discussed in Note J to the financial statements, the District has suffered recurring losses from operations, which raise substantial doubt about its ability to continue as a going concern. Management's plans regarding those matters also are described in Note J. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Because of the significance of the matters described in the preceding paragraphs, we are unable to express, and we do not express, an opinion on the financial statements referred to in the first paragraph.

In accordance with *Government Auditing Standards*, we have also issued our report on our consideration of the Agency's internal control over financial reporting and our tests of its compliance with certain provisions of laws,

To the Board of Directors
Rio Linda/Elverta Community Water District

regulations, contracts and grants. 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 the 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 *Governmental Auditing Standards*, and should be read in conjunction with this report in considering the results of our audit.

The District has not presented Management's Discussion and Analysis that accounting principles generally accepted in the United States has determined is necessary to supplement, although not required to be part of the basic financial statements.

Richardson & Company

June 12, 2012

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

BALANCE SHEETS

June 30, 2011 and 2010

	2011	2010
ASSETS		
CURRENT ASSETS		
Cash and investments	\$ 280,622	\$ 102,720
Accounts receivable	329,629	287,572
Accrued interest receivable	18	309
Inventory	45,894	45,894
Prepaid expenses	18,708	27,708
TOTAL CURRENT ASSETS	674,871	464,203
RESTRICTED ASSETS		
Restricted cash and investments	386,433	251,264
CAPITAL ASSETS, NET		
	8,309,700	8,223,760
OTHER NONCURRENT ASSETS		
Deferred bond issuance costs	173,557	181,641
TOTAL ASSETS	\$ 9,544,561	\$ 9,120,868
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable	\$ 653,042	\$ 194,130
Accrued salaries and benefits	21,055	36,353
Accrued interest payable	24,719	25,169
Deposits payable	25,922	30,489
Deferred revenue	22,032	22,032
Current portion of compensated absences	15,234	20,182
Current portion of bonds payable	95,000	90,000
TOTAL CURRENT LIABILITIES	857,004	418,355
LONG-TERM LIABILITIES		
Bonds payable	2,698,100	2,754,334
TOTAL LONG-TERM LIABILITIES	2,698,100	2,754,334
TOTAL LIABILITIES	3,555,104	3,172,689
NET ASSETS		
Invested in capital assets, net of related debt	5,516,600	5,357,179
Restricted for debt service	243,329	242,485
Restricted for capital improvements	143,104	8,779
Unrestricted	86,424	339,736
TOTAL NET ASSETS	5,989,457	5,948,179
TOTAL LIABILITIES AND NET ASSETS	\$ 9,544,561	\$ 9,120,868

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

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

For the Years Ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
OPERATING REVENUES		
Water sales	\$ 1,546,497	\$ 1,420,153
Account service charges	136,453	123,907
Other water service fees	2,955	2,180
Other	10,733	10,097
TOTAL OPERATING REVENUES	<u>1,696,638</u>	<u>1,556,337</u>
OPERATING EXPENSES		
Personnel services	698,360	688,774
Professional services	478,968	174,163
Field operations:		
Transmission and distribution	53,781	100,181
Pumping	190,191	176,198
Transportation	16,450	17,695
Treatment	20,198	15,611
Other	168,342	84,655
Conservation	1,896	3,505
Administration	217,313	184,078
Depreciation and amortization	321,697	307,009
TOTAL OPERATING EXPENSES	<u>2,167,196</u>	<u>1,751,869</u>
NET (LOSS) INCOME FROM OPERATIONS	(470,558)	(195,532)
NON-OPERATING (EXPENSES) REVENUES		
Surcharge	462,681	364,204
Interest income	575	1,469
Miscellaneous income	3,319	8,032
Property tax	63,296	63,348
Rental income	69,464	58,859
Lawsuit settlement	102,057	
Interest expense	(186,898)	(216,223)
Other non-operating expenses	(2,658)	(2,066)
TOTAL NON-OPERATING REVENUES (EXPENSES)	<u>511,836</u>	<u>277,623</u>
CHANGE IN NET ASSETS	41,278	82,091
Net assets, beginning of year	<u>5,948,179</u>	<u>5,866,088</u>
NET ASSETS AT END OF YEAR	<u>\$ 5,989,457</u>	<u>\$ 5,948,179</u>

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

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

STATEMENTS OF CASH FLOWS

For the Years Ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash receipts from customers	\$ 1,663,958	\$ 1,557,225
Cash paid to suppliers for goods and services	(679,227)	(686,537)
Cash paid to employees for services	(718,606)	(680,089)
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>266,125</u>	<u>190,599</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Miscellaneous income	3,319	8,032
Property taxes received	63,296	63,348
Rental income received	69,464	58,859
Non-operating expense paid	(2,658)	(2,066)
Settlements received	102,057	-
NET CASH PROVIDED BY NONCAPITAL FINANCING ACTIVITIES	<u>235,478</u>	<u>128,173</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Surcharge received	448,737	334,025
Payments on long-term debt	(90,000)	(85,000)
Purchase and construction of property	(399,553)	(440,334)
Interest paid on long-term debt	(148,582)	(152,288)
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	<u>(189,398)</u>	<u>(343,597)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment income received	866	2,139
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>866</u>	<u>2,139</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	313,071	(22,686)
Cash and cash equivalents at beginning of year	<u>353,984</u>	<u>376,670</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 667,055</u>	<u>\$ 353,984</u>
Cash and cash equivalents consist of the following:		
Unrestricted	\$ 280,622	\$ 102,720
Restricted	386,433	251,264
	<u>\$ 667,055</u>	<u>\$ 353,984</u>

(Continued)

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

STATEMENTS OF CASH FLOWS (Continued)

For the Years Ended June 30, 2011 and 2010

	<u>2011</u>	<u>2010</u>
RECONCILIATION OF NET INCOME FROM OPERATIONS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net income from operations	\$ (470,558)	\$ (195,532)
Adjustments to reconcile net income from operations to net cash provided by operating activities:		
Depreciation and amortization	321,697	307,009
Changes in assets and liabilities:		
Accounts receivable	(28,113)	4,278
Prepaid expenses and other assets	9,000	(5,908)
Accounts payable	458,912	75,457
Accrued salaries and benefits	(15,298)	36,090
Deposits payable	(4,567)	(3,390)
Compensated absences	(4,948)	(27,405)
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 266,125</u>	<u>\$ 190,599</u>

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

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

NOTES TO THE BASIC FINANCIAL STATEMENTS

June 30, 2011

NOTE A – REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of the Rio Linda/Elverta Community Water District (District) have been prepared in conformity with generally accepted accounting principles as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. As allowed by the GASB, the District has elected not to apply to its proprietary activities Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee of Accounting Procedures issued after November 30, 1989. The more significant of the District's accounting policies are described below.

