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RAINBOW MUNICIPAL WATER DISTRICT

**REPORT ON EXAMINATION OF
FINANCIAL STATEMENTS**

FOR THE FISCAL YEAR ENDED

JUNE 30, 2014

RAINBOW MUNICIPAL WATER DISTRICT

INTRODUCTORY SECTION

JUNE 30, 2014

**RAINBOW MUNICIPAL WATER DISTRICT
TABLE OF CONTENTS
JUNE 30, 2014**

	<u>Page Number</u>
INTRODUCTORY SECTION	
Table of Contents	i
FINANCIAL SECTION	1
Report of Independent Auditors	2 - 3
Management's Discussion and Analysis	4 - 9
Statement of Net Position	10
Statement of Revenues, Expenses, and Changes in Net Position	11
Statement of Cash Flows	12 - 13
Notes to the Basic Financial Statements	14 - 26
SUPPLEMENTARY INFORMATION SECTION	27
Organization	28
Assessed Valuation	29
OTHER REPORTS OF INDEPENDENT AUDITORS SECTION	30
Report of Independent Auditors on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	31 - 32
FINDINGS AND RECOMMENDATIONS SECTION	33
Schedule of Audit Findings and Questioned Costs	34
Status of Prior Year Findings and Recommendations	35

RAINBOW MUNICIPAL WATER DISTRICT

FINANCIAL SECTION

JUNE 30, 2014



REPORT OF INDEPENDENT AUDITORS

Board of Directors
Rainbow Municipal Water District
Fallbrook, California

Report on the Financial Statements

We have audited the accompanying financial statements of Rainbow Municipal Water District, as of and for the fiscal year ended June 30, 2014, and the related notes to the financial statements, as listed in the table of contents.

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 opinions on these financial statements based on our audit. We conducted our audit 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 the State Controller's *Minimum Auditing 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 from 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 opinions.

REPORT OF INDEPENDENT AUDITORS

Page 2

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Rainbow Municipal Water District, as of June 30, 2014, and the changes in financial position and cash flows thereof for the fiscal year then ended, in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 through 9 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 October 2, 2014, on our consideration of the Rainbow Municipal 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 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 Rainbow Municipal Water District's internal control over financial reporting and compliance.

Hosaka, Rotherham & Company

San Diego, California

October 2, 2014

**RAINBOW MUNICIPAL WATER DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2014**

As management of the Rainbow Municipal Water District (District), we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended June 30, 2014. We encourage readers to consider the information presented here in conjunction with the District's basic financial statements, which begin immediately following this analysis. This annual financial report consists of two main parts (1) Management's Discussion and Analysis and, (2) Basic Financial Statements.

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments. GASB No. 34 established financial reporting standards for state and local governments, including cities, villages and special purpose governments.

FINANCIAL HIGHLIGHTS

- The District's ending total net position was \$92,048,072.
- The change in net position for the fiscal year was a decrease of \$1,045,057.
- The District had operating expenses in excess of operating revenues in the amount of \$963,514 in the current year compared to of operating revenues over expenses of \$201,669 in the previous year.
- This year the District had \$998,949 worth of net additions to capital assets compared to \$5,283,316 last year.
- The District's budget for this year showed excess revenue over expenditures (before transfers) of \$455,177 compared to the actual amount of \$1,045,057.

OVERVIEW OF FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's audit report is comprised of four components: 1) financial statements and notes, 2) supplementary information, 3) reports on compliance and internal control, and 4) findings and recommendations.

Basic financial statements. The basic financial statements include District financial statements and fund statements.

The District, as a whole, is reported in the District statements and uses accounting methods similar to those used by companies in the private sector.

The *Statement of Net Position*, a District statement, presents information on all of the District's assets, deferred outflow of resources, and liabilities, deferred inflow of resources, with the difference between the four reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

**RAINBOW MUNICIPAL WATER DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2014**

OVERVIEW OF FINANCIAL STATEMENTS (CONTINUED)

The *Statement of Revenues, Expenses and Changes in Net Position*, a District statement, presents information showing how the District's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

The *Statement of Cash Flows* provides information regarding the District's cash receipts and cash disbursements during the fiscal year.

The *Notes to the Basic Financial Statements* are included to provide more detailed data and explain some of the information in the statements.

The *Supplementary Information* gives an overview of the operations of the District and the governing body and outlines assessed property valuation.

Reports on Compliance and Internal Control encompass the independent auditor's reports showing compliance with *Government Auditing Standards* and provides additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

The *Findings and Questioned Costs* section notes material weaknesses in the system and recommendations.

DISTRICT'S FINANCIAL ANALYSIS

The District's net position decreased from the prior fiscal year by 0.9%. Revenue for this fiscal year increased 17.7% over the prior year. The Metropolitan Water District suspended all mandated water supply reductions in April 2011. The Interim Agricultural Water Program ended December 31, 2012. The Special Agricultural Water Rate has been extended by San Diego County Water Authority through 2014.

The District sold approximately 21,045 acre feet of water during 2013-2014 compared with 21,002 acre feet in the fiscal year prior. Approximately 64% of water sales was for agricultural customers.

Operating expenses increased from the prior year due to increased wholesale water prices as well as an 6% increase in sales volume. Operating expenses other than water decreased by 15.9% due to staffing reductions and the payoff of the CalPERS side fund in the prior year.

New development paid \$318,275 for water capacity fees and the District refunded \$33,605 in sewer capacity fees to developers that abandoned their construction projects.

Statement of Net Position

To begin our analysis, a summary of the District's Condensed Statement of Net Position is presented in Table 1 for the current year and the prior year.

