

CITRUS HEIGHTS WATER DISTRICT

**Management Report
For the Year Ended December 31, 2008**

CITRUS HEIGHTS WATER DISTRICT
Management Report
For The Year Ended December 31, 2008

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Board of Directors
Citrus Heights Water District
Citrus Heights, California

In planning and performing our audit of the basic financial statements of the Citrus Heights Water District (District) for the fiscal year ended December 31, 2008, we considered its internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the basic financial statements and not to provide assurance on internal control.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control was for the limited purpose described in the first paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls. We consider the following deficiency to be a significant deficiency in internal controls as reported within the report on the District's internal control in the audit report dated March 31, 2009:

2007-1: Controls Over Financial Reporting

The memorandum that accompanies this letter summarizes our comments and suggestions concerning certain recommendations made in the District's prior year audit and current year recommendations. We previously reported on the District's internal control in our report dated March 31, 2009. This letter does not affect our report dated March 31, 2009 on the financial statements of the Citrus Heights Water District.

Board of Directors
Citrus Heights Water District
Citrus Heights, California

Citrus Heights Water District's management has provided responses to the comments described in the memorandum that accompanies this letter. We did not audit the District's responses and accordingly, we express no opinion on it.

This report is intended for the use of management, the Board of Directors, and others within the organization, and is not intended to be and should not be used by anyone other than these specified parties. We thank the District's staff for its cooperation during our audit.

Gallina LLP

Roseville, California
March 31, 2009

CITRUS HEIGHTS WATER DISTRICT

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Our Responsibility under U.S. Generally Accepted Auditing Standards and Government Auditing Standards

As stated in our engagement letter dated October 24, 2008, 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 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 Citrus Heights Water District's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our tests was not to provide an opinion on compliance with such provisions.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our engagement letter dated October 24, 2008.

Qualitative Aspects of Accounting Practices

Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the District are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year ended December 31, 2008. We noted no transactions entered into by the District during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

Significant Accounting Estimates

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

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Management Report Required Communication as of December 31, 2008

affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

- Accrual and disclosure of compensated absences: Management's estimate is based on information collected by the District using current pay rates and District's policy on employee use of compensating time-off. Our audit agreed balances reported in the financial statements to those in the District calculated spreadsheets.
- Capital asset lives and the related depreciation expense: Management's estimate is based on the District's policy of depreciating assets. We scanned asset listings for reasonable compliance to this approach.

Difficulties Encountered in Performing the Audit

We encountered no significant 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. None of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole.

Immaterial Misstatements Corrected by Management

The following misstatement was brought to the attention of, and corrected by, management:

- Grants receivable was understated by \$276,618 for anticipated grant reimbursements related to Mitchell Farms and Bonita Groundwater Well construction performed during the year ended.

Immaterial Misstatements Not Corrected by Management

Management passed on the following adjustments:

- Adjust restricted for debt service net assets by \$24,789 to agree to the restricted cash amount at December 31, 2008.

Management has determined that the effect is immaterial to the financial statements taken as a whole.

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Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the 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 March 31, 2009.

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 governmental unit'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.

Other Audit Findings or Issues

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.

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Management Report Current Year Findings and Recommendations For the Year Ended December 31, 2008

GRANTS RECEIVABLE

Criteria

During its year-end closing process, the District should enforce policies and procedures to ensure that year-end accruals are properly identified, reviewed and recorded for all account balances, including grant revenues and grant receivables.

Condition

During the Audit, we noted that grants receivable was not recorded at the end of the year despite the revenue recognition criteria being met. The amount of the audit adjustment was \$276,618.

Cause

During the year-end closing process, the District did not gather the grant revenue accrual data and record the adjustment on its general ledger. A schedule of grants receivable is maintained independent of the general ledger.

Effect of Condition

By not recording the grant revenue accrual at year-end even though eligibility requirements are met, the District could materially understate its receivables and revenue. Internal controls over financial reporting are strengthened when general ledger balances directly translate to the District's financial reports.

Recommendation

We recommend that the District implement its year-end closing process by obtaining the grant receivable adjustment and accordingly record the accrual on its general ledger.

Management's Response

District Management agrees with the Auditor's recommendation. The District has a procedure in place for recording grant revenue accrual at the time when requests are submitted for grant reimbursement, but the procedure was not followed on one occasion in 2008. This resulted in a grants receivable not being recorded at the time it was accrued. District staff has been re-instructed as to the procedure, which involves providing a copy of all grant reimbursement requests to District accounting staff at the time that such requests are prepared and submitted by any District staff member.

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Status of Prior Year Recommendations As of December 31, 2008

<u>Recommendation</u>	<u>Status</u>
<p>We recommended that the District reduce the possibility of misappropriation by restricting access or by using other compensating controls such as use of a perpetual inventory system. The District may find it costly to restrict access because of the nature of the inventory items. The implementation of a perpetual inventory system will provide compensating controls.</p>	<p>The District considered the recommendation and determined that costs to implement exceed benefits. No further action required.</p>
<p>We recommended that the District consider implementing a perpetual inventory system. This system will allow management to monitor inventory levels on hand, provide a comparison for the physical inventory count, and allow for better inventory management.</p>	<p>The District considered the recommendation and determined that costs to implement exceed benefits. No further action required.</p>