MERCY SPRINGS WATER DISTRICT

INDEPENDENT AUDITOR'S REPORT
AND
FINANCIAL STATEMENTS
FEBRUARY 29, 2020

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Mercy Springs Water District
Firebaugh, California

Report on the Financial Statements

We have audited the accompanying financial statements of the Mercy Springs Water District (District), which comprise the statement of net position as of February 29, 2020, and the related statement of revenues, expenses and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements, which collectively comprise the District's basic 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 controls 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 basic financial statements based on our audit. 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, 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Mercy Springs Water District as of February 29, 2020, and the changes in its net position and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

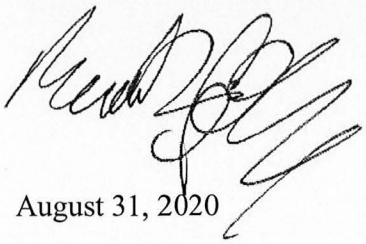
Other Matters

Required Supplementary Information

Management has omitted the management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing 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. Our opinion on the basic financial statements is not affected by this missing information.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated August 31, 2020, on our consideration of the Mercy Springs Water District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, 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 the 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.



August 31, 2020

MERCY SPRINGS WATER DISTRICT

STATEMENT OF NET POSITION
FEBRUARY 29, 2020

ASSETS	
Current assets	
Cash and investments	$ 304,429
Accounts receivable	2,217
Prepaid expense	2,121
Total current assets	308,767
Total assets	308,767
LIABILITIES	
Current liabilities	
Accounts payable and accrued expenses	-
Total current liabilities	-
Non-current liabilities	
Nonexchange guarantee	66,983
Total noncurrent liabilities	66,983
Total liabilities	66,983
NET POSITION	
Unrestricted	241,784
Total net position	$ 241,784

MERCY SPRINGS WATER DISTRICT

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
YEAR ENDED FEBRUARY 29, 2020

Operating Revenues	
Water sales	$ 361,907
Total operating revenues	361,907
Operating Expenses	
San Luis & Delta-Mendota other water costs	4,672
Purchased water	197,542
Administration	46,013
Legal and professional	8,400
Miscellaneous	1,114
Dues	19,085
Insurance	2,102
Total operating expenses	278,928
Operating income/(loss)	82,979
Nonoperating Revenues/(Expenses)	
Interest income	20
Interest expense	(3,433)
Total nonoperating revenues/(expenses)	(3,413)
Change in Net Position	79,566
Net Position	
Beginning of year, restated	162,218
End of year	$ 241,784

MERCY SPRINGS WATER DISTRICT

STATEMENT OF CASH FLOWS
YEAR ENDED FEBRUARY 29, 2020

Operating Activities		
Receipts from landowners and other districts	$	345,608
Payments to suppliers for goods and services		(410,360)
Net cash provided by (used in) operating activities		(64,752)
Non-capital Financing Activities		
Payment on nonexchange guarantee		(1,538)
Interest paid on nonexchange guarantee		(3,433)
Net cash provided by (used in) noncapital financing activities		(4,971)
Investing Activities		
Interest received		20
Net cash provided by (used in) investing activities		20
Net Increase (Decrease) in Cash		(69,703)
Cash and Investments		
Beginning of year		374,132
End of year	$	304,429
Cash Flows from Operating Activities		
Operating income (loss)	$	82,979
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:		
(Increase) Decrease in accounts receivable		2,088
(Increase) Decrease in prepaid expense		(1,261)
Increase (Decrease) in accounts payable and accrued expense		(130,171)
Increase (Decrease) in due to water users		(18,387)
Net Cash Provided by/(Used in) Operating Activities	$	(64,752)

Note 1 – Summary of Significant Accounting Policies

The financial statements of the Mercy Springs Water District (District) have been prepared in conformity with accounting principles generally accepted in the United States of America as applied to enterprise funds of governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The significant accounting principles and policies utilized by the District are described below:

Reporting Entity

The Mercy Springs Water District was formed in accordance with the provisions of the California water district statutes of the California Water Code on May 24, 1952. The purpose of the District is to supply irrigation water to approximately 1,240 acres of land located west of Firebaugh, California. The District is entitled to receive 2,842 acre feet of water each year under contract with the Bureau of Reclamation (based on 100% allocation). The governing board of the District consists of five members who elect from their membership a president, vice-president, secretary and treasurer.

Mercy Springs Water District does not have a relationship with any other related activities, organizations or functions of government which should be included in the financial reporting entity of the District as required by GASB Statement No. 14, *The Financial Reporting Entity.* In addition, the District is not a component unit of any other governmental entity.

