CITRUS HEIGHTS WATER DISTRICT

AUDITED FINANCIAL STATEMENTS

December 31, 2014

CITRUS HEIGHTS WATER DISTRICT

AUDITED FINANCIAL STATEMENTS

December 31, 2014 and 2013

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Citrus Heights Water District
Citrus Heights, California

Report on the Financial Statements

We have audited the accompanying financial statements of Citrus Heights Water District (the District), which comprise the balance sheets as of December 31, 2014 and 2013, and the related statements of revenues, expenses, changes in net position, and cash flows for the years then ended and the related notes to the financial statements.

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.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits 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, 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's 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.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

To the Board of Directors
Citrus Heights Water District

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the District as of December 31, 2014 and 2013 and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America as well as accounting systems prescribed by the State Controller's Office and state regulations governing special districts.

Report on Supplemental Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis information on pages 3 through 12 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 6, 2015 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 and contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on 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 the District's internal control over financial reporting and compliance.

Richardson & Company, LLP

April 6, 2015

CITRUS HEIGHTS WATER DISTRICT

Management's Discussion and Analysis
December 31, 2014

The management of the Citrus Heights Water District (District) presents this Management Discussion and Analysis to achieve two goals:

1. To comply with the requirements of Governmental Accounting Standards Board Statement 34 (GASB 34) that are designed to provide more and easier-to-understand information about the finances of local government agencies such as the District; and

2. To provide readers with narrative information that may help in understanding and interpreting the information presented in the District's financial statements for the fiscal year ended December 31, 2014 (FY2014).

Questions or comments regarding this Management Discussion and Analysis may be directed to the District Treasurer via the following methods:

Mailing address:	Citrus Heights Water District P.O. Box 286 Citrus Heights, California 95611-0286
Telephone:	(916) 725-6873
Facsimile:	(916) 725-0345
E-mail:	custserv@chwd.org

Financial Highlights

The following items are, in the opinion of District management, among the most significant in assessing the District's overall financial activities during FY2014 and its financial position at the close of FY2014:

- The District's assets exceeded its liabilities at the end of FY2014 by $55,900,828. About 82.2 percent of the District's net position, $45,931,665, is composed of the capital assets of the District – the water transmission and distribution system, water production facilities, land, buildings and equipment belonging to the District. Unrestricted net assets totaled $9,432,200, down from $10,414,469 at the end of FY2013. This decrease is due primarily to increased capital improvement spending in FY2014 as compared with FY2013. The decrease in unrestricted net assets represents a leveling off of the District's efforts to rebuild its financial reserves after depleting them between 2000 and 2008 to pay for water meters, groundwater wells and other capital improvements. The District has designated $1,000,000 from its unrestricted net position for rate stabilization and/or catastrophic losses, leaving $8,432,200 for current and future operations and projects.

- The District's operating revenues for FY2014 were $11,331,301. About 89.8 percent of operating revenues, $10,171,473, came from water sales to customers. As previously mentioned, the District adopted a rate increase for FY2014, increasing water rates by 3 percent above water rates that were in place for FY2013. However, a 20 percent decrease in water sales during FY2014 caused a dip in operating revenues even with an increase in rates. There was a corresponding decrease in water purchase costs, $1,984,921 in FY2014 compared with $2,322,002 in FY 2013.

- The District's total net long-term liabilities at the end of FY2014 including the 2012 Revenue Refunding bonds, the 2010 Revenue Refunding Certificates of Participation, accrued other postemployment benefits and compensated absences, is $5,759,107. This is a decrease of $415,381 from net long-term liabilities at the end of FY2013, due in large part to a reduction in principal on debt during 2014 resulting from debt service payments during the year.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of two parts: (1) management's discussion and analysis; and (2) the financial statements, including the notes to financial statements.

The financial statements provide both long-term and short-term information about the District's overall financial status. The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data.

The District's financial statements are prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units on an accrual basis. Under this basis, revenues are recognized in the period in which they are earned, expenses are recognized in the period in which they are incurred, and depreciation of assets is recognized in the Statement of Revenues, Expenses and Changes in Net Assets. All assets and liabilities associated with the operation of the District are included in the Balance Sheet.

The Balance Sheet presents the financial position of the District on a full accrual historical cost basis and provides information about the nature and amount of resources and obligations at year-end.

Balance Sheet

As of December 31, 2014, the total net position of the District was $55,900,828. The following table summarizes assets, deferred outflows, liabilities, deferred inflows and net assets at December 31, 2014 and 2013:

	2014	2013
Current assets, unrestricted	$ 11,897,541	$ 12,628,608
Restricted cash and cash equivalents	536,963	536,973
Capital assets, net	50,782,462	47,548,396
Deferred outflows	75,042	88,093
Total Assets and Deferred Outflows	63,292,008	60,802,068
Current liabilities	1,601,576	1,538,722
Long-term liabilities	5,759,107	6,174,488
Deferred Inflows	30,497	29,172
Total Liabilities and Deferred Inflows	7,391,180	7,742,382
Net Position		
Net investment in capital assets	45,931,665	42,108,244
Restricted	536,963	536,973
Unrestricted	9,432,200	10,414,469
Total Net Position	$55,900,828	$53,059,686

The District's net position reflects restrictions imposed as a condition of its Certificates of Participation debt. The remaining net position is unrestricted.

Changes in Net Position

The following table summarizes the changes in net position for the fiscal years ended December 31, 2014 and 2013:

	2014	2013
Operating revenues	$ 11,331,301	$ 11,358,086
Operating expenses:		
Customer service, administration and general	2,752,172	2,763,786
Water purchases	1,984,921	2,322,002
Transmission and distribution	1,282,941	1,289,768
Pumping and well maintenance	239,344	133,950
Water demand management	99,235	88,817
Depreciation and amortization	2,003,488	1,898,303
Total operating expenses	8,362,101	8,496,626
Operating income	2,969,200	2,861,460
Net nonoperating revenues (expenses)	(187,306)	(163,505)
Net income before capital contributions	2,781,894	2,697,955
Capital contributions:		
Contributed (donated) assets	59,248	70,657
Capital grants	-	-
Total capital contributions	59,248	70,657
Change in net position	2,841,142	2,768,612
Net position, beginning of year	53,059,686	50,291,074
Net position, end of year	$ 55,900,828	$ 53,059,686

Total net position increased $2,841,142, or 5.4 percent from the prior year. Operating revenue that exceeded operating expenses by $2,969,200 accounts for the increase in net assets, and most of these funds were expended for the construction of capital improvements or set aside for that purpose. The receipt of $59,248 in donated assets from private developer additions to the District's water distribution system accounted for about 2.1 percent of the increase in net assets.

Total operating revenues decreased very slightly, $26,785 or 0.2 percent from the prior year despite an increase in water rates for FY2014. This was due to a decrease in water sales. Water consumption by District customers decreased by 20 percent in FY2014 compared with consumption in FY2013. With a third year of drought conditions in California, water supplies in the State became a greater concern. Customers responded to the declaration of a Stage 3 –Water Warning by the CHWD Board of Directors and State-wide emergency water use regulations by significantly reducing their water consumption.

Operating expenses also decreased slightly in FY2014 by $134,525, a 1.6 percent reduction compared with FY2013. A decreased cost for water purchases for FY2014, $337,081 compared with purchases in FY2013, resulted from the reduction in water consumption by District customers and increased groundwater production from the District's wells. This decrease in water purchase cost more than offset an increase of $105,394 in pumping and well maintenance costs that resulted from increased groundwater pumping. The increased groundwater pumping was done to help extend limited surface water supplies from Folsom Lake, the District's primary source of water supply.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

As of December 31, 2014, the District's investment in capital assets, net of related debt, was $45,931,665, including: the water transmission and distribution system (underground pipelines, water services, water meters, fire hydrants, and other components); water production facilities (groundwater wells); land; buildings and both mobile and fixed equipment.

Replacement of aging pipelines and water service connections throughout the District's system continued to represent the majority of the $3.23 million additions to the District's capital assets in FY2014. A number of private development projects resulted in the addition of $59,248 in donated capital assets.