Net position may serve over time, as a useful indicator of a District's financial position. In the case of the District, assets exceeded liabilities by \$92,048,072 as of June 30, 2014.

Total assets increased 10.0% from the prior fiscal year mostly due to the increase in cash.

**RAINBOW MUNICIPAL WATER DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2014**

DISTRICT'S FINANCIAL ANALYSIS (CONTINUED)

Noncurrent assets increased due to the increase in investments.

Total liabilities increased as a result of the addition of two new long-term notes.

The District's financial position is the product of several financial transactions including the net results of revenue and expense, the acquisition and disposal of capital assets, and the depreciation of capital assets.

**Table 1
Condensed Statement of Net Position**

	<u>2014</u>	<u>2013</u>	<u>\$ Change</u>	<u>% of Change</u>
Assets:				
Current assets	\$ 23,270,265	\$ 10,034,639	\$ 13,235,626	131.9%
Noncurrent assets	9,900,879	6,634,848	3,266,031	49.2%
Capital assets, net	85,350,581	87,646,848	(2,296,267)	-2.6%
Total assets	<u>\$ 118,521,725</u>	<u>\$ 104,316,335</u>	<u>\$ 14,205,390</u>	13.6%
Liabilities:				
Current liabilities	\$ 7,478,124	\$ 5,604,265	\$ 1,873,859	33.4%
Noncurrent liabilities	13,015,044	5,618,942	7,396,102	131.6%
Total liabilities	<u>\$ 20,493,168</u>	<u>\$ 11,223,207</u>	<u>\$ 9,269,961</u>	82.6%
Net position:				
Net investment in capital assets	\$ 85,350,581	\$ 87,646,849	\$ (2,296,268)	-2.6%
Unrestricted	6,697,491	5,446,280	1,251,211	23.0%
Total net position	<u>\$ 92,048,072</u>	<u>\$ 93,093,129</u>	<u>\$ (1,045,057)</u>	-1.1%

Statement of Revenues, Expenses and Changes in Net Position

- The District's total operating revenues for the fiscal year ended June 30, 2014, excluding inter-fund transfers, increased by \$1,951,728 to \$40,627,469. This was due primarily to the increase in the pass-through price of water purchased for the fiscal year as well as increased water sales to customers.
- The District's total operating expenses increased by \$3,089,911 to \$41,563,983 due to the increased wholesale cost of water purchases and increased sales.
- The excess of operating expenses over operating revenues was \$936,514.

**RAINBOW MUNICIPAL WATER DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2014**

DISTRICT'S FINANCIAL ANALYSIS (CONTINUED)

The following table presents a summary of the Statement of Revenues, Expenses, and Changes in Net Position for the fiscal year ended June 30, 2014:

Table 2
Condensed Statement of Revenues, Expenses, and Changes in Net Position

	<u>2014</u>	<u>2013</u>	<u>\$ Change</u>	<u>% of Change</u>
Operating revenues:				
Direct	\$ 39,051,174	\$ 37,078,500	\$ 1,972,674	5.3%
Indirect	1,576,295	1,597,241	(20,946)	-1.3%
Total operating revenues	<u>40,627,469</u>	<u>38,675,741</u>	<u>1,951,728</u>	5.0%
Operating expenses:	41,563,983	38,474,072	3,089,911	8.0%
Nonoperating revenues:	-	40,687	(40,687)	-100.0%
Nonoperating expenses:	<u>108,543</u>	<u>67,774</u>	<u>40,769</u>	N/A
Change in net position	<u>\$ (1,045,057)</u>	<u>\$ 174,582</u>	<u>\$ (1,219,639)</u>	-698.6%

General fund budgetary highlights

The General fund did not have any excess of expenditures over appropriations (instances where actual amounts significantly exceeded budgeted amounts) in individual categories.

The District's total operating expenses other than purchased water was 6% less than the budget.

The District has reduced its annual operating budget each of the last four years. Several expense categories including wages and benefits have been reduced in efforts to meet the challenge of decreasing water sales. The District has been successful with staff reductions through the process of not replacing staff members when they leave or retire.

**RAINBOW MUNICIPAL WATER DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2014**

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital assets

**Table 3
Changes in Capital Assets**

	<u>2014</u>	<u>2013</u>	<u>\$ Change</u>	<u>% of Change</u>
Land	\$ 1,977,491	\$ 1,977,489	\$ 2	0.0%
Construction in progress	1,124,824	14,881,758	(13,756,934)	-92.4%
Buildings and improvements	969,773	969,773	-	0.0%
Reservoir, pipelines, and tanks	138,626,289	124,046,235	14,580,054	11.8%
Meters	302,678	302,678	-	0.0%
Equipment	3,101,023	2,925,195	175,828	6.0%
Investment in sewer rights	7,246,540	7,246,540	-	0.0%
Less: accumulated depreciation	(67,998,036)	(64,702,819)	(3,295,217)	5.1%
Total capital assets, net	<u>\$ 85,350,582</u>	<u>\$ 87,646,849</u>	<u>\$ (2,296,268)</u>	-2.6%

The decrease in Construction in Progress is due to the continued capitalization of the Morro reservoir rehabilitation projects. The increase in Property, Plant, and Equipment resulted from the Morro reservoir project being placed into service.

Long-term debt

The District applied for and received funding from the Safe Drinking Water State Revolving Fund/American Recovery and Reinvestment Act. The District became eligible for a \$6,702,680 loan with subsidization in the form of 50% in forgiveness of principal. The award was used to pay for most of the covering and rehabilitation of the North and Northside reservoirs as mandated by the Department of Public Health Services. The District elected to retire this debt and made payment in full in August 2012.

