

**HIDDEN VALLEY LAKE
COMMUNITY SERVICES DISTRICT,
CALIFORNIA**

**SINGLE AUDIT ACT
REPORTS AND SCHEDULES
FOR THE YEAR ENDED
JUNE 30, 2012**

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HIDDEN VALLEY LAKE COMMUNITY SERVICES DISTRICT
Single Audit Act
For the Year Ended June 30, 2012

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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
Hidden Valley Lake Community Services District
Middletown, California

We have audited the financial statements of the proprietary funds of Hidden Valley Lake Community Services District, California (District), as of and for the year ended June 30, 2012, which collectively comprise the District's basic financial statements and have issued our report thereon dated March 26, 2013. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

Management of the District is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

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.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying Schedule of Findings and Questioned Costs that we consider to be significant deficiencies in internal control over financial reporting. (12-FS-01, 12-FS-02 12-FS-03 and 12-FS-04) A significant deficiency is a deficiency, or 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.

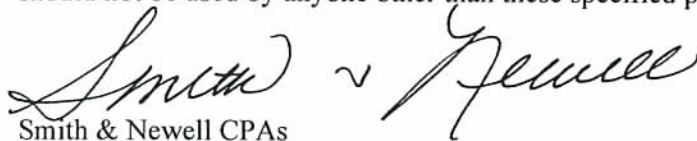
To the Board of Directors
Hidden Valley Lake Community Services District
Middletown, California

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

The District's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the District's responses, and accordingly, we express no opinion on them.

This report is intended solely for the information and use of management, the Board of Directors, others within the entity, and Federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Handwritten signatures of Smith and Newell in cursive script, with a tilde symbol between them.

Smith & Newell CPAs
Yuba City, California
March 26, 2013

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS THAT
COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND
ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB
CIRCULAR A-133**

To the Board of Directors
Hidden Valley Lake Community Services District
Middletown, California

Compliance

We have audited Hidden Valley Lake Community Services District, California's compliance with the types of compliance requirements described in the OMB Circular A-133 Compliance Supplement that could have a direct and material effect on each of the District's major federal programs for the year ended June 30, 2012. The District's major federal programs are identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the District's management. Our responsibility is to express an opinion on the District's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the District's compliance with those requirements.

In our opinion, the District complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as item 12-SA-01 and 12-SA-02.

Internal Control Over Compliance

Management of the District is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the District's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over compliance.

To the Board of Directors
Hidden Valley Lake Community Services District
Middletown, California

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

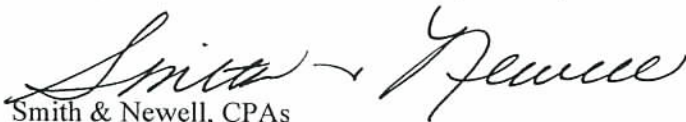
Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the proprietary fund of Hidden Valley Lake Community Services District, California, as of and for the year ended June 30, 2012, and have issued our report thereon dated March 26, 2013, which contained unqualified opinions on those financial statements. Our audit was conducted for the purposes of forming our opinions on the financial statements that collectively comprise the District's financial statements. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedule of Expenditures of Federal Awards is fairly stated in all material respects in relation to the financial statements as a whole.

The District's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the District's responses, and accordingly, we express no opinion on them.

The purpose of this report is solely to describe the scope of our testing of compliance with the types of compliance requirements applicable to each of the District's major programs and our testing of internal control over compliance and the results of our testing, and to provide an opinion on the District's compliance but not to provide an opinion on the effectiveness of the District's internal control over compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the District's compliance with requirements applicable to each major program and its internal control over compliance. Accordingly, this report is not suitable for any other purpose.



Smith & Newell, CPAs
Yuba City, California
March 26, 2013

HIDDEN VALLEY LAKE COMMUNITY SERVICES DISTRICT
Schedule of Expenditures of Federal Awards
For the Year Ended June 30, 2012

<u>Federal Program/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Federal Grantor/ Pass-Through Grantor Number</u>	<u>Disbursements/ Expenditures</u>
U.S. Department of Agriculture			
Direct Program:			
Water and Waste Disposal Systems for Rural Communities	10.760	-	<u>\$ 1,512,192</u>
Total U.S. Department of Agriculture			<u>1,512,192</u>
Total			<u><u>\$ 1,512,192</u></u>

See accompanying Notes to Schedule of Expenditures of Federal Awards

HIDDEN VALLEY LAKE COMMUNITY SERVICES DISTRICT
Notes to Schedule of Expenditures of Federal Awards
For the Year Ended June 30, 2012

1. REPORTING ENTITY

The accompanying Schedule of Expenditures of Federal Awards presents the activity of all federal financial assistance programs of the Hidden Valley Lake Community Services District, Middletown, California. The Hidden Valley Lake Community Services District's reporting entity is defined in Note 1 to the District's basic financial statements. All federal awards received directly from federal agencies as well as federal awards passed through other government agencies are included in the Schedule of Expenditures of Federal Awards.