Additional information on the District's capital assets can be found in Note C, Capital Assets, of the notes to the basic financial statements.

Debt Administration

The District continues to meet its debt obligations under its 2010 Refunded Certificates of Participation (COPs), and the 2012 Revenue Refunding bonds. Through scheduled debt service payments during FY2014, principal on its collective debt was reduced by $544,820 during the year. The District's total debt from its COP and bond issuances now stands at approximately $5.43 million.

Total compensated absences (long-term liability and current portion combined), are composed of leave hours earned by employees that are payable upon termination or retirement and are valued at $373,174 at the end of FY2014, a decrease from the FY2013 year-end amount of $404,756. This reduction was due primarily to cash payments for accrued leave balances during the year to two retiring employees.

The accrual for other post-employment benefits increased by $97,800 in FY2014 as a result of the annual cost of these benefits exceeding the amounts currently paid for premiums.

Additional information on the District's debt activity can be found in Note D, Long-Term Liabilities, of the notes to the basic financial statements.

ECONOMIC FACTORS AND FUTURE BUDGET CONSIDERATIONS

The District continued to exercise fiscal restraint in budgeting for District operations in FY2015, with an overall decrease of 0.12 percent compared with the FY2014 Operating Budget. This budget includes:

- Maintaining the current level of services and programs for District customers;

- Continuing increases in regulatory compliance costs such as permitting costs paid to other public agencies and new water quality testing regulations;

- Decreases in some salary and benefits costs due to retirement of long-tenured employees and hiring of new employees at lower levels of the salary range for the same positions. New employees that were not previously members of the CalPERS retirement system also have significantly lower retirement contribution costs due to benefit formulas set in place by the Public Employee Pension Reform Act (PEPRA) enacted by the California Legislature in 2012. Even with these decreases, total salary and benefit costs for District employees were budgeted at 1.58 percent above FY2014 compensation levels;

- A total of $1.95 million in funds allocated to rebuilding financial reserves for capital improvement and employment-related benefits.

A 2015 Operating Budget Summary is included at the conclusion of this Management's Discussion and Analysis to provide an overview of the District's operating budget.

The District has rebuilt its financial reserves from their 13-year low of $3.03 million at the end of FY2008 to a level that supports a higher level of capital investment from reserves. Total capital improvement expenditures budgeted for FY2015 are about $9.96 million compared with $9.87 million in FY2014. This amount includes about $8.23 million in carry-over projects from prior years, and about $1.73 million in new projects for FY2015. Completion of construction of a new groundwater well accounts for $1.64 million of planned spending in FY2015, with completion of several water main installation and replacement projects approved in prior years totaling over $1.82 million. An expansion and interior improvements to the District's Administration Building, which began in FY2012, is budgeted for construction in FY2015 at about $978,171. The District has budgeted for over $678,000 in water service connection replacements during FY2015, and about $174,000 for replacing fire hydrants, or upgrading or adding new hydrants to the District's system. Also budgeted is the replacement of field operations equipment such as a loader, a 1-ton dump truck and two pickup trucks to be replaced in FY2015 in the amount of about $174,000. A 2015 Capital Improvement Budget Summary is included at the conclusion of this Management's Discussion and Analysis to provide an overview of the District's capital improvement budget.

A significant but declining portion of the District's budget continues to be the repayment of long-term debt financing in the form of Certificates of Participation originally issued in 2000 (refunded in 2010) and Certificates of Participation originally issued in 2003 (refunded as Revenue Refunding Bonds in 2012). The annual debt service for these two issuances is budgeted at $736,488 for FY2015, representing about 7.6 percent of the District's FY2015 Operating Budget.

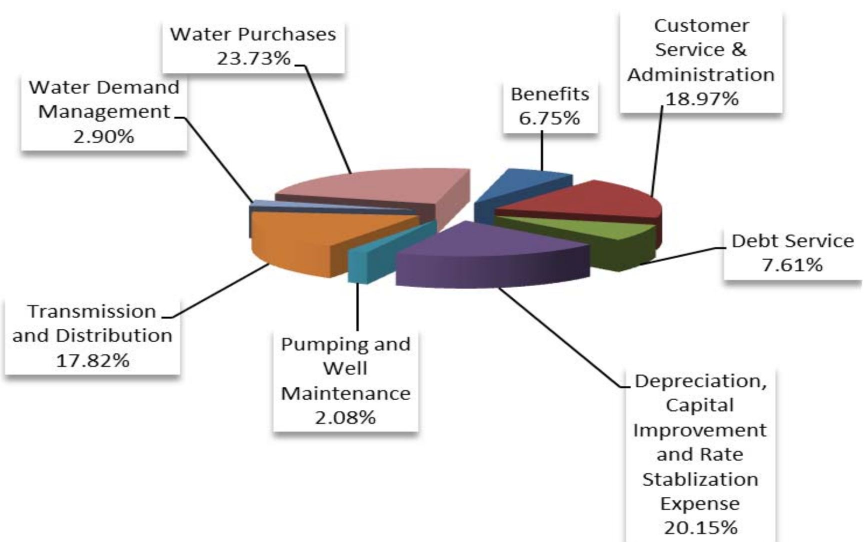
The District's Board of Directors levied a water rate increase designed to achieve an overall increase in water rate revenues of 3.00 percent for 2015. The water rate increase continued to follow the structure of water rates that was set in place for FY2014 after performing a detailed cost-of-service and financial plan study in FY2013. The restructuring of water rates done for FY2014 was designed to more accurately and equitably assign the cost of service provided to the customers receiving the benefit of those services. Included in this restructuring of rates was the elimination of inclining block tiered rates for water consumption in favor of a single uniform tiered rate for all units of water consumed by customers. The increase in revenues resulting from the FY2015 water rates will provide additional revenue to offset rising operating costs and the increasing costs of reinvestment in the District's aging water transmission and distribution infrastructure.

The District anticipates the need to consider future annual water rate increases to fund replacement of portions of the District's 265 miles of underground water mains and to pay the continually-rising operating costs of the District while maintaining financial reserves to comply with debt covenants and to provide funds for emergencies or catastrophic losses. The financial plan adopted by the Board of Directors in FY2013 contemplates water rate increases in the 3 percent range every year through FY2018. However, water rates for years beyond FY2015 have not been adopted by the Board of Directors.

2015 OPERATING BUDGET SUMMARY

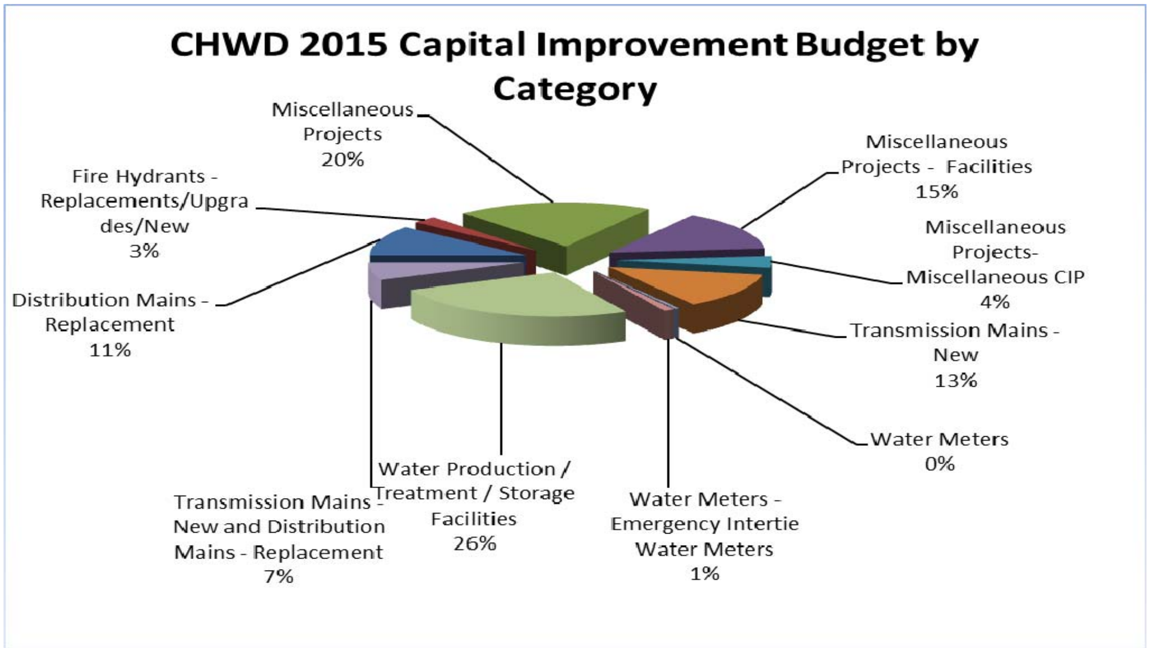
Expense Category	*2015 Adopted Budget*	*% Change 2015 vs. 2014*
Benefits	$ 652,658	-4.48%
Customer Service & Administration	1,834,870	-4.22%
Debt Service	736,488	-0.94%
Depreciation, Capital Improvement and Rate Stabilization Expense	1,949,000	3.18%
Pumping and Well Maintenance	200,723	42.11%
Transmission and Distribution	1,723,790	2.25%
Water Demand Management	280,130	5.79%
Water Purchases	2,295,483	-2.79%
	$9,673,142	-0.12%