Reporting Entity: The District was formed on November 9, 1948 and provided water and sewer services. Sewer services were transferred to Sacramento County in 1976. The District no longer provides sewer service. The District currently provides domestic water service and fire flows to approximately 4,610 metered accounts, including procurement, quality, and distribution. The District is governed by a Board of Directors consisting of five directors elected by residents of the District.

Basis of Presentation – Fund Accounting: The District's resources are allocated to and accounted for in these basic financial statements as an enterprise fund type of the proprietary fund group. The enterprise fund is used to account for operations that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges, or where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other policies. Net assets for the enterprise fund represent the amount available for future operations.

Basis of Accounting: The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. The enterprise fund type is accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of this fund are included on the balance sheet. Net assets are segregated into amounts invested in capital assets, net of related debt, amounts restricted and amounts unrestricted. Enterprise fund type operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets.

The District uses the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. Earned but unbilled water services are accrued as revenue.

Operating revenues and expenses consist of those revenues and expenses that result from the ongoing principle operations of the District. Operating revenues consist primarily of charges for services. Non-operating revenues and expense consist of those revenues and expenses that are related to financing and investing types of activities and result from nonexchange transactions or ancillary activities.

When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, then unrestricted resources as they are needed.

Use of Estimates: The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents: For purposes of the statement of cash flows, the District considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents. Cash and cash equivalents held include bank deposits, Local Agency Investment Fund (LAIF), an investment pool managed by the State of California, and money market mutual funds.

Restricted Assets: Certain proceeds of the District's long-term debt are classified as restricted investments on the balance sheet because their use is limited by applicable debt covenants and ordinances. In addition, proceeds from the surcharge levied on customer accounts are restricted for capital improvements.

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT
NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

June 30, 2011

NOTE A – REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investments: Investments are stated at their fair value, which represents the quoted or stated market value. Investments that are not traded on a market, such as investments in external pools, are valued based on the stated fair value as represented by the external pool. The District does not have a Board approved Investment Policy.

Inventory: Inventory consists primarily of materials used in the construction and maintenance of the water distribution facilities and is valued on a first-in, first-out basis.

Capital Assets: Capital assets are recorded at historical cost. Donated assets are valued at estimated fair value on the date received. Self-constructed assets are recorded based on the amount of direct labor, material, and certain overhead charged to the asset construction. Depreciation is calculated using the straight-line method over estimated useful lives of 8 to 60 years for transmission and distribution and 3 to 50 years for general plant assets. Depreciation expense in the amount of \$313,613 and \$298,925 was recorded for the years ended June 30, 2011 and 2010, respectively, and is included with depreciation and amortization expense.

Maintenance and repairs are charged to operations when incurred. It is the District's policy to capitalize all capital assets with an initial cost of more than \$1,500 and an estimated useful life in excess of two years. Costs of assets sold or retired (and the related amounts of accumulated depreciation) are eliminated from the balance sheet in the year of sale or retirement, and the resulting gain or loss is recognized in operations.

Accounts Receivable: The District issues water invoices bi-monthly based on meter readings. Delinquent water invoices may have a lien placed on the property. The District does not provide for an allowance for uncollectible accounts due to the lien process.

Bond Premiums and Deferred Bond Issuance Costs: Bond premiums, as well as issuance costs, are deferred and amortized over the lives of the bonds. Long-term liabilities are reported net of the applicable bond premiums. Bond issuance costs are reported as a component of Other Noncurrent Assets.

Deferred Revenues: Deferred revenue represents funds received for future service installation and is recognized as revenue when installations are performed.

Contributed Facilities: The District receives facilities (hydrant, pipes, valves, etc.) from developers resulting from developers preparing the sites to connect to the District. The District records these items as capital assets and depreciates them over their estimated useful life.

Property Taxes: Property tax in California is levied in accordance with Article XIII A of State Constitution at 1% of countywide assessed valuations. The property taxes are placed in a pool and are then allocated to the local governmental units based upon complex formulas. The County of Sacramento is responsible for collection of property tax, and the District recognizes property taxes when received from or collected by the County. Amounts levied but not collected at June 30 (delinquent property taxes) have not been reported since these amounts could not be readily determined.

Compensated Absences: The District has a policy whereby employees can accrue up to a maximum of 240 hours of vacation leave. All accrued vacation leave will be paid to the employee on termination of employment. Accumulated unpaid vacation leave is accrued when earned. The District does not accrue sick leave.

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT
 NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

June 30, 2011

NOTE B – CASH AND INVESTMENTS

Cash and investments as June 30, 2011 and 2010 are classified in the accompanying financial statements as follows:

	2011	2010
Cash and cash equivalents	\$ 280,622	\$ 102,720
Restricted cash and investments	386,433	251,264
Total cash and investments	\$ 667,055	\$ 353,984

Cash and investments as of June 30, 2011 and 2010 consisted of the following:

	2011	2010
Cash on hand	\$ 200	\$ 1,013
Deposits with financial institutions	408,126	95,107
Total cash	408,326	96,120
Investments in Local Agency Investment Fund (LAIF)	15,400	15,379
Held by bond trustee:		
Money market mutual fund	34,608	34,844
LAIF	208,721	207,641
Total investments	258,729	257,864
Total cash and investments	\$ 667,055	\$ 353,984

Investment policy: California statutes authorize districts to invest idle, surplus or reserve funds in a variety of credit instruments as provided for in the California Government Code, Section 53600, Chapter 4 - Financial Affairs. The table below identifies the investment types that are authorized for the District by the California Government Code that address interest rate risk, credit risk, and concentration of credit risk. This table does not address investments of debt proceeds held by the bond trustee that are governed by the provisions of debt agreements of the District, rather than the general provisions of the California Government Code or the District's investment policy. During the year ended June 30, 2011, the District's permissible investments included the following instruments:

Authorized Investment Type	Maximum Maturity	Maximum Percentage of Portfolio*	Maximum Investment in One Issuer
Local Agency Bonds	None	None	None
U.S. Treasury Obligations	None	None	None
U.S. Agency Securities	None	None	None
State of California obligations	None	None	None
Bankers Acceptances	180 days	40%	30%
Commercial Paper	270 days	40%	10%
Negotiable Certificates of Deposits	None	30%	None
Repurchase Agreements	92 days	None	None
Medium Term Corporate Notes	None	30%	None
Money Market Mutual Funds	N/A	20%	10%
Mortgage pass-through securities	5 years	20%	None
LAIF	N/A	None	None

*Excluding amounts held by the bond trustee that are not subject to California Government Code restrictions.