Basis of Accounting and Measurement Focus

The District accounts for its operations in an enterprise fund using the economic resources measurement focus and the accrual basis of accounting. A fund is an accounting entity with a self-balancing set of accounts established to record the financial position and results of operations of a specific government activity. The activities of enterprise funds closely resemble those of ongoing businesses in which the purpose is to conserve and add to basic resources while meeting operating expenses from current revenues. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

An enterprise fund distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the District's principal ongoing operations. The principle operating revenues of the District are irrigation water sales, operations and maintenance charges, and standby charges. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Financial Statement Amounts

Cash and Investments – Cash and investments represent the District's cash bank accounts including, but not limited to, certificates of deposit, money market funds and cash management pools for reporting purposes in the Statement of Cash Flows. Additionally, investments with maturities of three months or less when purchased are included as cash equivalents in the Statement of Cash Flows.

Investments primarily consist of certificates of deposit with Bank of America. Investments are stated at fair value.

Note 1 – Summary of Significant Accounting Policies (Continued)

Accounts Receivable – Billed, but unpaid, services provided to individuals or non-governmental entities are recorded as accounts receivable. The Proprietary Funds include a year-end accrual for services through the end of the fiscal year which have not yet been billed. All receivables are reported at their gross value and, where appropriate, are reduced by the estimated portion that is expected to be uncollectible.

Long-Term Obligations – Long-term debt and other long-term obligations are reported as liabilities in the Proprietary Fund Statement of Net Position. Debt principal payments are reported as decreases in the balance of the liability on the Statement of Net Position.

Net Position/Fund Equity – The financial statements utilize a net position presentation. Net position is categorized as net investment in capital assets, restricted and unrestricted.

- Net Investment in Capital Assets – This category groups all capital assets, including infrastructure, into one component of net position. Accumulated depreciation and the outstanding balances of debt that are attributable to the acquisition, construction or improvement of these assets reduce the balance in this category.

- Restricted Net Position – This category presents external restrictions on net position imposed by creditors, grantors, contributors, laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation.

- Unrestricted Net Position – This category represents net position of the District not restricted for any project or other purpose.

When an expense is incurred for the purposes for which there are both restricted and unrestricted net position available, it is the District's policy to apply those expenses to restricted net position to the extent such are available and then to unrestricted net position.

Revenues and Expenses – The District distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the District's principle ongoing operations. The principle operating revenues of the District are irrigation water sales, operations and maintenance charges, and standby charges. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 expenditures/expenses during the reporting period.

Note 2 – Cash and Investments

Cash and investments are reported in the financial statements as follows:

Statement of Net Position	
Cash and investments	$ 304,429
	$ 304,429

Cash and investments as of February 29, 2020 consist of the following:

Deposits with financial institutions	$ 304,429
Total Cash and Investments	$ 304,429

Fair Value Measurements

The framework for measuring fair value provides a fair value hierarchy that categorizes the inputs to valuation techniques used to measure fair value into three levels. The fair value hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are described as follows:

Level 1: Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets that a government can access at the measurement date.

Level 2: Inputs to valuation methodology include inputs – other than quoted prices included within Level 1 – that are observable for an asset or liability, either directly or indirectly.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within a fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Note 2 – Cash and Investments (Continued)

Authorized Investments by the District

The District's investment policy and the California Government Code allows the District to invest in the following, provided the credit ratings of the issuers are acceptable to the District. The following also identifies certain provisions of the District and California Government Code that address interest rate risk, credit risk, and concentration of credit risk. The District's Investment Policy authorizes the following:

Authorized Investment Type	Maximum Maturity	Maximum Percentage of Portfolio	Minimum Credit Quality
Local District Bonds	5 Years	50%	AA
U.S. Treasury Obligations	5 Years	100%	N/A
State of California Obligations	5 Years	100%	A
California Local District Obligations	5 Years	50%	AA
U.S. Agencies	5 Years	100%	AAA
Bankers Acceptances	180 Days	40%	A
Commercial Paper	270 Days	25%	AA
Negotiable Certificates of Deposit	5 Years	30%	N/A
Repurchase Agreements	92 Days	20% of Base	A
Reverse Repurchase Agreements	5 Years	30%	A or >
Medium Term Notes	N/A	20%	N/A
Money Market Mutual Funds	5 Years	20%	AA
Collateralized Bank Deposits	2 Years	20%	None
Mortgage Pass-Through Securities	2 Years	20%	N/A
Time Deposits	N/A	No limit	None
Local Agency Investment Fund (LAIF)	N/A	30%	N/A
Non-Negotiable Certificates of Deposit	1 Year	20%	None

Disclosures Relating to 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. As of February 29, 2020 the District had no investments.

Disclosures Relating to 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.

Note 2 – Cash and Investments (Continued)

Concentration of Credit Risk

The investment policy of the District contains no limitations on the amount that can be invested in any one issuer beyond that stipulated by the California Government Code. Investments in any one issuer, other than U.S. Treasury securities, mutual funds, and external investment pools, There are no investments in any one issuer, other than U.S. Treasury securities, mutual funds, time deposits, 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 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 District deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits. As of February 29, 2020, the District's bank balance of $374,132 was exposed to custodial credit risk because it was uninsured and collaterized with securities held by the pledging financial instituion's trust department or agent, but not in the name of the District.