CHWD 2015 Operating Budget by Category



2015 Capital Projects Budget Summary

Category	Project Budget	Prior years additonal cost approval	2015 New Capital Project Total	2015 Capital Projects Approved
Distribution Main -Replacement / Rehabilitation and New	$ 33,469	$ -	$ -	$ -
Distribution Mains - Replacement	2,015,454	21,978	271,621	293,599
Fire Hydrants - Replacements/Upgrades/New	173,738	-	173,738	173,738
Miscellaneous Projects	1,873,588	-	1,423,588	1,423,588
Miscellaneous Projects - Facilities	1,131,872	336,993	-	336,993
Miscellaneous Projects- Miscellaneous CIP	291,629	-	291,761	291,761
Transmission Mains - New	1,064,993	(47,125)	12,680	(34,445)
Transmission Mains - New and Distribution Mains - Replacement	471,102	(1,633)	-	(1,633)
Water Meters	28,441	-	28,441	28,441
Water Meters - Emergency Intertie Water Meters	121,937	3,290	-	3,290
Water Production / Treatment / Storage Facilities	2,749,882	(831,588)	51,829	(779,759)
Grand Total	**$ 9,956,104**	**$ (518,085)**	**$ 2,253,658**	**$ 1,735,573**



CITRUS HEIGHTS WATER DISTRICT

BALANCE SHEETS

December 31, 2014 and 2013

	2014	2013
ASSETS AND DEFERRED OUTFLOWS		
CURRENT ASSETS		
Cash and investments	$ 9,240,707	$ 10,018,613
Accounts receivable	1,901,082	1,879,615
Due from other governments	1,173	
Accrued interest receivable	4,186	4,203
Inventory	297,799	314,643
Prepaid expenses and other assets	452,594	411,532
TOTAL CURRENT ASSETS	11,897,541	12,628,606
RESTRICTED ASSETS		
Restricted cash and investments	536,963	536,973
CAPITAL ASSETS, NET	50,782,462	47,548,396
TOTAL ASSETS	63,216,966	60,713,975
DEFERRED OUTFLOWS		
Deferred amount from refunding debt	75,042	88,093
TOTAL ASSETS AND DEFERRED OUTFLOWS	$ 63,292,008	$ 60,802,068
LIABILITIES, DEFERRED INFLOWS, AND NET POSITION		
CURRENT LIABILITIES		
Accounts payable	$ 496,440	$ 417,934
Retentions payable	21,824	
Accrued payroll	29,812	39,819
Accrued interest payable	73,557	74,677
Deposits payable	300,771	263,899
Current portion of long-term liabilities	679,172	742,393
TOTAL CURRENT LIABILITIES	1,601,576	1,538,722
LONG-TERM LIABILITIES		
Long-term debt	4,912,305	5,467,125
Accrued other postemployment benefits	632,800	535,000
Compensated absences	214,002	172,363
TOTAL LONG-TERM LIABILITIES	5,759,107	6,174,488
TOTAL LIABILITIES	7,360,683	7,713,210
DEFERRED INFLOWS		
Deferred amount from refunding debt	30,497	29,172
NET POSITION		
Net investment in capital assets	45,931,665	42,108,244
Restricted for debt service	536,963	536,973
Unrestricted	9,432,200	10,414,469
TOTAL NET POSITION	55,900,828	53,059,686
TOTAL LIABILITIES, DEFERRED INFLOWS, AND NET POSITION	$ 63,292,008	$ 60,802,068

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

CITRUS HEIGHTS WATER DISTRICT

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

For the Years Ended December 31, 2014 and 2013

	2014	2013
OPERATING REVENUES		
Water sales	$ 10,171,473	$ 10,905,197
Connection and other fees	1,159,828	452,889
TOTAL OPERATING REVENUES	11,331,301	11,358,086
OPERATING EXPENSES		
Customer service, administration and general	2,752,172	2,763,786
Water purchases	1,984,921	2,322,002
Transmission and distribution	1,282,941	1,289,768
Pumping and well maintenance	239,344	133,950
Conservation	99,235	88,817
Depreciation and amortization	2,003,488	1,898,303
TOTAL OPERATING EXPENSES	8,362,101	8,496,626
NET INCOME FROM OPERATIONS	2,969,200	2,861,460
NON-OPERATING REVENUES (EXPENSES)		
Investment income	15,547	24,586
Miscellaneous income	12,716	13,616
Grant revenue	10,310	3,178
Interest expense	(195,210)	(206,480)
(Loss) gain on disposal of capital assets	(30,669)	1,595
TOTAL NON-OPERATING REVENUES (EXPENSES)	(187,306)	(163,505)
CAPITAL CONTRIBUTIONS		
Contributed assets	59,248	70,657
TOTAL CAPITAL CONTRIBUTIONS	59,248	70,657
CHANGE IN NET POSITION	2,841,142	2,768,612
Net position at beginning of year	53,059,686	50,291,074
NET POSITION AT END OF YEAR	$ 55,900,828	$ 53,059,686

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

CITRUS HEIGHTS WATER DISTRICT

STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 2014 and 2013

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash receipts from customers	$ 11,346,706	$ 11,166,550
Cash paid to suppliers for goods and services	(4,342,498)	(4,366,169)
Cash paid to employees for services	(1,904,291)	(1,968,456)
NET CASH PROVIDED BY OPERATING ACTIVITIES	5,099,917	4,831,925
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Receipts from other net nonoperating revenues	21,853	207,702
NET CASH PROVIDED BY NONCAPITAL FINANCING ACTIVITIES	21,853	207,702
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Purchase or construction of capital assets	(5,224,550)	(3,399,403)
Payments on long-term debt	(510,000)	(530,000)
Proceeds from the issuance of long-term debt		
Interest paid on capital debt	(231,150)	(245,260)
Proceeds from disposal of capital assets	50,450	29,771
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	(5,915,250)	(4,144,892)
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment income received	15,564	25,653
NET CASH PROVIDED BY INVESTING ACTIVITIES	15,564	25,653
NET (DECREASE)/INCREASE IN CASH AND CASH EQUIVALENTS	(777,916)	920,388
Cash and cash equivalents at beginning of year	10,555,586	9,635,198
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 9,777,670	$ 10,555,586
Cash and cash equivalents consist of the following:		
Unrestricted	$ 9,240,707	$ 10,018,613
Restricted	536,963	536,973
	$ 9,777,670	$ 10,555,586

(Continued)

CITRUS HEIGHTS WATER DISTRICT

STATEMENTS OF CASH FLOWS (Continued)

For the Years Ended December 31, 2014 and 2013

	2014	2013
RECONCILIATION OF NET INCOME FROM OPERATIONS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net income from operations	$ 2,969,200	$ 2,861,460
Adjustments to reconcile net income from operations to net cash provided by operating activities:		
Depreciation and amortization	2,003,488	1,898,303
Changes in assets and liabilities:		
Accounts receivable	(21,467)	(210,996)
Inventory	16,844	30,565
Prepaid expenses and other assets	(41,062)	260,699
Accounts payable	78,506	(23,030)
Accrued payroll	(10,007)	(53,143)
Deposits payable	36,872	19,460
Accrued other postemployment benefits	97,800	100,152
Compensated absences	(31,582)	(51,545)
Deferred amount from refunding debt	1,325	
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 5,099,917	$ 4,831,925
SUPPLEMENTAL DISCLOSURE OF NON-CASH ACTIVITIES		
Receipt of contributed assets	$ 59,248	$ 70,657

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

NOTE A – REPORTING ENTITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of the Citrus Heights 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. The District is accounted for as an enterprise fund and applies all applicable GASB pronouncements in its accounting and reporting. In addition, the District follows Financial Accounting Standards Board pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. The more significant of the District's accounting policies are described below.