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT
 NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

June 30, 2011

NOTE B – CASH AND INVESTMENTS (Continued)

The District complied with the provisions of the California Government Code pertaining to the types of investments held, the institutions in which deposits were made and the security requirements. The District will continue to monitor compliance with applicable statutes pertaining to public deposits and investments.

Investments Authorized by Debt Agreements: Investments of debt proceeds held by the bond trustee are governed by provisions of the debt agreements, rather than the general provisions of the California Government Code or the District's investment policy. The Water Revenues Refunding Bond agreements contain certain provisions that address interest rate risk and credit risk, but not concentration of credit risk.

Interest rate risk: Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. One of the ways the District manages its exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations. All of the District's investments mature within 12 months.

Credit Risk: Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the minimum rating required by (where applicable) the California Government Code, the District's investment policy, or debt agreements, and the actual rating as of year-end for each investment type.

	Minimum Legal Rating	Total	Ratings as of Year End	
			AAA	Not Rated
LAIF	N/A	\$ 15,400		\$ 15,400
Held by bond trustee:				
Money market mutual fund	N/A	34,608	\$ 33,764	
LAIF	N/A	208,721		208,721
		<u>\$ 258,729</u>	<u>\$ 33,764</u>	<u>\$ 224,121</u>

Custodial credit risk: Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The California Government Code and the District's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits, other than the following provision for deposits: The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure public agency deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits.

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT
 NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

June 30, 2011

NOTE B – CASH AND INVESTMENTS (Continued)

At June 30, 2011, the carrying amount of the District's deposits were \$408,126 and the balances in financial institutions were \$405,389. Of the balance in financial institutions, the entire amount of \$405,389 was covered by federal depository insurance. As of June 30, 2011, District investments in the following investment types were held by the same broker-dealer (counterparty) that was used by the District to buy the securities:

Reported Investment Type	Amount
Money market mutual funds	\$ 34,608
LAIF	208,721

Investment in LAIF: LAIF is stated at amortized cost, which approximates fair value. The LAIF is a special fund of the California State Treasury through which local governments may pool investments. The total fair value amount invested by all public agencies in LAIF is \$66,489,270,508 managed by the State Treasurer. Of that amount, 5.01% is invested in structured notes and asset-back securities. No amounts were invested in derivative financial products. The Local Investment Advisory Board (Board) has oversight responsibility for LAIF. The Board consists of five members as designated by State Statute. The fair value of the District's investment in this pool is reported in the accompanying financial statements at amounts based upon the District's pro-rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis.

NOTE C – CAPITAL ASSETS

Capital asset activity for the years ended June 30, 2011 and 2010 are as follows:

	Balance July 1, 2010	Additions	Disposals	Adjustments	Balance June 30, 2011
Capital assets not being depreciated:					
Land	\$ 410,723				\$ 410,723
Construction in progress	631,313	\$ 387,769			1,019,082
Total capital assets, not being depreciated	1,042,036	387,769			1,429,805
Capital assets being depreciated:					
Transmission and distribution	11,273,400	11,784			11,285,184
General plant assets	792,013				792,013
Intangible assets	363,185				363,185
Total capital assets, being depreciated	12,428,598	11,784			12,440,382
Less accumulated depreciation for:					
Transmission and distribution	(4,387,197)	(271,823)			(4,659,020)
General plant assets	(693,772)	(29,266)			(723,038)
Intangible assets	(165,905)	(12,524)			(178,429)
Total accumulated depreciation	(5,246,874)	(313,613)			(5,560,487)
Total capital assets, being depreciated, net	7,181,724	(301,829)			6,879,895
Capital assets, net	\$ 8,223,760	\$ 85,940	\$ -	\$ -	\$ 8,309,700

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT
 NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

June 30, 2011

NOTE C – CAPITAL ASSETS (Continued)

	Balance July 1, 2009	Additions	Disposals	Adjustment	Balance June 30, 2010
Capital assets not being depreciated:					
Land	\$ 410,723				\$ 410,723
Construction in progress	200,975	\$ 430,338			631,313
Total capital assets, not being depreciated	611,698	430,338			1,042,036
Capital assets being depreciated:					
Transmission and distribution	11,273,400				11,273,400
General plan assets	782,017	9,996			792,013
Intangible assets	363,185				363,185
Total capital assets, being depreciated	12,418,602	9,996			12,428,598
Less accumulated depreciation for:					
Transmission and distribution	(4,117,026)	(270,171)			(4,387,197)
General plan assets	(681,894)	(11,878)			(693,772)
Intangible assets	(149,029)	(16,876)			(165,905)
Total accumulated depreciation	(4,947,949)	(298,925)			(5,246,874)
Total capital assets, being depreciated, net	7,470,653	(288,929)			7,181,724
Capital assets, net	<u>\$ 8,082,351</u>	<u>\$ 141,409</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 8,223,760</u>

NOTE D – LONG-TERM LIABILITIES

2003 Water Revenue Refunding Bonds: On January 22, 2003, the District issued \$3,970,000 of Water Revenue Refunding Bonds with interest ranging from 3.25% to 4.75%. These 2003 Bonds were issued to finance certain capital improvements to the District's water system. Annual principal payments, ranging from \$95,000 to \$235,000 are due on November 1 through November 1, 2032 and semi-annual interest payments, ranging from \$5,581 to \$74,156 are due on May 1 and November 1 through November 1, 2032.