Since that time the District has applied for and received approval for a State Revolving Fund loan for the purpose of funding the construction of the Morro reservoir project and the Pala Mesa Tank project as mandated by the Department of Public Health Services. The loan proceeds had not been received as of June 30, 2014; therefore, loan amounts are not reflected as a long-term liability.

FACTORS BEARING ON THE DISTRICT'S FUTURE

The District recorded a loss from operations of \$963,514 which includes \$3,295,219 of depreciation expense. Net income from all sources resulted in a loss of \$1,045,057. The District was able to increase water sales over the previous year as growers and residents began to recover from the severe economic difficulties of prior years. The District has historically been dependent on agriculture for the majority of its water sales; however, many growers had abandoned or greatly reduced their operation which leaves the District with the challenge of providing a reliable supply of drinking water at a reasonable cost. A significant variance in delivery and consumption of water can greatly affect the District's financial position. The District purchases 100% of its water from the San Diego County Water Authority and Metropolitan Water District. Extended periods of drought can also significantly affect the amount of available water supply.

**RAINBOW MUNICIPAL WATER DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
JUNE 30, 2014**

FACTORS BEARING ON THE DISTRICT'S FUTURE (CONTINUED)

The San Diego County Water Authority continues to pursue seawater from the Carlsbad desalination plant. The desalination project will reduce the dependence of purchased water on the entire San Diego County region. Rainbow Municipal Water District continues to explore the possibility of locating and tapping new ground water supplies within the District sphere of influence. Access to other water sources does not promise to be a cost savings but it does provide a more dependable supply of quality drinking water.

CONTACTING THE DISTRICT

Questions regarding this report should be directed to Tom Kennedy, General Manager, or Margaret Thomas, Finance Manager, at (760) 728-1178, or by mail at 3707 Old Highway 395, Fallbrook, California 92028.

Rainbow Municipal Water District

**RAINBOW MUNICIPAL WATER DISTRICT
STATEMENT OF NET POSITION
JUNE 30, 2014**

ASSETS:

Current assets:	
Cash and cash equivalents	\$ 16,118,721
Accounts receivable:	
Water and sewer, net of allowance	5,815,821
Interest receivables	19,209
Other receivables	153,965
Inventory	1,111,250
Prepaid expenses	51,299
Total current assets	23,270,265
Noncurrent assets:	
Investments	9,900,879
Capital assets:	
Land	1,977,490
Construction in progress	2,999,904
Buildings and improvements	969,773
Reservoir, pipelines, and tanks	136,751,210
Meters	302,678
Equipment	3,101,023
Investment in sewer rights	7,246,540
Less: accumulated depreciation	(67,998,037)
Total noncurrent assets	95,251,460
Total assets	118,521,725

LIABILITIES:

Current liabilities:	
Accounts payable	5,878,015
Accrued expenses	479,022
Current portion of note payable	1,120,142
Other current liabilities	945
Total current liabilities	7,478,124
Noncurrent liabilities:	
Note payable, net of current portion	13,015,044
Total noncurrent liabilities	13,015,044
Total liabilities	20,493,168

DEFERRED INFLOWS OF RESOURCES:

Fees collected for future expenditures	5,980,485
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NET POSITION:

Net investment in capital assets	85,350,581
Unrestricted	6,697,491
Total net position	\$ 92,048,072

The notes to the financial statements are an integral part of these statements.

**RAINBOW MUNICIPAL WATER DISTRICT
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
FOR THE FISCAL YEAR ENDED JUNE 30, 2014**

Operating revenues:	
Direct operating revenues:	
Water sales	\$ 36,497,373
Waste water revenue	2,553,801
Total direct operating revenues	<u>39,051,174</u>
Indirect operating revenues:	
Property tax revenue	831,294
Interest	34,158
Other	710,843
Total indirect operating revenues	<u>1,576,295</u>
Total operating revenues	<u>40,627,469</u>
Operating expenses:	
Water purchases	26,649,303
Water pumping	3,836,825
Transmission and distribution	1,113,721
Meter services	768,966
Sewer services	1,763,824
Administrative and general	4,009,381
Engineering	(21,694)
Finance	-
Customer service	148,438
Depreciation	3,295,219
Total operating expenses	<u>41,563,983</u>
Loss from operations	<u>(936,514)</u>
Non-operating revenues (expenses):	
Interest income	-
Interest expense	(108,543)
Total non-operating revenues (expenses)	<u>(108,543)</u>
Change in net position	(1,045,057)
Net position, beginning	<u>93,093,129</u>
Net position, ending	<u>\$ 92,048,072</u>

The notes to the financial statements are an integral part of these statements.

**RAINBOW MUNICIPAL WATER DISTRICT
STATEMENT OF CASH FLOWS
FOR THE FISCAL YEAR ENDED JUNE 30, 2014**

CASH FLOWS USED BY OPERATING ACTIVITIES:

Receipts from customers	\$ 38,791,127
Receipts from the state	64,448
Receipts from county	1,690,964
Receipts from others	1,380,380
Payments to suppliers and vendors	(33,467,669)
Payments to employees	(4,161,500)
Payments to customers	(350)
	4,297,400
Net cash used by operating activities	4,297,400

CASH FLOWS USED BY INVESTING ACTIVITIES:

Acquisition and construction of capital assets	(13,632,441)
Reclassification of capital assets	12,633,491
	(998,950)
Net cash used by investing activities	(998,950)

CASH FLOWS PROVIDED FROM FINANCING ACTIVITIES:

Increase in investments	(3,266,031)
Proceeds from loans	14,135,186
Payment on loan	(1,120,142)
Interest received	2,269
Interest paid	(40,769)
	9,710,513
Net cash provided from financing activities	9,710,513

NET DECREASE IN CASH AND CASH EQUIVALENTS 13,008,963

CASH AND CASH EQUIVALENTS - BEGINNING 3,109,758

CASH AND CASH EQUIVALENTS - ENDING \$ 16,118,721

The notes to the financial statements are an integral part of these statements.