Reporting Entity: The District was established on October 25, 1920 as an irrigation district under Division 11 of the Act of Legislature of the State of California. The District constructs and maintains waterworks and supplies domestic water in an area of approximately 12 square miles to about 19,600 connections in Sacramento and Placer counties with an estimated population of 66,000. The District is governed by a Board of Directors consisting of three directors elected by residents of the District. The accompanying basic financial statements present the District and its component unit. The component unit discussed below is included in the District's reporting entity because of the significance of its operational and financial relationship with the District.

The District has created the Citrus Heights Water District Financing Corporation (the Corporation) to provide assistance to the District in the issuance of debt. Although legally separate from the District, the Corporation is reported as if it were part of the primary government because it shares a common Board of Directors with the District and its sole purpose is to provide financing to the District under the debt issuance documents of the District. Debt issued by the Corporation is reflected as debt of the District in these financial statements. The Corporation has no other transactions and does not issue separate financial statements.

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 position 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, deferred outflows, liabilities, and deferred inflows associated with the operation of this fund are included on the balance sheet. Net position is 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 position.

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. Grant revenue is recognized when program expenditures are incurred in accordance with program guidelines. When such funds are received they are

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

recorded as unearned revenue until earned. Earned but unbilled water services are accrued as revenue. Water lines are constructed by private developers and then dedicated to the District, which is then responsible for their future maintenance. These lines are recorded as capital contributions when they pass inspection by the District and the estimated costs are capitalized as donated pipelines.

Operating revenues and expenses consist of those revenues and expenses that result from the ongoing principal operations of the District. Operating revenues consist primarily of charges for services. Non-operating revenues and expenses 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 and restricted and unrestricted investments in money market mutual funds and LAIF.

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.

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.

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 the following estimated useful lives:

Description	Estimated Life
Pipeline and infrastructure	20-40 years
Equipment and machinery	5-10 years
Buildings	15-40 years
Well improvements	40 years
Donated pipelines	40 years
Improvements	40 years

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

Depreciation expense aggregated $1,990,437 and $1,886,578 for the years ended December 31, 2014 and 2013, 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 a cost of more than $1,000 for tangible personal property and $3,000 for infrastructure, building or improvements. 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.

Bond Premiums and Bond Issuance Costs: Bond premiums 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 recognized as an expense in the period incurred.

Deferred Amount from Refunding Debt: The difference between the reacquisition price of refunded debt and the net carrying amount of the previously outstanding debt is deferred and reported as either a deferred outflow or deferred inflow on the balance sheet. These amounts are amortized over the shorter of the term of the old debt or the new debt.

Compensated Absences: The District's policy allows employees to accumulate earned but unused annual leave, management leave and compensatory time-off which will be paid to employees upon separation from the District's service. The cost of annual leave, management leave and compensatory time-off is recognized in the period earned.

Upon death while employed by the District or retirement from the District, employees are paid one-third of their accumulated sick leave time. This amount is also recognized in the period earned.

New Pronouncements: In June 2012, the GASB approved Statement No. 68, *Accounting and Financial Reporting for Pensions*. This Statement requires governments providing defined benefit pension plans to recognize their long-term obligation for pension benefits as a liability on the statement of net position and to more comprehensively and comparably measure the annual costs of pension benefits. This Statement also requires revised and new note disclosures and required supplementary information (RSI) to be reported by employers. The implementation of this GASB Statement will have a significant impact on the District's financial statements and is effective for the District's December 31, 2015 financial statements.

NOTE B – CASH AND INVESTMENTS

Cash and investments as December 31, 2014 and 2013 are classified in the accompanying financial statements as follows:

	2014	2013
Cash and cash equivalents	$ 9,240,707	$ 10,018,613
Restricted cash and investments	536,963	536,973
Total cash and investments	$ 9,777,670	$ 10,555,586

NOTE B – CASH AND INVESTMENTS (Continued)

Cash and investments as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
Cash on hand	$ 550	$ 550
Deposits with financial institutions	2,716,364	3,509,732
Total cash	2,716,914	3,510,282
Investments in Local Agency Investment Fund (LAIF)	6,523,793	6,508,331
Held by fiscal agent:		
Money market mutual fund	536,963	536,973
Total investments	7,060,756	7,045,304
Total cash and investments	$ 9,777,670	$ 10,555,586

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 (or the District's investment policy, where more restrictive) 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 December 31, 2014, 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	5 years	None	None
U.S. Treasury Obligations	5 years	None	None
U.S. Agency Securities	5 years	None	None
State of California obligations	5 years	None	None
Bankers Acceptances	180 days	40%	30%
Commercial Paper	270 days	40%	10%
Negotiable Certificates of Deposits	5 years	30%	None
Repurchase Agreements	92 days	20%	None
Medium Term Corporate Notes	5 years	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.

NOTE B – CASH AND INVESTMENTS (Continued)

The District complied with the provisions of the California Government Code (or the District's investment policy, where more restrictive) 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: Investment 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 Certificates of Participation debt agreements contain certain provisions that address interest rate risk and credit risk, but not concentration of credit risk.

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
Bankers Acceptances	1 year	None	None
Commercial Paper	None	None	None
Certificates of Deposits	None	None	None
Investment Agreements	None	None	None
Repurchase Agreements	None	None	None
Money Market Mutual Funds	N/A	None	None
LAIF	N/A	None	None

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 in 12 months or less.

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	$ 6,523,793		$ 6,523,793
Held by bond trustee:				
Money market mutual funds	AAA	536,963	$ 536,963	
		$ 7,060,756	$ 536,963	$ 6,523,793

NOTE B – CASH AND INVESTMENTS (Continued)

Concentration of Credit Risk: The investment policy of the District limits the amount that can be invested in any one issuer to the lesser of the amount stipulated by the California Government Code or 50% of total investments, with the exception of U.S. Treasury obligations, U.S. Agency Securities and LAIF. There are no investments in any one issuer (other than mutual funds and external investment pools) that represent 5% or more of total District investments.

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.