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT
 NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

June 30, 2011

NOTE D – LONG-TERM LIABILITIES (Continued)

The activity of the District's long-term liabilities during the years ended June 30, 2011 and 2010 was as follows:

	Balance July 1, 2010	Additions	(Reductions)	Balance June 30, 2011	Due Within One Year
2003 Water Revenue Refunding Bonds	\$ 3,400,000		\$ (90,000)	\$ 3,310,000	\$ 95,000
Less: Deferred amount on refunding	(555,666)		38,766	(516,900)	
	<u>2,844,334</u>		<u>(51,234)</u>	<u>2,793,100</u>	<u>95,000</u>
Compensated absences	20,182		(4,948)	15,234	15,234
	<u>\$ 2,864,516</u>	<u>\$ -</u>	<u>\$ (56,182)</u>	<u>\$ 2,808,334</u>	<u>\$ 110,234</u>
	Balance July 1, 2009	Additions	(Reductions)	Balance June 30, 2010	Due Within One Year
2003 Water Revenue Bonds	\$ 3,485,000		\$ (85,000)	\$ 3,400,000	\$ 90,000
Less: Deferred amount on refunding	(594,432)		38,766	(555,666)	
	<u>2,890,568</u>		<u>(46,234)</u>	<u>2,844,334</u>	<u>90,000</u>
Compensated absences	47,587		(27,405)	20,182	20,182
	<u>\$ 2,938,155</u>	<u>\$ -</u>	<u>\$ (73,639)</u>	<u>\$ 2,864,516</u>	<u>\$ 110,182</u>

The advance refunding of the 1999 Certificates of Participation with the 2003 Water Revenue Refunding Bonds resulted in differences between the reacquisition price and the net carrying amount of the outstanding debt of \$854,898 at June 30, 2011 and 2010, net of accumulated amortization of \$337,998 and \$299,232, respectively. This deferred amount on refunding, reported in the accompanying financial statements as a deduction from long-term debt, is being charged to operations over the remaining life of the 2003 Water Revenue Bonds.

The annual requirements to amortize the outstanding debt as of June 30, 2011 are as follows:

For the Year Ended June 30:	2003 Water Revenue Refunding Bonds		
	Principal	Interest	Total
2012	\$ 95,000	\$ 146,769	\$ 241,769
2013	95,000	143,562	238,562
2014	100,000	140,087	240,087
2015	105,000	136,175	241,175
2016	110,000	131,875	241,875
2017-2021	605,000	588,206	1,193,206
2022-2026	765,000	334,044	1,099,044
2027-2031	975,000	229,781	1,204,781
2032-2034	460,000	22,087	482,087
	<u>\$ 3,310,000</u>	<u>\$ 1,872,586</u>	<u>\$ 5,182,586</u>

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT
 NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

June 30, 2011

NOTE D – LONG-TERM LIABILITIES (Continued)

Pledged Revenue: The District pledged future water system revenues, net of specified expenses, to repay the 2003 Water Revenue Refunding Bonds in the original amount of \$3,970,000. Proceeds of the Bonds funded the acquisition and construction of certain facilities, as indicated above. The Bonds are payable solely from water customer net revenues and are payable through November, 2032. Annual principal and interest payments on the Bonds are expected to require less than 80% of net revenues. Total principal and interest remaining to be paid on the Bonds was \$5,182,586 and \$5,523,250 at June 30, 2011 and 2010, respectively.

Total principal and interest paid on all debt payable from net revenues was \$239,663 and \$237,288 and the total water system net revenues were \$450,474 and \$716,442 for the years ended June 30, 2011 and 2010, respectively. At June 30, 2011 and 2010, the District's net revenues were 188% and 302% of debt service payments, respectively.

NOTE E – ARBITRAGE REBATE LIABILITY

Section 148(f) of the Internal Revenue Code requires issuers of tax-exempt state and local bonds to remit to the federal government amounts equal to (a) the excess of the actual amounts earned on all "Non-purpose Investments" allocable to "Gross Proceeds" of an issue of municipal obligations less the amount that would have been earned if the investments bore a rate equal to the amount that would have been earned if the investments bore a rate equal to the yield on the issue, plus (b) all income attributable to the excess. Issuers must make rebate payments at least once every five years and upon final retirement or redemption of the bonds. There was no arbitrage liability at June 30, 2011 and 2010.

NOTE F – NET ASSETS

Restrictions: Restricted net assets consist of constraints placed on net asset use through external requirements imposed by creditors (such as through debt covenants), grantors, contributors, or laws and regulations of other governments or constraints by law through constitutional provisions or enabling legislation. Restricted net assets consisted of the following at June 30:

	2011	2010
Debt service reserve on 2003 Water Revenue Refunding Bonds	\$ 243,329	\$ 242,485
Restricted for capital improvement projects	143,104	8,779
Total restricted net assets	\$ 386,433	\$ 251,264

The restrictions for debt service represent debt service and other reserves required by the related debt covenants. The restriction for capital improvement projects represents surcharges collected under Ordinance No. 2009-03 passed by the Board in May 2009 to fund projects to comply with a State of California Department of Public Health Compliance Order. As of June 30, 2011, the District owes the restricted for capital improvement projects account, \$145,902 from its unrestricted net assets because not all of the surcharge revenues were deposited in this account and certain expenditures were paid out of this account that do not appear to qualify for the use of these funds.

NOTE G – DEFINED BENEFIT PENSION PLAN

Plan description: The District contributes to the California Public Employees Retirement System (PERS), a cost sharing multiple-employer public employee defined benefit pension plan. The District participates in the miscellaneous 2% at 55 risk pool. PERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. PERS acts as a common investment and administrative agent for participating public employers within the State of California. CalPERS require agencies with less than 100 active members in the plan to participate in the risk pool. All full and part-time District

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT
 NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

June 30, 2011

NOTE G – DEFINED BENEFIT PENSION PLAN (Continued)

employees working at least 1,000 hours per year are eligible to participate in PERS. Under PERS, benefits vest after five years of service. Upon retirement, participants are entitled to an annual retirement benefit, payable for life, in an amount equal to a benefit factor times the monthly average salary of their highest twelve consecutive months full-time equivalent monthly pay. A menu of benefit provisions as well as other requirements is established by State statutes within the Public Employees' Retirement Law. The Plan selects optional benefit provisions from the benefit menu by contract with PERS and adopts those benefits through District resolution. PERS issues a separate comprehensive annual financial report. Copies of the PERS' annual financial report may be obtained from the PERS Executive Office - 400 P Street - Sacramento, California 95814.