**RAINBOW MUNICIPAL WATER DISTRICT
STATEMENT OF CASH FLOWS (CONTINUED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2014**

**RECONCILIATION OF OPERATING INCOME TO NET CASH
USED BY OPERATING ACTIVITIES:**

Operating income	\$	(936,514)
Adjustments to reconcile net income from operations to net cash provided by operating activities:		
Depreciation		3,295,217
(Increase) decrease in operating assets:		
Water and sewer		(108,604)
Property taxes		786
Other receivables		(74,418)
Inventory		(122,526)
Prepaid expenses		8,057
Increase (decrease) in operating liabilities:		
Accounts payable		906,186
Accrued expenses		(152,119)
Deferred revenue		361,543
Other current liabilities		1,119,792
Net cash used by operating activities	\$	<u>4,297,400</u>

RECONCILIATION TO BALANCE SHEET

Cash	\$	16,118,721
Net reconciliation to balance sheet	\$	<u>16,118,721</u>

The notes to the financial statements are an integral part of these statements.

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

A. Summary of significant accounting policies

Rainbow Municipal Water District (District) accounts for its financial transactions in accordance with the policies and procedures of the Irrigation District Law, now Division 11 of the California State Water Code. The accounting policies of the District conform to accounting principles generally accepted in the United States of America (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB) and the American Institute of Certified Public Accountants (AICPA).

1. Reporting entity

The District's combined financial statements include the accounts of all its operations. The District evaluated whether any other entity should be included in these financial statements. The criteria for including organizations as component units within the District's reporting entity, as set forth in GASB Statement No. 14. "The Financial Reporting Entity," as amended by GASB Statement No. 39 "Determining Whether Certain Organizations are Component Units", include whether:

- the organization is legally separate (can sue and be sued in its name)
- the District holds the corporate powers of the organization
- the District appoints a voting majority of the organization's board
- the District is able to impose its will on the organization
- the organization has the potential to impose a financial benefit/burden on the District
- there is fiscal dependency by the organization on the District
- it would be misleading or cause the financial statements to be incomplete to exclude another organization

Based on these criteria, the District has no component units. Additionally, the District is not a component unit of any other reporting entity as defined by the GASB statement.

2. Basis of accounting

The District reports its activities as an enterprise fund, which is used to account for operations that are financed and operated in a manner similar to a private business enterprise, where the intent of the District is that the costs of providing water to its customers on a continuing basis be financed or recovered primarily through user charges (water sales and services) or similar funding. Revenues and expenses are recognized on the full accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and expenses are recognized in the period incurred, regardless of when the related cash flow took place.

Operating revenues and expenses are generated and incurred through the water sales activities to the District's customers. Administration and depreciation expenses are also considered operating expenses. Other revenues and expenses not included in the above categories are reported as non-operating revenues and expenses.

3. Financial reporting

GASB No. 34 and subsequent GASB pronouncements provide for a revised view of financial information and restructure the format of financial information provided prior to its adoption. A statement of net assets replaces the balance sheet and reports assets, liabilities, and the difference between them as net assets, not equity. A statement of revenues, expenses, and changes in net assets replaces both the income statement and the statement of changes in retained earnings and contributed capital. GASB No. 34 also requires that the statement of cash

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

A. Summary of significant accounting policies (continued)

3. Financial reporting (continued)

flows be prepared using the direct method. Under the direct method, cash flows from operating activities are presented by major categories.

Under GASB No. 34, enterprise funds, such as the District, have the option of consistently following or not following pronouncements issued by the Financial Accounting Standards Board (FASB) subsequent to November 30, 1989. The District has elected not to follow FASB standards issued after that date, unless such standards are specifically adopted by GASB.

The District's basic financial statements are also presented in conformance with the provisions of GASB Statement No. 63 (GASB 63), *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. The objective of this Statement is to provide guidance to include two classifications separate from assets and liabilities. Amounts reported as deferred outflows of resources are required to be reported in a Statement of Net Position in a separate section following assets. Similarly, amounts reported as deferred inflows of resources are required to be reported in a Statement of Net Position in a separate section following liabilities. In addition, the totals of these two new classifications should be added to the total for assets and liabilities, respectively.

The District had \$5,980,485 of deferred inflows of resources at June 30, 2014. The adoption of this pronouncement resulted in a retroactive change in the term "net assets" being changed to "net position" throughout the financial statements.

4. Assets, liabilities, and equity

a. Deposits and investments

For purposes of the statement of cash flows, cash and cash equivalents consist of short-term highly liquid investments with maturities of ninety days or less from the date of purchase. These include cash on hand, cash held in the restricted assets accounts, and the Local Agency Investment Fund.

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

A. Summary of significant accounting policies (continued)

4. Assets, liabilities, and equity (continued)

The District's investment policy and state statutes authorize the District to invest in obligations of the U.S. Treasury, its agencies and instrumentalities, certificates of deposit with national and state-licensed or chartered banks or federal or state savings and loan associations, money market and mutual funds whose portfolios consist of one or more of the foregoing investments, and the Local Agency Investment Fund.

State statutes require all deposits be insured or collateralized. Depositories holding public funds on deposit are required to maintain collateral in the form of a pool of securities with the agent of the depository having a market value of at least 10 to 50 percent in excess of the total amount of all public funds on deposit.

b. Stores inventories and prepaid expenditures

Inventories are recorded using the purchase method in that the cost is recorded as an expenditure at the time individual inventory items are purchased. Inventories are valued at average cost and consist of expendable supplies held for consumption. Reported inventories are equally offset by a fund balance reserve, which indicates that these amounts are not "available for appropriation and expenditure" even though they are a component of net current assets.