At December 31, 2014, the carrying amount of the District's deposits were $2,716,364 and the balances in financial institutions were $2,767,357. Of the balance in financial institutions, $780,382 was covered by federal depository insurance and $1,986,975 was collateralized as required by State law (Government Code Section 53630), by the pledging financial institution with assets held in a common pool for the District and other governmental agencies, but not in the name of the District. As of December 31, 2014, 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	$ 536,963

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 $60,268,887,722 managed by the State Treasurer. Of that amount, 1.32% is invested in structured notes and asset-backed 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 December 31, 2014 and 2013 are as follows:

	Balance January 1, 2014	Additions	Deletions	Transfers	Balance December 31, 2014
Capital assets not being depreciated:					
Land	$ 955,683				$ 955,683
Right of ways	26,080				26,080
Construction in progress	1,261,705	$ 2,140,051		$ (1,016,179)	2,385,577
Total capital assets, not being depreciated	2,243,468	2,140,051		(1,016,179)	3,367,340
Capital assets being depreciated:					
Capacity entitlements	5,636,711				5,636,711
Improvements	55,847				55,847
Pipelines and infrastructure	44,280,594	2,758,687	$ (159,183)	1,016,179	47,896,277
Equipment and machinery	2,904,443	236,327	(173,689)		2,967,081
Buildings and improvements	1,466,585				1,466,585
Well improvements	4,747,168	111,310			4,858,478
Donated pipelines	16,005,039	59,247			16,064,286
Total capital assets, being depreciated	75,096,387	3,165,571	(332,872)	1,016,179	78,945,265
Less accumulated depreciation for:					
Capacity entitlements	(1,684,579)				(1,684,579)
Improvements	(35,527)	(783)			(36,310)
Pipelines and infrastructure	(15,807,753)	(1,254,637)	94,680		(16,967,710)
Equipment and machinery	(2,144,421)	(157,676)	157,073		(2,145,024)
Buildings	(658,699)	(40,012)			(698,711)
Well improvements	(1,044,132)	(123,155)			(1,167,287)
Donated pipelines	(8,416,348)	(414,174)			(8,830,522)
Total accumulated depreciation	(29,791,459)	(1,990,437)	251,753		(31,530,143)
Total capital assets, being depreciated, net	45,304,928	1,175,134	(81,119)	1,016,179	47,415,122
Capital assets, net	$ 47,548,396	$ 3,315,185	$ (81,119)	$ -	$ 50,782,462

NOTE C – CAPITAL ASSETS (Continued)

	Balance January 1, 2013	Additions	Deletions	Transfers	Balance December 31, 2013
Capital assets not being depreciated:					
Land	$ 824,210	$ 131,473			$ 955,683
Right of ways	26,080				26,080
Construction in progress	1,107,744	1,005,554		$ (851,593)	1,261,705
Total capital assets, not being depreciated	1,958,034	1,137,027		(851,593)	2,243,468
Capital assets being depreciated:					
Capacity entitlements	5,636,711				5,636,711
Improvements	55,847				55,847
Pipelines and infrastructure	41,649,675	1,879,665	$ (92,257)	843,511	44,280,594
Equipment and machinery	2,689,194	356,407	(141,158)		2,904,443
Buildings and improvements	1,461,146	5,939	(500)		1,466,585
Well improvements	4,718,721	20,365		8,082	4,747,168
Donated pipelines	15,934,382	70,657			16,005,039
Total capital assets, being depreciated	72,145,676	2,333,033	(233,915)	851,593	75,096,387
Less accumulated depreciation for:					
Capacity entitlements	(1,684,579)				(1,684,579)
Improvements	(34,745)	(782)			(35,527)
Pipelines and infrastructure	(14,694,003)	(1,179,908)	66,158		(15,807,753)
Equipment and machinery	(2,151,188)	(132,814)	139,581		(2,144,421)
Buildings	(619,662)	(39,037)			(658,699)
Well improvements	(922,324)	(121,808)			(1,044,132)
Donated pipelines	(8,004,119)	(412,229)			(8,416,348)
Total accumulated depreciation	(28,110,620)	(1,886,578)	205,739		(29,791,459)
Total capital assets, being depreciated, net	44,035,056	446,455	(28,176)	851,593	45,304,928
Capital assets, net	$ 45,993,090	$ 1,583,482	$ (28,176)	$ -	$ 47,548,396

Capacity Entitlements: From 1993 through 1998, the District participated with four other water agencies in a cooperative transmission pipeline project for the construction of additional transmission pipeline facilities. The District's share of these pipeline costs totaled $5,636,711. The Capacity Entitlements asset represents the capacity rights the District has purchased in the cooperative transmission pipeline project owned by San Juan Water District. The asset is being amortized over the pipeline estimated useful life of forty years.

NOTE D – LONG-TERM LIABILITIES

Long-term liabilities consist of the following:

2010 Certificates of Participation: In 2010, the District issued $5,155,000 of Revenue Certificates of Participation (Certificates) with an interest rate of 4.00%. These 2010 Certificates were issued to refund certificates to finance certain capital improvements to the District's water system. The District is required to collect rates and charges from its water system that will be sufficient to yield net revenues equal to 110% of debt service payments on any future debt issued and to deposit the net revenues in a revenue fund pledged for such future debt service payments. Annual principal payments, ranging from $450,000 to $545,000 are due on September 28 through September 28, 2020 and semi-annual interest payments, ranging from $10,900 to $59,600 are due on March 28 and September 28 through September 28, 2020.

2012 Revenue Refunding Bonds: In April 2012, the District issued $2,275,000 of Revenue Refunding Bonds with interest rates ranging from 3.00% to 5.25%. These 2012 Revenue Refunding Bonds were issued to refund the 2003 Certificates of Participation, which were issued to finance the cost of certain capital improvements to the District's water system. The District is required to collect rates and charges from its water system that will be sufficient to yield net revenues equal to 110% of debt service payments on any future debt issued and to deposit the net revenues in a revenue fund pledged for such future debt service payments. Annual principal payments, ranging from $70,000 to $160,000 are due on February 1 through February 1, 2033 and semi-annual interest payments, ranging from $4,200 to $48,600 are due on February 1 and August 1 through February 1, 2033.

The activity of the District's long-term liabilities during the years ended December 31, 2014 and 2013 was as follows:

	Balance January 1, 2014	Additions	(Reductions)	Balance December 31, 2014	Due Within One Year
2010 Certificates of Participation	$ 3,415,000		$ (435,000)	$ 2,980,000	$ 450,000
2012 Revenue Refunding Bonds	2,170,000		(75,000)	2,095,000	70,000
Less: Unamortized premiums	392,125		(34,820)	357,305	
	5,977,125		(544,820)	5,432,305	520,000
Accrued other postemployment benefits (OPEB)	535,000	$ 123,901	(26,101)	632,800	
Compensated absences	404,756	41,639	(73,221)	373,174	159,172
	$ 6,916,881	$ 165,540	$ (644,142)	$ 6,438,279	$ 679,172

NOTE D – LONG-TERM LIABILITIES (Continued)

	Balance January 1, 2013	Additions	(Reductions)	Balance December 31, 2013	Due Within One Year
2010 Certificates of Participation	$ 3,840,000		$ (425,000)	$ 3,415,000	$ 435,000
2012 Revenue Refunding Bonds	2,275,000		(105,000)	2,170,000	75,000
Less: Unamortized premiums	426,944		(34,819)	392,125	
	6,541,944		(564,819)	5,977,125	510,000
Accrued other postemployment benefits (OPEB)	434,848	$ 116,968	(16,816)	535,000	
Compensated absences	456,301	22,360	(73,905)	404,756	232,393
	$ 7,433,093	$ 139,328	$ (655,540)	$ 6,916,881	$ 742,393

The annual requirements to amortize the outstanding debt as of December 31, 2014 are as follows:

	2010 Certificates of Participation			2012 Revenue Refunding Bonds		
For the Year Ended December 31:	Principal	Interest	Total	Principal	Interest	Total
2015	$ 450,000	$ 119,200	$ 569,200	$ 70,000	$ 96,238	$ 166,238
2016	470,000	101,200	571,200	75,000	94,063	169,063
2017	485,000	82,400	567,400	80,000	91,338	171,338
2018	505,000	63,000	568,000	80,000	87,938	167,938
2019	525,000	42,800	567,800	85,000	84,862	169,862
2020-2024	545,000	21,800	566,800	500,000	359,037	859,037
2025-2029				605,000	238,556	843,556
2030-2033				600,000	64,837	664,837
	$ 2,980,000	$ 430,400	$ 3,410,400	$ 2,095,000	$ 1,116,869	$ 3,211,869

Pledged Revenue: The District pledged future water system revenues, net of specified expenses, to repay the 2012 Revenue Refunding Bonds in the original amount of $2,275,000. Proceeds of the Revenue Refunding Bonds were used to refund the 2003 Certificates of Participation to finance capital improvements to the District's water system. The Revenue Refunding Bonds are payable solely from water customer net revenues and are payable through February, 2033. 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 Revenue Refunding Bonds was $3,211,869 and $3,384,909 at December 31, 2014 and 2013, respectively.