Funding policy: Active plan members were required to contribute 7% of their annual covered salary. The District made contributions required of District employees on their behalf and for their account up through October 2009. The contribution made by the District on behalf of the employees was \$6,449 for the year ended June 30, 2010. No amounts were paid on the employees' behalf during the year ended June 30, 2011. The District is required to contribute at an actuarially determined rate. The required employer contribution rate for 2010/11 and 2009/10 was 12.813% and 13.097%, respectively. The contribution requirements of the plan members and the District are established and may be amended by PERS. The District's contributions for the years June 30, 2011, 2010 and 2009 were \$40,146, \$39,513, and \$88,291, respectively, which were equal to the required contributions each year.

NOTE H – COMMITMENTS AND CONTINGENCIES

The District is party to various claims, legal actions, and complaints that arise in the normal course of business. Management and the District's legal counsel believe that there are no material loss contingencies that would have a material adverse impact on the financial position of the District. In June 2012, the District settled several lawsuits with a former employee, for which the District will be required to pay [REDACTED]

The District entered into two construction contracts and two other contracts subsequent to June 30, 2011. The commitment amounts on these contracts total \$2,302,430. In addition, unexpended commitments on contracts in place as of June 30, 2011 totaled \$142,073.

NOTE I – INSURANCE

The District participates in the Association of California Water Agencies Joint Powers Insurance Authority (ACWA/JPIA) a public entity risk pool of California water agencies, for general and auto liability, public officials liability, property damage and fidelity insurance. ACWA/JPIA provides insurance through the pool up to a certain level, beyond which group purchased commercial excess insurance is obtained.

The District pays an annual premium to ACWA/JPIA that includes its pro-rata share of excess insurance premiums, charges for the pooled risk, claims adjusting and legal costs, and administrative and other costs to operate the ACWA/JPIA. The District's deductibles and maximum coverage are as follows:

Coverage	ACWA/JPIA	Commercial Insurance	Deductible
General and Auto Liability (Includes Public Officials Liability)	\$ 1,000,000	\$ 60,000,000	None
Property Damage	50,000	100,000,000	\$ 500 - 25,000
Fidelity	100,000		1,000

The District continues to carry commercial insurance for all other risks of loss to cover all claims for risk of loss to which the District is exposed. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT
NOTES TO THE BASIC FINANCIAL STATEMENTS (Continued)

June 30, 2011

NOTE J – GOING CONCERN

The financial statements for the years in question have been prepared assuming that the District will continue as a going concern, which contemplates the realization of assets and satisfaction of liabilities in the normal course of business. The District has suffered reoccurring operating losses and diminishing working capital since 2007 through the period ended June 30, 2009. In addition, although the balance sheet shows unrestricted net assets of \$86,424 as of June 30, 2011, because \$145,902 is owed to the restricted for capital improvements as discussed in Note F, unrestricted net assets has a deficit of \$59,478 after considering this amount that is owed. As a result of these factors, there is doubt about the District's ability to continue as a going concern. The District has reduced personnel expenses, plans to increase revenue through an increase in the capital surcharge and in water rates, and has obtained a State safe drinking water loan to finance additional wells. The District is addressing reorganization, receivership and other options, but the outcome cannot be assured at this time.

NOTE K – SUBSEQUENT EVENTS

On November 19, 2007 the District received the California Department of Public Health Compliance Order 01-09-07-CO-004 with a full compliant date of December 31, 2008. The Compliance Order documents finding or facts about the water source capacity and low-pressure problems observed in the District, and includes nine Directives to accurately characterize the problems, evaluate solution options, and implement interim measures towards the complete resolution of the water source capacity and low-pressure problems. On October 13, 2008, the District requested and received an extension to March 31, 2009 from the Department of Public Health to become fully compliant with Compliance Order No. 01-09-07-CO-004. On November 23, 2010, the District's application was accepted for a \$7,499,045 State safe drinking water loan to finance the drilling of new wells to meet the requirements stipulated in the Department of Public Health Compliance Orders. As of the date of this report, loan proceeds totaling \$695,455 have been received. The District was required to adopt an increase in water rates of \$5.46 per month per connection effective within two years after the date of execution of the funding agreement to repay the loan. Payments on the loan will be covered by the surcharge collected from the customers. The loan will be required to be repaid over 20 years, starting after completion of the project. The interest rate on the loan will be 2.5707 percent, with semi-annual payments of \$240,959 required.

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INDEPENDENT AUDITOR'S 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
Rio Linda/Elverta Community Water District
Rio Linda, California

We have audited the financial statements of the Rio Linda/Elverta Community Water District (the District) as of and for the year ended June 30, 2011 and have issued our report thereon dated June 12, 2012. We did not express an opinion on the District because of the departures from generally accepted accounting principles and uncertainties described in the audit opinion. Except as discussed in the preceding sentence, 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

Management of the District is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered 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.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying schedule of findings, we identified certain deficiencies in internal control over financial reporting, that we consider to be material weaknesses.

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 deficiencies described in the accompanying schedule of findings to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the 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*.

To the Board of Directors
Rio Linda/Elverta Community Water District

We noted certain other matters that we reported to management of the District in a separate letter dated June 12, 2012.

This report is intended solely for the information and use of the Board of Directors, management and the State of California and is not intended to be and should not be used by anyone other than these specified parties.

Richardson & Company

June 12, 2012

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

SCHEDULE OF FINDINGS

June 30, 2011

Finding 2011-1: Payroll Accounting Entries

The District recorded salary expense net of withholdings starting in November 2010, resulting in payroll-related transactions being recorded in the incorrect expense or liability account. We also noted the District did not have separate accounts set up for some of the necessary payroll-related expenses or accrual entries. These items resulted in numerous adjusting journal entries to correct the mispostings. We recommend the District revise its entries for posting payroll transactions, establish separate expense and accrual accounts for the individual payroll-related entries and reconcile the payroll register with the general ledger accounts after each payroll period.

Finding 2011-2: Year-end Payroll Accrual

The District did not accrue for five days for payroll expenses at the end of June that were not paid until July 15 in the next fiscal year. We recommend the District include this accrual into their year-end closing checklist.

Finding 2011-3: Internal Control and Management Review

Management review and oversight is an important internal control. During fiscal year 2010/11, the District had three general managers, with most of the fiscal year the District's legal counsel was functioning as the interim general manager. We noted several areas where review by management was not performed, or at least not documented during fiscal year 2010/11:

- a. Management was not reviewing or approving journal entries prepared and entered into the general ledger by the bookkeeper.
- b. The General Manager was not reviewing and approving the timesheets for supervisors.
- c. There is no indication of review of the payroll registers by the General Manager.
- d. Many of the invoices did not have initials indicating approval by the General Manager. In addition, several check copies could not be located.

