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September 19, 2019

To the Board of Directors
Volcano Community Service District

I have audited the financial statements of the governmental activities, the business- type activities, and each major fund of Volcano Community Service District for the years ended June 30, 2015, 2016, 2017, and 2018 and have issued our report thereon dated September 19, 2019. Professional standards require that I provide you with information about my responsibilities under generally accepted auditing standards (and, if applicable, *Government Auditing Standards* and OMB Circular A-133), as well as certain information related to the planned scope and timing of my audit. I have communicated such information in my letter to you dated February 5, 2019. Professional standards also require that I communicate to you the following information related to my audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by Volcano Community Service District are described in Note 2 to the financial statements. As described in Note 2 of the 2015 and 2016 financial statements, the District accounts for the hall fund and general fund separate from the water fund. I noted no transactions entered into by the District during the years 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 estimate affecting the financial statements was:

Management's estimate of the depreciation expense is based on the straight-line method of depreciating assets over the estimated useful lives of those assets. We evaluated the key factors and assumptions used to develop depreciation expense in determining that it is reasonable in relation to the financial statements taken as a whole.

Management's estimate of land value allocated to the Hall and General Fund.

Management's estimate of waived and uncollected rental fees.

The disclosures in the financial statements are neutral, consistent and clear.

Difficulties Encountered in Performing the Audit

The completion of the audit was delayed due to postponement in rental contracts being available for testing for our staff. We initially requested the rental contracts on May 1, 2019. The contracts were not provided to our office until the middle of July.

Corrected and Uncorrected Misstatements

Professional standards require me 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. The following statements detected as a result of audit procedures were corrected by management:

- Adjust beginning net position balance to agree to prior year audit report
- Record depreciation expense
- Reclassify certain equipment and improvements as capital assets
- Record prepaid expenses and accrue year end expenses
- Reclassify hall improvement donations as donation income
- Create a general fund and hall fund separate from the water fund

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. I am pleased to report that no such disagreements arose during the course of my audit.

Management Representations

I have requested certain representations from management that are included in the management representation letter dated September 19, 2019.

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 my knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

I 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 my professional relationship and my responses were not a condition to my retention.

New Accounting Pronouncements

There are significant changes to how capital and operating leases will be handled in the financial statements for the fiscal year ending June 30, 2021. While the District does not have any leases currently effected by this change, management should be aware of this change should the District enter lease agreements in the future.

Fund Accounting

Governmental accounting is organized and operated on a fund basis, based on the operational needs of the District. Funds are created and separated based on the specific activities, objectives, and restrictions of the District. This year, the financial reports report three different funds for the District. The General Fund accounts for and reports all activity not reported in another fund. The Water Fund and Hall Fund report their respective activities and assets.

Purchase of Gifts

We noted the District thanks volunteers with gift cards for services offered to the District. The California State Constitution specifically restricts the "gift of public funds". This prohibits the use of tax assessments to purchase gifts. As such these gifts have been reported in the Water Fund, as water assessments were used to purchase the gifts. As you move forward in Fund Accounting, please be aware that any future gifts must be accounted for in the Water or Hall Fund, and not the General Fund.

Website

On September 14, 2018, California approved SB- 929 Special Districts: Internet Web Sites. In an effort to create transparency between local special districts and the public, the State of California is requiring that all Special Districts develop and maintain a website by January 1, 2020. While there are limited exceptions to this law, we recommend that the Board contact the County of Amador or the Local Agency Formation Commission (LAFCO) to see what assistance is available to special districts in building and maintaining a website for the District that not only meets the requirements set in SB-929 but also allows for increased public accessibility to the District.