The District pledged future water system revenues, net of specified expenses, to repay the 2010 Certificates of Participation in the original amount of $5,155,000. Proceeds of the Certificates of Participation funded the acquisition and construction of certain facilities, as indicated above. The Certificates of Participation are payable solely from water customer net revenues and are payable through September, 2020. Annual principal and interest payments on the Certificates of Participation are expected to require less than 80% of net revenues. Total principal and interest remaining to be paid on the Certificates of Participation was $3,410,400 and $3,977,650 at December 31, 2014 and 2013, respectively.

NOTE D – LONG-TERM LIABILITIES (Continued)

Total principal and interest paid on all debt payable from net revenues was $739,660 and $770,688 and the total water system net revenues were $4,926,354 and $4,823,936 for the years ended December 31, 2014 and 2013, respectively. At December 31, 2014 and 2013, the District's net revenues were 666% and 621% 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 December 31, 2014 and 2013.

NOTE F – NET POSITION

Restrictions: Restricted net position 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 position at December 31, 2014 and 2013 consisted of the debt service reserve on the 2010 Certificates of Participation. The restrictions represent debt service and other reserves required by the related debt covenants.

Designations: Designations of unrestricted net position may be imposed by the Board of Directors to reflect future spending plans or concerns about the availability of future resources. Designations may be modified, amended or removed by Board action. Designations included the following as of December 31:

	2014	2013
Rate stabilization	$ 1,000,000	$ 1,000,000
Operating reserve	2,835,989	3,085,466
Depreciation reserve capital improvements	983,540	(621,260)
Capital improvement reserve	656,208	627,185
Fleet equipment reserve	290,636	400,229
Employment-related benefits reserve	316,968	423,120
Total	$ 6,083,341	$ 4,914,740

The designations are for the following:

Designated for rate stabilization represents the amount to be used to ensure financial and customer rate stability in responding to certain conditions.

Designated for operating reserve is maintained for operating funds collected in advance for the following year, accrued leave reserve, self-insurance reserve, unanticipated operating expenses, unanticipated economic shortfall and unallocated funds.

NOTE F – NET POSITION

Designated for depreciation reserve represents amounts set aside to replace or rehabilitate capital facilities at the end of their useful life.

Designated for capital improvement reserve represents amounts set aside for use in evaluating and constructing new capital facilities to benefit existing District customers. This reserve had a negative balance in past years due to large capital expenditures, including the meter retrofit program and well construction.

Designated for fleet equipment reserve represents amounts set aside to replace fleet equipment at the end of its useful life.

Designated for employment-related benefits reserve represents amounts set aside to pay the costs of employment-related benefits for existing and retired District employees.

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. California Public Employees' Pension Reform Act of 2012 (PEPRA) became law during the current fiscal year. Effective January 1, 2013, newly hired employees' pension benefits are governed by PEPRA, subject to limited exceptions. PEPRA employees have lower benefits and more pension cost sharing than employees hired prior to January 1, 2013. 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 requires agencies with less than 100 active members in the plan to participate in the risk pool. All full and part-time District 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 either their highest twelve consecutive months full-time equivalent monthly pay for employees with the Tier 1 benefit, or their highest 36 consecutive months full-time equivalent monthly pay for employees with the Tier 2 or PEPRA plan. 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 non-PEPRA plan members are required to contribute 7% and active PEPRA plan members are required to contribute 6.25% of their annual covered salary. The District makes the contributions required of non-PEPRA plan members on their behalf and for their account. The amount paid by the District on behalf of the employees was $149,604 during 2014 and $143,328 during 2013. The District is required to contribute at an actuarially determined rate. The required employer contribution rate for 2012/13 was 17.831%, for 2013/14 was 18.959%, and for 2014/15 was 20.612%. 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 December 31, 2014, 2013 and 2012 were $464,401, $428,425, and $400,048, respectively, which were equal to the required contributions each year.

NOTE H – OTHER POST-RETIREMENT BENEFITS

Plan Description: The District administers a single-employer defined benefit other postemployment healthcare (OPEB) plan providing health plan coverage to eligible retired employees and their eligible dependents. The District offers retirees the option to obtain coverage under the same medical plans as its active employees if such coverage is offered by the health insurer. Employees become eligible to retire and receive healthcare benefits with at least 20 years of service to the District. The OPEB Plan does not issue a publicly available financial report.

Funding Policy: The contribution requirements of plan members and the District are established and may be amended by the Board of Directors. The required contribution is based on projected pay-as-you-go financing requirements. For 2014 and 2013, the District contributed $26,101 and $16,816, respectively, to the plan.

Annual OPEB Cost and Net OPEB Obligation: The District's annual OPEB cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The following table shows the components of the District's annual OPEB cost for 2014 and 2013, the amount actually contributed to the plan, and changes in the District's net OPEB obligation to the OPEB plan:

	2014	2013
Normal cost	$ 61,705	$ 58,640
Amortization of unfunded AAL	62,118	58,250
Annual required contribution	123,823	116,890
Interest and amortization of net OPEB obligation	78	78
Contributions made (premium payments made)	(26,101)	(16,816)
Change in net OPEB obligation	97,800	100,152
Net OPEB obligation, beginning of year	535,000	434,848
Net OPEB obligation, end of year	$ 632,800	$ 535,000

The District's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2014, 2013, and 2012 were as follows:

Year Ended	Annual OPEB	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
December 31, 2012	$ 120,000	17.97%	$ 434,848
December 31, 2013	116,890	14.39%	535,000
December 31, 2014	123,823	21.08%	632,800

Funded Status and Funding Progress: As of December 31, 2012, the most recent actuarial valuation date, the actuarial accrued liability for benefits was $1,414,800, all of which was unfunded. The covered payroll (annual payroll of active employees covered by the plan) was $2,266,500, and the ratio of the UAAL to the covered payroll was 62.42%.

NOTE H – OTHER POST-RETIREMENT BENEFITS (Continued)

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information below, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions: Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets consistent with the long-term perspective of the calculations.

In the December 31, 2012 actuarial valuation, the projected unit credit actuarial method was used. The actuarial assumptions included a 4.25% investment rate of return (net of administrative expenses), which is based on the District's own investments. The annual healthcare-cost trend rates are as follows: for medical premiums, 5% per year; for dental premiums, 4.00% per year. The assumptions also include a 3.25% annual increase in covered payroll and a 3% inflationary factor. The UAAL is being amortized as a level percentage of projected payroll on an open basis. The remaining amortization period at December 31, 2012, was 30 years.

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL)-Simplified Entry Age (b)	Unfunded AAL (Uaal) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of /Covered Payroll ((b-a)/c)
December 31, 2009	-	$ 1,449,500	$ 1,449,500	-	$ 2,154,000	67.29%
December 31, 2012	-	$ 1,414,800	$ 1,414,800	-	$ 2,266,500	62.42%

NOTE I – COMMITMENTS AND CONTINGENCIES

Various claims have been filed against the District. In the opinion of the District's management and legal counsel, the claims will not have a material impact on the basic financial statements.

The District has capital project commitments as of December 31, 2014 totaling $765,424 related to construction work.

NOTE J – ECONOMIC DEPENDENCY

During 2014 and 2013, the District purchased 84.86% and 96.87%, respectively, of its water supply from the San Juan Water District (SJWD). Total purchases for the year ended December 31, 2014 and 2013 was $1,984,921 and $2,322,002. In addition, the District owns water transmission capacity entitlements through the cooperative transmission pipeline project owned and operated by SJWD.

NOTE K – 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, fidelity insurance and workers compensation liability. 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)	$ 2,000,000	$ 58,000,000	None
Property Damage	50,000	100,000,000	$ 1,000 - 50,000
Crime	100,000	None	1,000
Workers Compensation Liability	2,000,000	Statutory	None
Employers Liability	2,000,000	Statutory	None

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.