2. BASIS OF ACCOUNTING

Basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements, regardless of the measurement focus applied. The accompanying schedule of expenditures of federal awards, is generally presented using the accrual basis of accounting for grants accounted for in the proprietary fund types, as described in the notes to the District financial statements. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Nonprofit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of the financial statements.

3. RELATIONSHIP TO FINANCIAL STATEMENTS

The amounts reported in the accompanying Schedule of Expenditures of Federal Awards agree, in all material respects, to amounts reported within the District's financial statements, federal award revenues are reported principally in the District's financial statements as intergovernmental revenue.

HIDDEN VALLEY LAKE COMMUNITY SERVICES DISTRICT
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2012

I. SUMMARY OF AUDITOR'S RESULTS

Financial Statements	<u>Status</u>
1. Type of auditor's report issued	Unqualified
2. Internal controls over financial reporting:	
a. Material weaknesses identified?	No
b. Significant deficiencies identified not considered to be material weaknesses?	Yes
3. Noncompliance material to financial statements noted?	No

Federal Awards

1. Internal control over major programs:	
a. Material weaknesses identified?	No
b. Significant deficiencies identified not considered to be material weaknesses?	No
2. Type of auditor's report issued on compliance for major programs:	
All major programs	Unqualified
3. Any audit findings disclosed including those that are required to be reported in accordance with OMB Circular A-133 Section 510(a)?	Yes
4. Identification of major programs:	
10.760 Water and Waste Disposal Systems for Rural Communities	
5. Dollar threshold used to distinguish between Type A and Type B programs?	\$300,000
6. Auditee qualified as a low-risk auditee under OMB Circular A-133, Section 530?	No

II. FINANCIAL STATEMENT FINDINGS

- 12-FS-01 Account Balances (Significant Deficiency)
- 12-FS-02 Fund Equity Reserves (Significant Deficiency)
- 12-FS-03 CIEDB Debt Service Coverage (Significant Deficiency)
- 12-FS-04 Year-End Closing Process (Significant Deficiency)

HIDDEN VALLEY LAKE COMMUNITY SERVICES DISTRICT
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2012

III. FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

12-SA-01	10.760	Water and Waste Disposal Systems for Rural Communities
12-SA-02	10.760	Water and Waste Disposal Systems for Rural Communities

HIDDEN VALLEY LAKE COMMUNITY SERVICES DISTRICT
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2012

12-FS-01 Account Balances (Significant Deficiency)

Condition

During our audit, we noted that various balance sheet accounts had not been adjusted to reflect current year end balances. This is a repeat of a prior year finding.

Cause

We noted that accounts receivable, assessments receivable, capital assets, accumulated depreciation, and Net OPEB obligation were not adjusted as necessary to accurately reflect current balances.

Criteria

Generally accepted accounting principles require that account balances be adjusted as necessary to reflect current balances.

Effect of Condition

Accounts were not properly adjusted prior to the start of the annual audit.

Recommendation

We recommend that the District reconcile and adjust account balances in a timely manner.

Corrective Action Plan

Prior to the close of the audit, all balance sheet accounts were reconciled and adjusted as necessary to reflect current balances.

12-FS-02 Fund Equity Reserves (Significant Deficiency)

Condition

We noted that in prior years the District had not established a reserve for connection fees. Although the District now has a reserve, the beginning carryover balance was not verified. This is a repeat of a prior year finding.

Cause

The connection fees in prior years had not been properly reserved when received.

Criteria

Generally accepted accounting principles require that revenues received that are legally restricted to be used only for specific purposes are to be appropriately reserved.

HIDDEN VALLEY LAKE COMMUNITY SERVICES DISTRICT
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2012

12-FS-02 Fund Equity Reserves (Significant Deficiency) (Continued)

Effect of Condition

The reserve for connection fees established by the District did not include a beginning carryover balance.

Recommendation

We recommend that the District review the collection of connection fees in prior years and determine an appropriate carryover balance.

Corrective Action Plan

The District will review the carryover balance established in 2007 to determine if corrective action must be taken.

12-FS-03 CIEDB Debt Service Coverage (Significant Deficiency)

Condition

We noted that the Water enterprise fund debt service coverage calculation as required by the California Infrastructure and Economic Development Bank for the fiscal year ended June 30, 2012 did not meet the requirements of section 5.06(b) of the loan document. This is a repeat of a prior year finding.

Cause

The District has been unable to increase revenues adequate to produce a net system revenue equal to 110 percent of the annual debt service.