We recommend the General Manager review these various documents and initial them to document review and approval, and that original checks be maintained.

Finding 2011-4: Account Reconciliations

The District had not recorded several smaller miscellaneous water billing system accounts into the general ledger accounts thereby understating water revenues. This oversight resulted in an audit adjustment to correct the revenue and receivable account balances. We recommend the billing system amounts and general ledger be compared monthly to ensure all revenues are being correctly recorded in the general ledger. We understand that the District has established this process in fiscal year 2011/12.

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

SCHEDULE OF PRIOR YEAR FINDINGS

June 30, 2011

Finding 2010-1: Other Post-Employment Benefits Accrual

Condition: In April 2004, the Governmental Accounting Standards Board issued Statement No. 45, *Accounting and Financial Reporting by Employers for Post-Employment Benefits Other than Pensions*, which was required to be implemented during the year ended June 30, 2010. The Statement requires that the District establish a liability for other post-employment benefits (OPEB) to be measured and reported according to certain parameters. Because the District did not have an actuarial study performed, an OPEB liability could not be recorded at June 30, 2010. Since the District is currently expensing the premiums paid for retirees as they are paid, the implementation of this Statement will result in the District being required to accrue an OPEB liability, which could be a significant amount. This Statement does not require the plan to be funded. In order to comply with generally accepted accounting principles, the District will need to have an actuarial valuation performed to determine the amount of liability to accrue.

Status: The District has not yet had the actuarial study performed, so an OPEB liability is not recorded as of June 30, 2011.

Finding 2010-2: Year-end Closing Procedures and Account Reconciliations

Condition: This year's audit and the District's closing process was delayed because of turnover in personnel, the lack of central oversight and the lack of resources dedicated to the close-out of the general ledger and preparing for the audit. The results were delays in producing closing entries, trial balances, schedules, reconciliations, account analyses, and other financial reports needed by management and the auditors and resulted in numerous audit adjustments. The large number of adjustments identified during the course of the audit indicates that the District does not have the internal controls in place to prevent or detect misstatements on a timely basis. To facilitate the closing process, a closing procedures checklist should be developed to ensure the District has all closing entries prepared before the start of the audit. The District needs to ensure that all balance sheet reconciliations and account balance analyses are prepared and reviewed. Areas where accounts and transactions were not adequately reconciled and evaluated for proper recording prior to the start of the audit fieldwork and areas that require improvement included the following:

- a. In preparing the reconciliations of accounts receivable and deposits payable from the billing system to the general ledger at June 30, 2010, the District had unreconciled differences of \$5,984 in accounts receivable and \$3,417 in deposits payable. In addition, the billing system showed a credit balance of \$5,444 in the surcharge receivables, which would indicate overpayments were made, that needs to be investigated. Reconciliation of the billing system to the general ledger should be performed throughout the year and at year-end so that such differences can be identified and corrected on a timely basis. Evaluation of the need for an allowance for doubtful accounts also needs to be performed at least annually. At June 30, 2010, receivables over 120 days past due totaled \$10,800.
- b. Until recently, the District had not been entering invoices in the accounts payable module as they were received, only as they were paid. As a result, the District had no way of knowing the amounts owed to vendors as of a given point in time. The District entered the invoiced owed but unpaid as of June 30, 2010 in preparation for the audit. Going forward, the District needs to generate an accounts payable trail balance and compare it to the general ledger on a regular basis.
- c. Procedures for accounting for long-term debt and related accounts needs to be established including: calculation and recording of interest payable on long-term debt, maintaining supporting documentation for the amounts recorded for the amortization of deferred amount on refunding and issuance costs related to the debt issuances of the District.
- d. The restricted net asset balances were not adjusted to agree to the corresponding restricted cash accounts. Procedures need to be established for adjusting restricted net assets to their proper balances.
- e. The District received land for well #14, but this land was not valued and recorded as an asset and contributed capital revenue in the general ledger. Procedures for identifying and quantifying donated assets need to be established.

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

SCHEDULE OF PRIOR YEAR FINDINGS (Continued)

June 30, 2011

- f. We noted that not all twelve months of cell tower lease revenue was recorded. The District needs to ensure the proper tracking of cell tower lease payments to ensure amounts are received on a timely basis or are accrued to ensure completeness of revenue.
- g. Prepaid expenses had not been adjusted since the prior fiscal year end. Procedures need to be established to ensure prepaid balances are expensed over the period for which the services were provided.
- h. The District had not performed a physical inventory count of its supplies inventory since June 30, 2009. Since a perpetual inventory system is not maintained, the inventory balance as of June 30, 2010 has not been revised. The District needs to ensure that a physical inventory count is performed at least annually so that the general ledger balance can be adjusted.
- i. A number of accrual adjustments were not reflected in the general ledger prior to the audit. These adjustments include accruing a receivable for the portion of the July water billings that relate to June, and May, accruing a liability for compensated absences and accruing the PERS retirement payments owed as of June 30.

We recommend that the District develop an accounting procedures manual to ensure continuity in processes when staff turnover occurs. Procedures should be in place to prepare the required reconciliations at year-end and throughout the year and post entries needed to close the books prior to the start of the audit.

Status: The District has addressed items b., f. and i. for the fiscal year 2010/11 audit. Unreconciled differences were noted between the billing system and the general ledger for the fiscal year 2010/11; however, we understand a reconciliation process has been put in place in fiscal year 2011/12. We also understand that a physical inventory of supplies has been taken during fiscal year 2011/12 to address item h. The remaining items still need to be addressed.