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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
Citrus Heights Water District
Citrus Heights, California

We have audited, in accordance with the 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, the financial statements of the Citrus Heights Water District (the District) as of and for the year ended December 31, 2014, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated April 6, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the 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 opinions 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.

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 District's financial statements will not be prevented, or detected and corrected on a timely basis. 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.

Our consideration of internal control was for the limited purpose described in the first paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that were not identified. The prior auditor identified certain deficiencies in internal control, described in the accompanying schedule of prior year findings, that they considered to be a significant deficiency as item 2009-1.

To the Board of Directors
Citrus Heights Water District

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's financial statements are free from 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*. We noted certain other matters that we reported to management of the District in a separate letter dated April 6, 2015.

The District's Response to Findings

The District's response to the findings identified in our audit are described in the accompanying schedule of current and prior year findings. The District's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

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 result of that testing, and not to provide an opinion on the effectiveness of the District'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 District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Richardson & Company, LLP

April 6, 2015

Finding 2013-1

Controls Over Financial Reporting

Reporting Requirement: Material Weakness

Criteria: Procedures need to be in place to ensure that costs added to construction in progress and the capital asset accounts can be reconciled to actual costs incurred.

Condition: In both 2012 and 2013, the District reclassified expenses to construction in progress that exceeded the actual expenditures incurred because certain expenditures were removed and capitalized twice.

Cause: The District does not have the necessary procedures to ensure that costs being removed from the expense accounts to be recorded as capital assets were not being double counted.

Effect: In 2012, construction in progress was overstated and expenses were understated by $396,275, resulting in a restatement of the prior year statement of net position. In 2013, a correcting adjusting journal entry was made in the amount of $435,865 to correct a double-posting of construction in progress costs.

Recommendation: Procedures should be put in place to enhance the District's project tracking system to ensure that the proper amounts of costs are reclassified out of expenses and into construction in progress. The District should also consider recording all project costs as additions to construction in progress and then transfer the entire project costs to the proper asset category, which may assist in ensuring that costs are not capitalized twice. Consideration should also be given to establishing separate general ledger accounts to record the entries made to capitalize certain expenditures.

Status: During 2014, the District modified its accounting for construction in progress costs by establishing a clearing account to track these costs instead of initially recording them as expenses and then reclassifying them as capital assets. This approach will ensure that capitalizable expenditures are not overlooked in an expense account.

Finding 2009 – 1

Controls Over Financial Reporting

Reporting Requirement: Significant Deficiency

Criteria: Statement on Auditing Standard No. 112, *Communicating Internal Control Related Matters Identified in an Audit* (SAS 112) applies to the District's internal control over preparation of the financial statements. The standard provides guidance to the auditor in evaluating an entity's internal controls over financial reporting.

External auditors cannot be part of an entity's internal controls, including controls over the preparation of the financial statements, and are prohibited from auditing their own work as doing so impairs their independence. Under SAS 112, an entity's inability to draft its own financial statements is an indication of a potential significant deficiency or material weakness.

The District should have the capacity to prepare full disclosure financial statements in accordance with generally accepted accounting principles (GAAP). To carry out this responsibility, an entity must have proper internal controls over financial reporting in place. Proper internal controls over financial reporting include, but are not limited to, internal controls that identify misstatements in the financial records, ensuring staff in financial reporting and related oversight roles (or outside consultants who fill reporting roles) are equipped with the necessary knowledge and abilities, and adequate design of internal control over the preparation of the financial statements.

Condition: Currently, the District relies on the external auditors to ensure its financial statements are in accordance with GAAP. In addition, the District relies on the external auditors to ensure that all necessary disclosures are included in the notes to the financial statements.

Cause: Prior to the issuance of SAS 112, the District was able to rely on the external auditors to assist with preparation of the financial statements and related notes without being subject to control deficiencies.

Effect or Potential Effect: The risk of misstatement in the financial statements increases when management is not able to apply GAAP in recording the entity's financial transactions or preparing its financial statements, including the related notes. Also, by relying on the external auditors to ensure its financial statements are in accordance with GAAP, the District is considering the external auditors a part of its internal controls over the preparation of the financial statements.

Recommendation: The District may consider the following possible actions:

- Provide training opportunities for its staff that would enable them to become more familiar with the requirements for financial statements prepared using GAAP.
- Hire an external professional experienced in preparing governmental type financial statements to confirm that the accounting records, financial statements and related disclosures are in accordance with GAAP.
- Take no action. The District may find that the costs outweigh the benefits to adhere to this standard. No action will result in a significant deficiency (or material weakness, depending on magnitude) in the District's internal controls over the preparation of the financial statements.

Management Response: The District first became aware of Statement on Auditing Standard No. 112 (SAS 112) in February 2007 during the audit for FY 2006. SAS 112 imposes a new standard that fundamentally changes the approach that Citrus Heights Water District (and thousands of other small public entities across the United States) has used for decades – having its independent auditor also prepare its financial statements. Although this Auditing Standard suggests that an entity's inability to draft its own financial statements may be a material weakness or significant deficiency, Management is confident that its internal controls are sound and that the approach used to prepare its FY 2014 financial statements is as fundamentally sound as it has been for many years before SAS 112 was issued.

Management has evaluated approaches that it can employ to comply with SAS 112. The Independent Auditor's Recommendation cites providing training opportunities for its accounting staff to enable preparation of the financial statements by District staff as one possible approach. However, by design, District financial and accounting staff members are generalists in nature. Each staff member has a broad array of functional responsibilities and as such they have never been expected to have the expertise to prepare full disclosure financial statements in accordance with generally accepted accounting principles. It is the position of Management that the level of training needed in order to attain this level of expertise is beyond what the District wishes to have its staff members undergo.

Contracting for preparation of the financial statements by a Certified Public Accountant or other qualified persons separate from the Independent Auditor has also been considered as a possible approach to comply with SAS 112. It appears that this approach would satisfy SAS 112. However, this approach also involves significant additional expense for the District to employ another individual or firm separate from the Independent Auditor to prepare its financial statements. It has been the recommendation of Management, supported by the District's Board of Directors, that the District not incur this significant additional expense simply to satisfy SAS 112.

As stated in the Recommendation for this finding, taking no action is a possible alternative to compliance with SAS 112. The District has elected to continue to employ this alternative in the preparation of its financial statements for FY 2014, and believes that this course of action best serves the District, its Board of Directors and its customers.

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To the Board of Directors
Citrus Heights Water District
Citrus Heights, California

We have audited the financial statements of the Citrus Heights Water District for the year ended December 31, 2014, and have issued our report thereon dated April 6, 2015. Professional standards require that we provide you with the information about our responsibilities under generally accepted auditing standards and, if applicable, *Government Auditing Standards,* as well as certain information related to the planned scope and timing of our audit. Professional standards also require that we communicate to you the following information related to our audit.

<u>Our Responsibility under U.S. Generally Accepted Auditing Standards (GAAS) and *Government Auditing Standards*</u>

As stated in our engagement letter dated November 29, 2010, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities.

As part of our audit, we considered the internal control of the District. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the District's compliance with certain provisions of laws, regulations, contracts and grants. However, providing an opinion on compliance with such provisions is not an objective of our audit.

<u>Planned Scope and Timing of the Audit</u>

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; therefore, our audit involves judgment about the number of transactions to be examined and the areas to be tested.

Our audit will include obtaining an understanding of the entity and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing, and extent of further audit procedures. Material misstatements may result from (1) errors, (2) fraudulent financial reporting, (3) misappropriation of assets, or (4) violations of laws or governmental regulations that are attributable to the entity or to acts by management or employees acting on behalf of the entity.

We performed the audit according to the planned scope previously communicated to you in our engagement letter dated November 29, 2010.

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the District are described in Note A to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year. We noted no transaction entered into by the District during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were: depreciable lives and method used to depreciate capital assets and the accrual for postemployment benefits. We evaluated the key factors and assumptions used to develop the estimates in determining that they are reasonable in relation to the financial statements taken as a whole. The accrual for postemployment benefits was determined by an actuarial valuation, which is required to be performed every three years.

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosure affecting the financial statements was the postemployment benefit disclosure in Note H to the financial statement.