The District has the option of reporting an expenditure in governmental funds for prepaid items either when purchased or during the benefiting period. The District has chosen to report the expenditure during the benefiting period.

c. Capital assets

Purchased or constructed capital assets are reported at cost or estimated historical cost. Donated fixed assets are recorded at their estimated fair value at the date of the donation. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend the assets' lives are not capitalized. A capitalization threshold of \$5,000 is used.

Capital assets are being depreciated using the straight-line method over the following estimated useful lives:

<u>Asset Class</u>	<u>Estimated Useful Lives</u>
Buildings	10-50
Water systems	10-50
Improvements of sites	7-25
Equipment	5-10

d. Compensated absences

Accumulated unpaid employee vacation benefits and sick leave are recognized as accrued payroll liabilities in the Statement of Net Position. As of June 30, 2014, the District had \$393,474 of accrued vacation and sick leave.

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

A. Summary of significant accounting policies (continued)

e. Deferred Inflows of Resources

Cash received for federal and state special projects and programs is recognized as revenue to the extent that qualified expenditures have been incurred. Deferred inflows of resources are recorded to the extent cash received on specific projects and programs exceeds qualified expenditures.

f. Interfund activity

Interfund activity results from loans, services provided, reimbursements or transfers between funds. Loans are reported as interfund receivables and payables as appropriate and are subject to elimination upon consolidation. Reimbursements occur when one fund incurs a cost, charges the appropriate benefiting fund and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers. Transfers In and Transfers Out are netted and presented as a single "Transfers" line on the government-wide statement of activities. Similarly, interfund receivables and payables are netted and presented as a single "Internal Balances" line of the government-wide statement of net position.

g. Property taxes

Secured property taxes attach as an enforceable lien on property as of January 1. Taxes are payable in two installments on November 1 and February 1. Unsecured property taxes are payable in one installment on or before August 31. The County of San Diego bills and collects the taxes for the District.

h. Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

B. Compliance and accountability

1. Finance-related legal and contractual provisions

In accordance with GASB Statement No. 38, "Certain Financial Statement Note Disclosures," violations of finance-related legal and contractual provisions, if any, are reported below, along with actions taken to address such violations:

<u>Violation</u>	<u>Action Taken</u>
None reported	Not applicable

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

B. Compliance and accountability (continued)

2. Deficit fund balance or fund net position of individual funds

The following are funds having deficit fund balances or fund net positions at year end, if any, along with remarks which address such deficits:

<u>Fund Name</u>	<u>Deficit Amount</u>	<u>Remarks</u>
None reported	Not applicable	Not applicable

C. Cash and cash equivalents

The summary of cash and cash equivalents is as follows at June 30, 2014:

	<u>Credit Quality Rating</u>	<u>Fair Value</u>
Cash on hand	Not applicable	\$ 1,200
Deposits with financial institutions	Not applicable	6,624,804
Pooled funds	Not applicable	9,492,717
Total cash and cash equivalents		<u>\$ 16,118,721</u>

The District is a voluntary participant in the Local Agency Investment Fund (LAIF) that is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California. 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 costs 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.

The summary which presents the amount of the District's deposits which are fully insured or collateralized with securities held by the District or its agent in the District's name (Category One), those deposits which are collateralized with securities held by the pledging financial institution's trust department, or agent in the District's name (Category Two), and those deposits which are not collateralized or are collateralized with securities held by the pledging financial institution, or its trust department, or agent, but not in the District's name (Category Three), is as follows at June 30, 2014:

	<u>Category One</u>	<u>Category Two</u>	<u>Category Three</u>	<u>Total Bank Balance</u>
Deposits with Financial institutions	<u>\$ 5,537,956</u>	<u>\$ 103,642</u>	<u>\$ -</u>	<u>\$ 5,641,598</u>

D. Investments

The District categorizes investments according to the level of risk assumed by the District. Category One includes investments that are insured or registered, with securities held by the District or its agent in the District's name. Category Two includes uninsured and unregistered investments held by the counter-party's trust department, or agent in the District's name. Category Three includes

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

D. Investments (continued)

uninsured and unregistered deposits held by the counter-party, its trust department, or its agent, but not in the District's name. Certain investments have not been categorized because securities are not used as evidence of the investment. These uncategorized investments include ownership interest in pooled investment funds.

A summary, which identifies the level of risk assumed by the District and the total carrying amount and market value of the District's investments are as follows at June 30, 2014:

	Category			Uncategorized	Total Investments	Market Value
	One	Two	Three			
U.S. Government Agency Obligation	\$ 9,932,000	\$ -	\$ -	\$ -	\$ 9,932,000	\$ 9,900,879
Total	\$ 9,932,000	\$ -	\$ -	\$ -	\$ 9,932,000	\$ 9,900,879

E. Accounts receivable

Accounts receivable as of June 30, 2014, consists of the following:

Water and sewer	\$ 5,886,843
Less: allowance for uncollectible accounts	(71,022)
Property tax	1,866
Interest receivables	19,209
Other receivables	152,099
Total accounts receivables	\$ 5,988,995

F. Capital assets

A schedule of changes in capital assets and accumulated depreciation for the fiscal year ended June 30, 2014, is shown as follows:

	Balance June 30, 2013	Additions	Deletions	Balance June 30, 2014
Capital assets, not being depreciated:				
Land	\$ 1,977,490	\$ -	\$ -	\$ 1,977,490
Construction in progress	14,881,758	751,637	(12,633,491)	2,999,904
Total capital assets, not being depreciated	16,859,248	751,637	(12,633,491)	4,977,394
Capital assets, being depreciated:				
Buildings and improvements	969,773	-	-	969,773
Reservoir, pipelines, and tanks	124,046,235	12,704,975	-	136,751,210
Meters	302,678	-	-	302,678
Equipment	2,925,194	175,829	-	3,101,023
Investment in sewer rights	7,246,540	-	-	7,246,540
Total capital assets, being depreciated	135,490,420	12,880,804	-	148,371,224

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

F. Capital assets (continued)

	Balance June 30, 2013	Additions	Deletions	Balance June 30, 2014
Less accumulated depreciation for:				
Buildings and improvements	(776,963)	(28,392)	-	(805,355)
Reservoir, pipelines, and tanks	(60,492,646)	(3,040,842)	-	(63,533,488)
Meters	(302,679)	-	-	(302,679)
Equipment	(2,509,560)	(113,081)	-	(2,622,641)
Investment in sewer rights	(620,971)	(112,902)	-	(733,873)
Total accumulated depreciation	(64,702,819)	(3,295,217)	-	(67,998,036)
Total capital assets, being depreciated, net	70,787,601	9,585,587	-	80,373,188
Government activities capital assets, net	<u>\$ 87,646,849</u>	<u>\$ 10,337,224</u>	<u>\$ (12,633,491)</u>	<u>\$ 85,350,581</u>

G. Deferred Inflows of Resources

Deferred inflows of resources represents fees collected for expansion, replacement, and capacity fees that have not yet been expended. At June 30, 2014, deferred inflows of resources consisted of the following:

Sewer replacement	\$ 1,512,128
Sewer expansion	4,112,440
Capacity fees	318,275
Construction meter deposits	24,891
Sewer Connection Fees	6,347
Developer deposits	6,404
Total deferred inflows of resources	<u>\$ 5,980,485</u>

H. Long-term obligations

1. Long-term obligation activity

Long-term obligations include debt and other long-term liabilities. Changes in long-term obligations for the fiscal year ended June 30, 2014, are as follows:

	Balance June 30, 2013	Additions	Retirements	Balance at June 30, 2014	Amount Due Within One Year
Loan Payable SRF Morro	\$ -	\$ 10,200,172	\$ -	\$ 10,200,172	\$ 633,191
Loan Payable SRF Beck	-	3,935,014	-	3,935,014	486,951
Total long-term debt	<u>\$ -</u>	<u>\$ 14,135,186</u>	<u>\$ -</u>	<u>\$ 14,135,186</u>	<u>\$ 1,120,142</u>

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

H. Long-term obligations (continued)

2. Capitalization grant for drinking water fund loan

On September 30, 2009, an agreement was entered into between the State of California, Department of Public Health (the State) and District which constituted funding in the form of a loan with a forgiveness of principal made by the State to the District under the provision of the California Safe Drinking Water State Revolving Fund Law of 1997, Part 12, Chapter 4.5, of Division 104 of Health and Safety Code (Section 116760 and following) and the American Recovery and Reinvestment Act of 2009 (ARRA) Public Law 111-5. The purpose of the funding is to assist in financing construction of a project which will enable the District to meet safe drinking water standards established pursuant to Part 12, Chapter 4 (commencing with Section 116270), of Division 104 of the Health and Safety Code and California Code of Regulations Title 22, or to address other health concerns, herein referred to as the "Project" whose costs are approved by the State.

The District is solely responsible for the design, construction, operation, and maintenance of the Project; and for all persons or entities engaged in such work, including but not limited to subcontractors, supplies, and providers of services. Total cost of the Project is estimated at \$7,475,000 and the State has agreed that \$6,702,680 is eligible for Safe Drinking Water State Revolving Fund ARRA financing.

Pursuant to the Safe Drinking Water State Revolving Fund Law of 1997, its applicable rules and regulations, and ARRA and its implementing guidelines and criteria, and subject to the availability of funds, the State will lend to the District in accordance with the terms of this agreement an amount not to exceed \$6,702,680 for a term of twenty (20) years with interest at 2.5017% per annum and that this agreement also constitutes a promissory note.

In addition, pursuant to the Safe Drinking Water State Revolving Fund Law of 1997, its applicable rules and regulations, and ARRA and its implementing guidelines and criteria, the State agrees to provide additional subsidization in the form of forgiveness of the principal portion of the promissory note equal to fifty percent (50%) of each disbursement to the District under the terms of this agreement and shall not be added to the principal amount of the loan.

A quarterly payment of \$55,662 was made on the loan on August 31, 2012, and then the District paid the remaining balance of \$2,810,871 back to the State on October 25, 2012. Total interest payments during the fiscal year totaled \$108,543.

3. State revolving fund loans

During the fiscal year ended June 30, 2014, the Organization secured a funding agreement with the State in the form of a State Revolving Fund loan constituting two promissory notes. For the first note, the State will lend to the District in accordance with the terms of this agreement an amount not to exceed \$7,924,076 for a term of twenty (20) years with interest at 2.0933% per annum. For the second note, the State will lend to the District in accordance with the terms of this agreement an amount not to exceed \$10,303,804 for a term of twenty (20) years with interest at 2.0933% per annum. At June 30, 2014 the outstanding balance of the two loans was \$14,135,186.