Finding 2010-3: Internal Controls and Separation of Duties

Condition: Certain procedures, which should be separated, are performed by the same person due to the District's small number of accounting staff. The lack of consistent segregation of duties is not unusual for small water districts; however, compensating controls need to be put in place to reduce the risk of misstatement or fraud. The following areas were identified where internal control deficiencies exist:

- a. The bookkeeper processes invoices, enters them into the accounts payable system, writes checks, has access to the general ledger, and receives the bank statements and reconciles the bank accounts, which is not an adequate segregation of duties. The previous long-time bookkeeper was also able to sign checks. To compensate for this lack of segregation of duties, the General Manager should receive all bank statements unopened and review them prior to forwarding to the bookkeeper. After completion of the monthly bank reconciliations by the bookkeeper, they should be reviewed and approved by the General Manager. Complete listings of checks written should be provided to the Board for review on a monthly basis.
- b. After accounts payable checks have been signed, they are returned to the bookkeeper, who prepares the checks for mailing. Signed checks should be mailed by someone not associated with the accounts payable function.
- c. Billing preparation, processing of customer payments, posting billing and payment information to customer accounts, making customer billing adjustments and follow-up on billing questions are all accomplished by the same employee, which is not an adequate segregation of duties. While a procedure is in place whereby the General Manager is to approve billing adjustments over \$100, the billing clerks have the ability to make these adjustments in the system without approvals. A review of all billing adjustments should be performed by the General Manager using the adjustment report generated from the system. The documentation of the authorization of billing write offs or adjustments needs to be maintained to document this approval.

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

SCHEDULE OF PRIOR YEAR FINDINGS (Continued)

June 30, 2011

- d. Currently all bank deposits are being made by the billing clerk, but this person also has access to the accounts receivable module, which is not an adequate segregation of duties. While it may not be feasible for physical bank deposits to be made by an individual who does not have access to the accounts receivable module, the bookkeeper, who does not have access to the billing system, should review the documents to ensure agreement of the deposit amount to the postings to customer accounts in the billing system and then compare the deposit slip to the bank statement.
- e. We noted that entries made to the payroll system, such as changes to the pay rates, were not being reviewed. We recommend that any payroll system changes be reviewed and approved by the General Manager. In addition, the General Manager should be reviewing the payroll registers and/or check stubs and documenting this review with an initial.
- f. Regular staff meetings should be held to identify and resolve issues and provide sound guidance.

The District needs to re-evaluate its internal control system to ensure adequate segregation of duties are in place, and reconciliation and review functions are taking place.

Status: Due to the timing of when this finding was first reported, the fiscal year was already past, so these internal controls have not yet been put into place.

Finding 2010-4: Financial Reporting

Condition: The District needs to establish a financial reporting system that includes the reporting of financial information to the Board on a regular basis. The District also needs to ensure that it complies with the California Government Code with regard to its investment reporting. The Government Code calls for quarterly reports on the District's financial holdings, a statement of compliance with the policy and a statement concerning the District's ability to meet its cash flow needs in the ensuing six months. We did not see where these investment reports were provided.

Status: Financial reports were not provided during fiscal year 2010/11; however, we understand that reports are being provided in fiscal year 2011/12.

Finding 2010-5: Organization of Accounting Records

Condition: We noted that the District's accounting records were disorganized making records difficult to locate for the audit, partly because of the records being confiscated by the District Attorney's Office. As a result, the District was not able to locate supporting invoices for 19 out of the 85 samples of expenses we selected for testing. We recommend the District develop accounting procedures for proper filing and storing of invoices and other accounting documentation.

Status: We noted an improvement in the maintaining of accounting records.

Finding 2010-6: Capital Asset Accounting

Condition: The District was unable to locate its capital asset listing and depreciation schedule and had to create one from the listing prepared by the prior auditor. The District needs to ensure it maintains its own capital asset listing and depreciation schedule, and that updates to the listing be made throughout the year.

The District records its capital asset additions as expenses instead of capital assets. The District needs to establish procedures to identify and record capital asset additions, including construction in progress, on the asset listing on a timely basis, to record depreciation expense and to track and record fixed asset disposals. We noted two vehicles were sold in fiscal year 2009/10, but these vehicles were not removed from the asset list. We also noted the District's capital asset listing still contained assets that had been disposed of years earlier and in several cases only a portion of the cost and accumulated depreciation of the assets was removed. Periodic inspections of capital assets need to be performed to ensure that recorded assets still exist. Reconciliations of the capital asset list to the general ledger need to be performed on a periodic basis, and adjustments to the general ledger need to be made timely.

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

SCHEDULE OF PRIOR YEAR FINDINGS (Continued)

June 30, 2011

We noted that the District's capital asset listing did not include intangible assets or land. As a result, amortization of the intangible assets was not calculated and recorded in the general ledger, which resulted in an audit adjustment being required. The District needs to ensure that a list of all land holdings, including those that were donated, and intangible assets is maintained as part of the capital asset listing.

Status: During the 2011 audit, we noted the District has now updated their capital asset listing. However, as part of the closing process, the District needs to reclassify capital assets from expense to capital assets and to include land and intangible assets on its asset listing.

Finding 2010-7: Surcharge Cash Account

Condition: We noted the District borrowed cash totaling \$37,500 from the restricted surcharge bank account to cover low or negative balances in the operating bank account. While we noted the funds were paid back to the surcharge account, any use or transfers of restricted funds should be reviewed and approved by management or the Board of Directors.

Currently when the capital improvements surcharge is collected, it is deposited into the operating bank account before being transferred to the surcharge bank account. Because revenues received in fiscal year 2010 exceeded the total funds deposited into the surcharge account by \$16,130, this implies that not all of the funds have been transferred from the operating bank account to the surcharge bank account. We recommend the surcharge amount collected for capital improvements be deposited directly into the surcharge bank account, if practicable to do so, or at a minimum, there be a quarterly reconciliation performed that compares revenues collected for the capital improvement surcharge with amounts deposited into the surcharge bank account to ensure surcharge receipts are recorded correctly, or whether a transfer needs to be made.

Status: The District believes it is not practical to deposit daily receipts into the surcharge account, but the District has plans to implement a process beginning in fiscal year 2011/12 where monthly, the billing system amounts are reconciled with the general ledger and the surcharge receipts for the month are transferred into the surcharge account from the District's operating account. In our fiscal year 2010/11 audit, we noted that revenues of approximately \$17,729 have not been recorded in the surcharge account. In addition, \$105,856 of expenditures were paid out of the surcharge account that do not appear to be qualifying expenditures. As a result, the operating account owes the surcharge account \$145,903 as of June 30, 2011.

Finding 2009-1: Organization of the District

Condition: The prior auditors observed the structure and the roles of the Board, management and employees and the effectiveness of the District's lines of communication. The prior auditors believed the District needs to review the tasks that have been assigned to the employees to ensure their completion but overall responsibilities of employees have not been formalized or properly defined. The prior auditors believed the District needs to rebalance the current workloads to ensure that the proper functions are performed by the proper employee, therefore ensuring proper internal control. Additionally, balanced workloads will ensure that employees have the appropriate time to dedicate to the accurate completion of their tasks and will also improve employee morale.