The financial statement disclosures are neutral, consistent, and clear.

Report on Cash and Investments

In accordance with the District's investment policy, we confirmed the District's cash and investment account balances and tested the reconciliation of those balance to the District's records, and determined that the balance agreed. In accordance with the District Investment Policy, we verified compliance with the policies and procedures. We noted the District is in compliance with the policies and procedures.

Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements.

During the course of our audit, the following material adjusting journal entries were made:

- True-up net assets invested in capital assets net of related debt was required to reflect changes for 2014 activity.

- Revise fund balance for entries made by the District in 2014 to 2013 amounts after the 2013 audit was completed.

- Record an asset disposal.

In addition, the attached schedule summarizes uncorrected misstatement of the financial statements. Management has determined that its effect is immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

Disagreements With Management

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated April 6, 2015.

Management Consultations With Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the District's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Issues Discussed Prior to Retention of Independent Auditors

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the District's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

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

Richardson & Company, LLP

April 6, 2015

CITRUS HEIGHTS WATER DISTRICT
SUMMARY OF UNADJUSTED DIFFERENCES
YEAR ENDED DECEMBER 31, 2014

Description (Nature) of Audit Difference	Financial Statement Effect - Amount of Overstatement (Understatement) of: Total Assets	Total Liabilities	Total Equity	Net Operating Income	Net Non-Operating Income	Net Income
Under accrual of estimated year-end water billing receivable	$ (51,597)		$ (51,597)	$ (51,597)		$ (51,597)
Net Audit Differences	(51,597)		(51,597)	(51,597)		(51,597)
Financial Statement Caption Totals	63,292,008	$ 7,360,683	55,900,828	2,969,200	$ (187,306)	2,841,142
Net Audit Differences as % of Financial Statement Captions	(0.082%)	0.000%	-0.09%	(1.738%)	0.00%	(1.816%)

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To the Board of Directors and Management
Citrus Heights Water District
Citrus Heights, California

In planning and performing our audit of the financial statements of the Citrus Heights Water District (the District) as of and for the year ended December 31, 2014, 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 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 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 matters that have been included in this letter for your consideration:

<u>Capital Assets and CIP Tracking</u>

We noted accumulated depreciation on the capital asset list did not agree with that shown in the general ledger. We also noted that there was no printed support for depreciation batch entries made throughout the year. Posting of depreciation from the capital assets system to the general ledger is an automated process initiated by the Accounting Supervisor at various times throughout the year. We recommend the District reconcile the capital asset system to the general ledger whenever new assets are added and when depreciation is posted in the system to ensure that the subsidiary capital asset system matches the general ledger. This process will allow for timely resolution to any inconsistencies that may be found. In addition, we recommend that support for depreciation from the capital asset listing be printed or retained electronically whenever batch postings of depreciation are run.

<u>Management's Response</u>: District Management agrees with the Auditor's recommendation. The District will immediately adopt the practice of reconciling the capital asset system to the general ledger whenever new assets are added and when depreciation is posted in the system to endure that the subsidiary capital asset system matches the general ledger. The District will also print or retain, in electronic format, support for the depreciation from the capital asset listing whenever batch postings of depreciation are run.

<u>Valuation of Capital Asset Retirements</u>

The District is in the process of updating and repairing its water system. The removal of the existing water system items being replaced from the capital asset listing is estimated by applying the Construction Cost Index (CCI) to current replacement costs. We noted the District used the CCI from 1950 for water systems placed into service for the years 1950 to 1980, a different index was used for water systems placed into service for the years 1981 through 1990 and for the years 1992 through 1999, then individual indexes were used for the years 2000 through 2014. Since a CCI index is available for each year, we recommend that the District use the applicable CCI index for each year the initial water system was completed. The impact in the current year of not using published CCI for each individual year to determine replacement costs is immaterial; however, we recommend the District use published CCI for each individual year for future replacements to estimate the costs of the items being replaced to remove from the capital asset system.

<u>Management's Response</u>: *District Management agrees with the Auditor's recommendation. The District will immediately begin to use the published CCI for each individual year for future replacements to estimate the costs of the items being replaced to remove from the capital asset system.*

<u>Adjustments to Prior Year Amounts</u>

We noted during our 2014 audit that adjustments had been made to the 2013 amounts after that audit was completed, resulting in net position not carrying over properly for the 2014 audit. We recommend that the District not adjust prior year amounts after the audit is completed, unless a material correction is noted, and those should be discussed with the auditor prior to adjusting prior year balances.

<u>Management's Response</u>: *District Management agrees with the Auditor's recommendations. The District will refrain in the future from adjusting prior year amounts after the audit is completed unless a material correction is noted, and then those will be discussed with the auditor prior to making any adjustments.*

The following matters noted in our prior year audit warrant additional consideration:

<u>Depreciation Calculations</u>

We noted that the District's capital asset reporting software is calculating depreciation on several fully depreciated assets past the final life of the assets. These incorrect amounts are being reflected in the year to date column of the "Depreciation Ledger Class Report," but are correctly not added to the accumulated depreciation column. The accumulated depreciation totals on the report were determined to be correct, and the District subsequently adjusted the depreciation expense amounts to arrive at the proper accumulated depreciation amounts, so the District's general ledger balances were correct. However, the District should be able to rely on these annual depreciation amounts to record its depreciation expense. We provided the Accounting Supervisor with list of these assets. We recommend the District contact their capital asset software vendor to assist them in correcting these errors within the capital asset reporting software.

<u>Management's Response</u>: *District Management agrees with the Auditor's recommendation. The District will contact the software vendor to report the issue with amounts not being reflected in the year to date depreciation column and determine if there is a software update or fix that will provide a remedy for the issue.*

<u>Reliance on Excel Spreadsheets</u>

The District utilizes spreadsheets to determine the inventory balance and for capital construction project costing, as well as to report a wide range of financial and management information. This reliance on spreadsheets places the District at increased risk of data input errors. We recommend that the District investigate dedicated software applications to perform inventory and capital construction project costing. Additionally, we recommend that management establish a framework within which spreadsheet use is defined and clearly linked to other business processes.

<u>Management's Response</u>: *District Management agrees with the Auditor's recommendations to the extent that they can be implemented in a cost-effective manner. For example, District staff will explore the possibility of using functionality within its existing maintenance management system software to expand its use for inventory purposes to replace or enhance the spreadsheet that is now used. District staff has*

also recently implemented improvements in the importing and exporting of data between the financial information system (FIS) and Excel spreadsheets to reduce the likelihood of data input errors. Other dedicated software applications, particularly those that are typically integrated with the FIS may not be cost-effective to implement until such time as the District replaces the existing system. District Management will formally identify and define those Excel spreadsheets that are integral to the financial accounting process as a first step toward determining where dedicated software applications may be an appropriate and cost-effective replacement for the spreadsheets now being used.

New Pronouncements

In June 2012, the GASB approved Statement No. 68, "Accounting and Financial Reporting for Pensions." This Statement requires governments providing defined benefit pension plans to recognize their long-term obligation for pension benefits as liability on the statement of net position and to more comprehensively and comparably measure the annual costs of pension benefits. Historically, GASB's pension standards viewed the obligation to provide benefits as belonging to the plan, rather than to the employer. As a result, employers disclosed the amount of unfunded pension liability in notes to their financial statements instead of recognizing a liability on the face of the statement of net position. As the District participates in a multi-employer cost-sharing plan, the District will be required to report a liability equivalent to their proportionate share of the net pension liability of the plan as well as the related pension expense and any deferred inflows or deferred outflow of resources. Historically, the District has only included their required contributions as an expense. The preliminary information provided by CalPERS indicates that the District's share of the unfunded pension liability is $3,279,974 as of June 30, 2013, which is the latest available actuarial study. Due to the significant impact this Statement could have on the District's financial statements, we recommend that the District monitor CalPERS' progress in providing the information needed to implement this Statement.

* * * * *

We would like to take this opportunity to acknowledge the courtesy and assistance extended to us during the course of the examination. 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, LLP

April 6, 2015