Criteria

The California Infrastructure and Economic Development Bank loan requirements require that system revenues meet the requirement so that revenues are in an amount sufficient to be at least equal to 110 percent of the annual debt service.

Effect of Condition

The District was required to establish a water rate stabilization account within the Water enterprise fund in the amount of \$201,000 to comply with the requirements of section 5.06(b).

Recommendation

We recommend that the District analyze options to ensure full compliance with the loan requirements of the California Infrastructure and Economic Development Bank.

HIDDEN VALLEY LAKE COMMUNITY SERVICES DISTRICT
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2012

12-FS-03 CIEDB Debt Service Coverage (Significant Deficiency) (Continued)

Corrective Action Plan

This District is current on all outstanding obligations and will continue to make timely payments to CIEDB. In 2010, The District's Board of Directors adopted a multi-year rate increase to help meet debt requirements.

12-FS-04 Year End Closing Process (Significant Deficiency)

Condition

The audit fieldwork process was delayed because of significant delays in receiving critical schedules and source documents.

Cause

District accounting staff was still posting year-end closing entries in March 2013.

Criteria

Governmental Accounting Standards identify timeliness as a key characteristic and objective of financial reporting system. Financial reports should be published soon after the close of the District's fiscal year so as to balance the needs of reliable financial data with the needs of financial statements users to make timely decisions.

Effect of Condition

The audit process for the District was significantly delayed.

Recommendation

We recommend that the District develop more sufficient procedures for year-end closing processes and produce critical schedules and source documents in a timely manner so as to not delay the financial reporting of the District.

Corrective Action Plan

The District has implemented this recommendation.

HIDDEN VALLEY LAKE COMMUNITY SERVICES DISTRICT
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2012

12-SA-01

Name:	Water and Waste Disposal Systems for Rural Communities
CFDA #:	10.760
Federal Grantor:	U.S. Department of Agriculture
Pass Through Entity:	None
Award No.:	N/A
Year:	2011/2012

Condition

The District did not obtain documentation from its vendors showing that laborers were being paid prevailing wage.

Cause

The District did not obtain weekly certified payrolls from contractors.

Criteria

For federally funded construction projects that exceed \$2,000, the Davis-Bacon Act requires contractors to pay federally prescribed prevailing wages to laborers. The Act requires recipients of federal funds to obtain weekly certified payrolls from all contractors and subcontractors to ensure prevailing wages are properly paid.

Effect of Condition

Without proper internal controls, the risk increases that laborers could be paid rates that did not meet federal regulations.

Questioned Costs

We could not determine whether the actual amounts paid to laborers met Federal requirements, as no certified weekly payrolls were obtained by the District for one contractor.

Recommendation

We recommend that the District establish internal controls to ensure it complies with the requirements of the Davis-Bacon Act. We further recommend that the District obtain certified weekly payrolls for the project to determine if federal prevailing wages were paid.

Corrective Action Plan

The District has received certified payroll and has ensured that prevailing wage was paid as required.

HIDDEN VALLEY LAKE COMMUNITY SERVICES DISTRICT
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2012

12-SA-02

Name: Water and Waste Disposal Systems for Rural Communities
CFDA #: 10.760
Federal Grantor: U.S. Department of Agriculture
Pass Through Entity: None
Award No.: N/A
Year: 2011/2012

Condition

During our reconciliation of the general ledger and actual expenses to reimbursement requests we noted estimated expenses of \$27,000 claimed and the actual cost was \$25,500, and \$400 of expenses claimed as the result of an input error.

Cause

The District reported program expenses that could not be supported by expenses recorded on the general ledger or actual invoice.

Criteria

Good internal control over federal grant programs require that amounts reported and invoiced as grant expenses be based on actual expenses.

Effect of Condition

The District reported amounts as expended on the grant that could not be supported.

Questioned Costs

The District reported \$1,900 in expenses that could not be supported by expenses recorded on the general ledger or actual invoice.

Recommendation

We recommend that the District only claim reimbursement for grant expenses based on actual amounts expended.

Corrective Action Plan

The District will await response from The United States Department of Agriculture, Rural Development, USDARD, as to action necessary to correct the overstatement.

HIDDEN VALLEY LAKE COMMUNITY SERVICES DISTRICT
Status of Prior Year Recommendations
For the Year Ended June 30, 2012

<u>Audit Reference</u>	<u>Status of Prior Year Audit Recommendation</u>
11-FS-01	<p>Account Balances</p> <p>Recommendation</p> <p>We recommend that the District reconcile and adjust account balances in a timely manner.</p> <p>Status</p> <p>Not Implemented</p>
11-FS-02	<p>Fund Equity Reserves</p> <p>Recommendation</p> <p>We recommend that the District review the collection of connection fees in prior years and determine an appropriate carryover balance.</p> <p>Status</p> <p>Not Implemented</p>