Water Activities

During our audit of the water activities, we noted internal control procedures of the water activities are insufficient, due to a lack of segregation of duties. The Board needs to make the following changes in respect to the water accounting to adequately address these deficiencies:

1. The Water Fund needs a separate bank account from the hall and general activities of the District.
2. The water bank statement should be reconciled by a designated member of the Board, and not Sharon. Other bank accounts may still be reconciled by Sharon.
3. The Board should implement electronic water reading/ billing software for the District. Software like UBMAX, allows to the option to use e-bill feature, make adjustments and reprint bills, and create notes in client files. Data can be exported to excel or QuickBooks. A link to the customer portal could be included on the District's website, allowing easy online bill payment for the District's water users.
4. We noted in our testing of water billings, that 15% of the sample had negative readings, which lead to billings less than the base rate. While this was not material to the financial statements, water billings should never be lower than the minimum base rate set by the District.
5. A separate budget should be prepared for the water activities within the District.

Financial Policies

One important role of the Board of Directors is to set financial policies for the District. One key financial policy every organization should have is a capitalization policy. This policy determines what new assets and major improvements will be added to the balance sheet and what will be expensed. We have enclosed a sample capitalization policy to educate the Board on what a capitalization policy should include. A typical capitalization level for similar entities is \$5,000.

The Board should also create an investment a deposit policy. It is the responsibility of the Board to be active fiscal agent of the District, setting appropriate operative and capital reserves, as well as managing the reserves to provide competitive interest rates, as well as provide the liquidity that will meet the needs of the District. As a government entity, the District is eligible to invest in the Local Agency Investment Fund managed by the State of California. In 2017 and 2018, the District received between .2- 1.09% interest on the CDs, which are held for a fixed period of time. During the same period of time LAIF offered an average interest rate of 1.376%. During 2018, the District reported \$598 in interest income. If the amount in the CDs, had been invested in LAIF, the District would have received around \$950 in interest income, as well as have the funds available within 24 hours. You can learn more about participation in LAIF online at <https://www.treasurer.ca.gov/pmia-laif/laif/index.asp>. Attached to this letter is a sample investment policy for the District to refer to, when creating an investment policy.

Audit Schedule

The state of California requires all Districts who receive tax assessments to undergo annual audits. In order to offer the most benefit to the Districts, audits should be performed in a timely manner. While the purpose of an audit is to provide a level of assurance on the financial statements, an auditor can provide many recommendations that can make the District operate more effectively. These recommendations are most beneficial when they can be implemented as quickly as possible. We recommend the District engage annual audit services, and audit be completed within six months of the close of the fiscal year, so recommendations may be implemented during the current period.

Rental Procedures

During our audit testing, we noted the procedures for rental activities are inadequate. In our testing we noted that not all rentals had signed contracts, rental activity is not promptly reported in QuickBooks, rental payments are not deposited prior to the events, and rents are reported at the amount collected, not the contract amount. Based on our testing we have the following recommendations for rental activity procedures:

1. Contracts should be numbered:
 - a. All activities held in the hall need a signed contract.
 - b. Any cancelled contracts should be retained and appropriately marked as cancelled.
 - c. Gross fees should be reported on the contract, as well as any resident (or board) fee waiver.
 - d. The district should have 3 copies of each contract- one for the renter, one for the hall manager, and one to the bookkeeper.
2. All deposits should be made PRIOR to the event:
 - a. Holding checks created an unnecessary risk that payments may be lost or uncollectible.
 - b. In order to make timely deposits, the hall manager should make rental deposits as soon as possible once the contract has been signed and payment made.
 - c. All payments should be promptly deposited- including refundable security deposits.
3. All fees should be collected by the District, in full, as required by the contract:
 - a. The District will make all commission and cleaning payments to the Hall manager after the event.
 - b. Payments for events should be made within 15 days of the close of the month after the event take place.
 - c. The Hall manager should provide a list of events for payment prior to payment from the District.
4. All rental activity needs to be reported in QuickBooks at GROSS rental fees:
 - a. All resident or board waivers should be reported separately.
 - b. Rental Activity should be reported in QuickBooks when contracts are signed- and a receivable set up, if payment is not made in full. Prepaid rental payments should be reported as a deferred revenue.
 - c. Security deposits collected should be reported in QuickBooks as a liability and refunded or credited once the event occurs.
 - d. Rental activity in Quickbooks should refer to the contract number to ease in tracking payments and rental activity.
5. A separate budget should be prepared for the Hall rental activities.

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

Very truly yours,

Cathy Castillo

Certified Public Accountant