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

H. Long-term obligations (continued)

3. State revolving fund loans (continued)

Required payments of principal and interest on the SRF loans at June 30, 2014, including current maturities are as follows:

Year Ending	Principal	Interest	Total
2015	\$ 758,066	\$ 362,076	\$ 1,120,142
2016	774,018	346,124	1,120,142
2017	790,306	329,837	1,120,143
2018	806,935	313,207	1,120,142
2019	823,915	296,227	1,120,142
2020	841,253	278,890	1,120,143
2021	858,954	261,187	1,120,141
2022	877,011	243,113	1,120,124
2023-2032	10,954,961	1,366,602	12,321,563
	<u>\$ 17,485,419</u>	<u>\$ 3,797,263</u>	<u>\$ 21,282,682</u>

I. Operating leases

The District has entered into operating leases for office equipment with lease terms in excess of one year. These agreements contain no purchase options. The agreements are non-cancelable leases. Future minimum lease payments are as follows:

Year Ending June 30,	Lease Payments
2015	\$ 24,252
2016	17,163
2017	2,641
Total future minimum lease payments	<u>\$ 44,056</u>

The District will receive no sublease rental revenues nor pay any contingent rentals associated with these leases. Rent expense for the fiscal year ended June 30, 2014, was \$35,419.

J. Joint ventures (joint powers agreements)

The District participates in the following jointly governed organization under a joint power agreement (JPA):

Special District Risk Management Authority (SDRMA)

The relationship between the District and the JPA is such that the JPA is not a component unit of the District for financial reporting purposes.

The JPA was established as an agency under the provisions of the California Government Code, Title I, Division 7, Chapter 5, Article 1, Section 6500, et seq. The purpose of the JPA is to provide self-insurance programs such as insurance premiums for general liability, employment practices, and property insurance.

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

North County Joint Powers Authority (NCJPA)

The relationship between the District and the JPA is such that the JPA is not a component unit of the District for financial reporting purposes.

The JPA was established as an agency under the provisions of the California Government Code, Title I, Division 7, Chapter 5, Article 1, Section 6500, et seq. The purpose of the JPA is to provide for the administration of the Member Agencies by managing the combined resources of the Member Agencies, including staffing and physical plant/infrastructure, to obtain cost-effective means of providing service to the ratepayers.

K. Employee retirement systems

Qualified employees are covered under multiple-employer defined benefit pension plans maintained by agencies of the State of California. Classified employees are members of the California Public Employees Retirement System (CalPERS).

PERS:

Plan description

The District contributes to the California Public Employees Retirement System (CalPERS); a cost-sharing multiple-employer public employee retirement system defined benefit pension plan. Plan information for PERS is not publicly available. The plan provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit provisions are established by State statutes, as legislatively amended, within the Public Employees' Retirement Law. CalPERS issues a separate comprehensive annual financial report that includes financial statements and required supplementary information.

Copies of the CalPERS' annual financial reports may be obtained from the CalPERS Executive Office, 400 P Street, Sacramento, CA 95814 and at www.calpers.ca.gov.

Funding policy

Active plan members are required to contribute 8.0% of their annual covered salary and the District contributes 15.098% of the annual covered salary. The District makes the contributions required of the District's employees on their behalf and for their account. The actuarial methods and assumptions used are those adopted by the CalPERS Board of Administration.

The required contribution rate for the fiscal year ended June 30, 2014 was 14.660%. The contribution requirements of the plan members are established by state statute. The District contributions to CalPERS for the fiscal years ending June 30, 2014, 2013 and 2012, were \$572,326, \$541,966 and \$613,212, respectively, and equal 100% of the required contributions for each year.

L. Deferred compensation plan

The District offers its employees a deferred compensation plan in accordance with Internal Revenue Code Section 457. The plan, administered by Lincoln Financial Group, is available to all regular employees, permits deferment of a portion of current salary to future years. Benefits from the plans are not available to employees until termination, retirement, disability, death, or unforeseeable emergencies.

All assets and income of the plans are held in trust for the exclusive benefit of the participants and their beneficiaries. The District does not meet the criteria for fiduciary fund reporting since it does not have either significant administrative involvement (e.g. custody) or perform the investment function. Therefore,

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

L. Deferred compensation plan (continued)

the fair market value of the plans assets at June 30, 2014, in the amount of \$2,285,166, is not included in the District's financial statements.

M. Other post-employment benefits

The District provides Other Post-Employment Benefits (OPEB) including medical, prescription drugs, and dental benefits, in accordance with a resolution approved by the board of Directors. Medical insurance is provided through a choice of a Blue Cross HMO or a Blue Cross Classic PPO, both offered through the Association of California Water Agencies Joint Powers Insurance Authority. Dental insurance is provided through Assurant Employee Benefits.

Plan description

Exempt employees of the District retiring after the later of age 50 and 5 consecutive years of District service are eligible to receive a monthly District contribution towards the purchase of health insurance. Non-exempt employees of the District are eligible after the later of age 50 and 20 consecutive years of District service.

The District makes the following contributions:

Total Monthly Payments	Exempt Employees	Non-Exempt Employees
\$ 2,252	5	-

The District contribution ends after ten (10) years of benefit payments have been made, even if retiree or spouse are still under age 65 at the time.

Funding policy

The District does not establish a trust account for this plan. The District funds the plan on a pay-as-you-go basis.

Annual OPEB cost

The District's OPEB cost is presented as follows:

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

M. Other post-employment benefits (continued)

	<u>As of June 30, 2012</u>
Present value of future benefits	
Active employees	\$ 414,343
Retired employees	71,986
Total present value of future benefits	<u>\$ 486,329</u>
Accrued liability	
Active employees	\$ 210,061
Retired employees	71,986
Total accrued liability	<u>282,047</u>
Total unfunded accrued liability	<u>\$ 282,047</u>
Annual required contributions	
Service cost at year ended	\$ 22,134
Thirty (30) year amortization of unfunded accrued liability	<u>18,347</u>
Total annual required contributions	<u>\$ 40,481</u>

The District provided 2012-2013 annual OPEB Cost analysis which is the most recent available information.