The custodial risk for investments is the risk that, in the event of the failure of the counterparty 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 investments. With respect to investments, custodial credit risk generally applies only to direct investments in marketable securities. Custodial credit risk does not apply to a local government's indirect investment in securities through the use of mutual funds or government investment pools.

Note 3 – Nonexchange Guarantee

On June 25, 2013, the San Luis Delta-Mendota Water Authority (the Authority) issued $37,550,000 of 2013A Revenue Refunding Bonds to refund the 2009A Series Revenue Bonds. The Series 2009A bonds were issued to fund the Delta Habitat Conservation and Conveyance Program (DHCCP) activity and the District, along with certain members of the Authority, entered into financing agreements with the Authority to pay their respective share of the bonds. The bonds are issued in the Authority's name and Westlands Water District is obligated to pay 100% for the principal and interest on the bonds when due under its DHCCP activity agreement with the Authority. The District is obligated under the DHCCP activity agreement to pay $4,965 in annual installments through 2045. The amount of the liability recognized, $68,521, is the best estimate of the discounted present value of the future outflows expected to be incurred as a result of the guarantee.

Note 3 – Nonexchange Guarantee (continued)

At February 29, 2020, the District has recorded a liability for the guarantee as follows:

	Balance March 1, 2019	Additions	Retirements	Balance February 28, 2020
DHCCP Nonexchange Financial Guarantee	68,521	-	(1,538)	66,983
Total Nonexchange Financial Guarantee	$ 68,521	$ -	$ (1,538)	$ 66,983

Future anticipated payments on the nonexchange financial guarantee are as follows:

Years ending February 28,	Nonexchange Financial Guarantee
2021	$ 1,620
2022	1,701
2023	1,782
2024	1,873
2025	1,964
2026-2030	11,410
2031-2035	14,549
2036-2040	18,558
2041-2043	13,526
	$ 66,983

Note 4 – Related Party Transactions

The District sells water to members of its Board of Directors at the same rate charged to unrelated parties.

Note 5 – Risk Management

Claims and judgements, including a provision for claims incurred but not reported, are recorded when a loss is deemed probable of assertion and the amount of the loss is reasonably determinable. As discussed above, the District has coverage for such claims.

Note 6 – Subsequent Events

The District evaluated subsequent events for recognition and disclosure through August 31, 2020, the date which these financial statements were available to be issued. Management concluded that no material subsequent events have occurred since February 29, 2020 that required recognition or disclosure in such financial statements.

Note 7 – Prior Period Adjustment

The District had a prior period adjustment of $106,180 for the understatement of accounts payable and expenses in the prior year, the net effect of this adjustment decreased net position by the same amount.

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
Mercy Springs Water District
Firebaugh, California

We have audited, 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, the financial statements of the Mercy Springs Water District (District), which comprise the statement of net position as of February 29, 2020, and the related statement of revenues, expenses and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated August 31, 2020.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Mercy Springs Water 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 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.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. 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 of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did identify a deficiency in internal control, described in the accompanying schedule of findings that we consider to be a material weakness: 2020-001.

Compliance and Other Matters

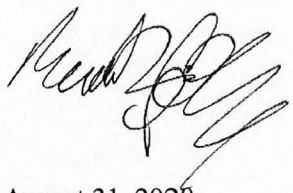
As part of obtaining reasonable assurance about whether the Mercy Springs Water District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have 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*.

Mercy Springs Water District's Response to Findings

The District's response to the findings identified in our audit is described in the accompanying schedule of 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 results of that testing, and not to provide an opinion on the effectiveness of the entity'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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



August 31, 2020

MERCY SPRINGS WATER DISTRICT

SCHEDULE OF FINDINGS
FEBRUARY 29, 2020

2020-001 - Internal Controls over Financial Reporting (Material Weakness)

Criteria:
An effective internal control system and timely financial reporting provides reasonable assurance for the safeguarding of assets, the reliability of financial information and compliance with laws and regulations.

Condition:
We have determined that processes utilized for closing and reporting of financial activity for the fiscal year ended February 29, 2020, were not effective, which contributed to the District's unpreparedness for the audit. We encountered several errors due to missing journal entries, in addition several accounts were not properly reconciled due to lack of an appropriate closing process.

Cause:
Lack of internal control procedures over financial reporting.

Effect:
The District's financial statements were materially misstated.

Recommendation:
We recommend that the District implement internal control procedures to properly close its books. These procedures may include: reconciling and balancing accounts to the general ledger, conducting a detailed review of the financial statements prior to the start of the audit fieldwork, and detailed review of all reconciliations and detailed listings to ensure accuracy.

Management's Response:

This is noted and agreed. The District will address this internal control weakness by implementing the recommendations set forth by the auditor. To effectively achieve this, the district accounting systems will be integrated into the Panoche Water District (PWD) accounting systems. The PWD administers the District and has an Accounting Policies & Procedure Manual that provides effective control through written procedures for the safeguarding of assets, the reliability of financial information, and compliance with laws and regulations.