Status: The organization structure and workloads do not appear to have been revised since the prior audit. Special attention needs to be given to addressing the internal control issues identified in Finding 2010-3 as far as workload re-assignments.

Finding 2009-2: Develop an Organization Chart

Condition: The District does not have an organization chart. There is a natural tendency to dismiss the need for an organization chart in a small business where management deals more or less directly with each employee, and where all personnel know each other and are generally aware of each other's area of responsibility. However, without an organization chart, there may be confusion about who is really accountable for particular areas and to whom employees are responsible. The result could be that some areas of operations do not receive adequate attention or

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

SCHEDULE OF PRIOR YEAR FINDINGS (Continued)

June 30, 2011

that duplicative or contradictory actions are taken. A good organization chart can prevent such misunderstandings and also increase administrative efficiency and control in the following ways:

- Indicate whether there is appropriate allocation of operating and supervisory responsibility.
- Indicate whether there is an adequate separation of duties.
- Inform management, new employees, and others of the District's management and operating style.
- Provide information for management to monitor and inquire into operations and procedures, assign new duties or responsibilities that may arise, or make reassignments when employee turnover, promotions, operational needs, desire for better separation of duties, or other circumstances call for it.

The prior auditor recommended that management prepare and maintain a chart of organization in sufficient detail to indicate the District's major areas of operations, the person responsible for each area, and who each supervisor reports to as well as which employees report to each supervisor. The chart should be updated whenever there is significant employee turnover or changes in operations.

Status: An organization chart was not in place as of June 30, 2011. However, we noted management has recently developed an organization chart for Board approval.

Finding 2008-3: Budget

Condition: The auditor's opinions for the past three fiscal years have been issued with the contingency of a going concern. This states to the readers of the District's financial statements that the District's auditors have found substantial doubt about the District's ability to maintain operations at sufficient levels to remain in business. In response to their concerns, former management provided several updated budgets which were unclear in nature therefore ineffective. The fundamental purpose of budgetary control is to plan beforehand the most efficient operation and then maintain operations according to the budget.

Budgets stimulate early identification of operational problems and help ensure that timely decisions are made for resolving the problems. Budgetary control also results in better coordination and control of the District's efforts and in more effective use of the District's resources.

We believe that the District could more accurately evaluate operational performance by revising current budgeting procedures to provide for the following:

- Obtaining estimates of future operational data from field operations, and administrative personnel.
- Updating the current year's budget at least quarterly for operational changes.
- Communicating operational performance to appropriate personnel.

It is understood that the nature of the District's operations, as well as the uncertainties inherent in economic activity, makes predications of the future subject to frequent change. Thus, we recommend that the District perform periodic reviews for variances between actual and budgeted results and document the variances between actual and budgeted results. Budget variances may indicate possible problems that can be identified quickly and followed-up. Variances can also be caused by erroneous assumptions, not business or economic factors. If investigations of budget variances suggest that the budget is inaccurate, or if business conditions vary from expectations, the budget should be revised to reflect current conditions or more reasonable estimates.

Status: The District has been through numerous management changes over the past few years such that there has not been continuity in the managers preparing the budget and monitoring variances throughout the fiscal year. As discussed in the Finding 2010-4, the District needs to ensure it has an adequate financial reporting system in place such that sound management decisions can be made.

RIO LINDA/ELVERTA COMMUNITY WATER DISTRICT

SCHEDULE OF PRIOR YEAR FINDINGS (Continued)

June 30, 2011

Finding 2007-2: Accounting Policies

Condition: The prior auditor's review of internal controls brought to their attention the fact that the District has no current formal accounting policies and procedures. Having an up-to-date accounting policies and procedures manual will provide for efficient training of new staff, effective and timely financial reporting and consistency within the Administrative department. We recommend the District prepare an accounting policies manual that should address management's risk factors in relation to financial reporting.

Status: Because the District does not have an accounting policies and procedures manual, the departure of the long-time bookkeeper has made it difficult for successor bookkeepers to ensure continuity in accounting functions and to follow the work of the predecessor bookkeeper.

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To the Board of Directors and Management
Rio Linda/Elverta Community Water District
Rio Linda, California

In planning and performing our audit of the financial statements of the Rio Linda/Elverta Community Water District (the District) as of and for the year ended June 30, 2011, in accordance with auditing standards generally accepted in the United States of America, we considered the District's internal control over financial reporting (internal control) 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. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

However, during our audit, we became aware of the following matter that is an opportunity for strengthening the financial position of the District and has been included in this letter for your consideration. A separate report dated June 12, 2012, contains our report on material weaknesses in the District's internal control. This letter does not affect our report dated June 12, 2012 on the financial statements of the District.

Bank reconciliations

We noted that one bank account, the LAIF account and the investments held by trustee Bank of New York Mellon, did not reconcile to the bank statements within immaterial amounts. We recommend that the District ensure that any unreconciled differences be researched and/or adjusted in the general ledger.

Standby

We recommend the District institute a policy to bill a standby fee to those properties connected to the District but which currently do not take any District water to ensure a consistent revenue stream for repayment of debt service. If the District were to charge the surcharge amount as a standby fee, an additional \$14,000 of revenue could be generated annually.

The following are our prior year findings that continue to be opportunities to strengthen internal controls and operating efficiencies:

Fraud Reporting Procedures

We recommend the District develop and adopt a Fraud Prevention/Whistle Blower Policy. The policy or procedures should include a discussion of what types of activities constitute fraud or contracting improprieties, how an employee should report such suspected fraud or contracting improprieties and to whom or where an employee should report such activities, including reporting procedures if an employee's supervisor or a member of senior management is suspected of these activities.

Risk Assessment Plan

We recommend that the District develop a risk assessment plan to identify those risks within the District that could result in fraud or material misstatement of the financial statements, and then to implement internal controls to mitigate those identified risks. This risk assessment plan should identify potential risk areas and then ensure controls or processes are in place to mitigate those risks. This risk assessment should be performed on a periodic basis and can be incorporated into existing staff and management meetings.

Investment Policy

The District does not have an approved investment policy as required by Government Code Section 53600.3. This policy and any changes must be considered at least annually by the Board at a public meeting. We understand that a policy was developed in fiscal year 2011/12.

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This report is intended solely for the information and use of the Board of Directors, management, and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

Richardson & Company

June 12, 2012