Funded status of the plan

Actuarial accrued liability and unfunded actuarial accrued liability are \$155,249. There are no plan assets because the District funds on a pay-as-you-go basis.

Actuarial assumptions

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. In order to perform the valuation, the actuary must make certain assumptions regarding such items as rate of employee turnover, retirement, and mortality, as well as economic assumptions regarding healthcare inflation and interest rates.

**RAINBOW MUNICIPAL WATER DISTRICT
NOTES TO BASIC FINANCIAL STATEMENTS
JUNE 30, 2014**

N. Commitments and contingencies

Tank maintenance commitments

On December 10, 2003, the District entered into a ten (10) year contract with Utility Service Co., Inc. to maintain twelve water tanks at an annual cost of \$615,585. The contract can be cancelled annually if intent to cancel is received within ninety (90) days prior to the anniversary date. Any outstanding balance for completed work would be due and payable within thirty (30) days of cancellation.

Capacity rights for sewage treatment

On February 13, 2002, Rainbow Municipal Water District (the District) entered into a contract with the City of Oceanside, California (the City) to provide for the construction, operation, maintenance, and replacement of a wastewater system to service the needs of both the City and the District. The City owns the wastewater conveyance, treatment, and disposal facilities and the District has the contractual right to discharge wastewater into the City's System. The City and the District have previously entered into agreements on January 2, 1973, and September 10, 1989. This agreement reflects the planned expansion and rehabilitation of facilities built from those previous agreements. Under the agreement, the District's share of cost for planned expansion and rehabilitation of the facilities would be 10%.

O. Subsequent event

The District's management has evaluated events or transactions that may occur for potential recognition or disclosure in the financial statements from the balance sheet date through October 2, 2014, which is the date the financial statements were available to be issued. Management has determined that there were no subsequent events or transactions that would have a material impact on the current year financial statements.

**RAINBOW MUNICIPAL WATER DISTRICT
SUPPLEMENTARY INFORMATION SECTION
JUNE 30, 2014**

**RAINBOW MUNICIPAL WATER DISTRICT
ORGANIZATION
JUNE 30, 2014**

The Board of Directors for the fiscal year ended June 30, 2014, was comprised of the following members:

Name	Office	Term	Term expires
George McManigle	President	4 years	December 31, 2014
Dennis Sanford	Vice President	4 years	December 31, 2016
Helene Brazier	Secretary	4 years	December 31, 2016
Jack Griffiths	Director	4 years	December 31, 2016
Robert Lucy	Director	4 years	December 31, 2014

Administration

Name	Position
Chuck Sneed	General Manager
Margaret Thomas	Finance Manager

**RAINBOW MUNICIPAL WATER DISTRICT
ASSESSED VALUATION
JUNE 30, 2014**

The assessed valuation of the Rainbow Municipal Water District at June 30, 2014, is as follows:

Assessed valuation	
Secured property	\$ 3,561,754,838
Unsecured property	<u>17,072,912</u>
Total assessed valuation	<u>\$ 3,578,827,750</u>

RAINBOW MUNICIPAL WATER DISTRICT
OTHER REPORTS OF INDEPENDENT AUDITORS SECTION
JUNE 30, 2014



**REPORT OF INDEPENDENT AUDITORS 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**

Board of Directors
Rainbow Municipal Water District
Fallbrook, California

We have audited, 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 the State Controller's *Minimum Auditing requirements for California Special Districts*, the financial statements of Rainbow Municipal Water District, as of and for the fiscal year ended June 30, 2014, and the related notes to the financial statements.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Rainbow Municipal 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 opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Rainbow Municipal Water District's internal control. Accordingly, we do not express an opinion on the effectiveness of Rainbow Municipal Water 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. 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 have not been identified.

**REPORT OF INDEPENDENT AUDITORS 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
Page 2**

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Rainbow Municipal 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*.

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.

Hosaka, Rotherham & Company

San Diego, California
October 2, 2014

**RAINBOW MUNICIPAL WATER DISTRICT
FINDINGS AND RECOMMENDATIONS SECTION
JUNE 30, 2014**

**RAINBOW MUNICIPAL WATER DISTRICT
SCHEDULE OF AUDIT FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2014**

A. Summary of auditors' results

1. Financial statements

Type of auditors' report issued: Unqualified

Internal control over financial reporting:

One or more material weaknesses identified? Yes X No

One or more significant deficiencies identified that are not considered to be material weaknesses? Yes X None Reported

Noncompliance material to financial statements noted? Yes X No

2. Federal awards

Internal control over major programs:

One or more material weaknesses identified? Yes N/A No

One or more significant deficiencies identified that are not considered to be material weaknesses? Yes N/A None Reported

Type of auditors' report issued on compliance for major programs: N/A

Any audit findings disclosed that are required to be reported in accordance with Section .510(a) of Circular A-133? Yes N/A No

Identification of major programs:

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Cluster</u>
-----------------------	---

The District did not have over \$500,000 in Federal Expenditures.

Dollar threshold used to distinguish between type A and type B programs: N/A

Auditee qualified as low-risk auditee? Yes N/A No

B. Financial statement findings

None

C. Federal award findings and questioned costs

None

**RAINBOW MUNICIPAL WATER DISTRICT
STATUS OF PRIOR YEAR FINDINGS AND RECOMMENDATIONS
JUNE 30, 2014**

<u>Findings/Recommendations</u>	<u>Current Status</u>	<u>Management's Explanation If Not Implemented</u>
None	N/A	N/A