

Board of Directors  
Hemet-San Jacinto Watermaster  
Corona, California

We have audited the financial statements of the Hemet-San Jacinto Watermaster (the Watermaster) as of and for the year ended December 31, 2017, and have issued our report thereon dated February 28, 2018. We have previously communicated to you information about our responsibilities under auditing standards generally accepted in the United States of America and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. Professional standards also require that we communicate to you the following information related to our audit.

## **Significant Audit Findings**

### ***Qualitative Aspects of Accounting Practices***

#### *Accounting policies*

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the Watermaster are described in Note 1 to the financial statements.

No new accounting policies were adopted and the application of existing policies was not changed during 2017.

We noted no transactions entered into by the entity during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

#### *Emphasis-of-Matter: Correction of an Error*

As described in Note 4 to the financial statements, the Watermaster reports its activities on a full accrual basis. During the year ended December 31, 2017, the Watermaster included revenue and expenses that were related to December 31, 2016. The Watermaster has corrected the errors by properly adjusting net position with a prior year restatement. Our opinion is not modified with respect to that matter.

#### *Accounting estimates*

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive accounting estimates affecting the financial statements was Management's estimate of groundwater monitoring and specific evaluation program expenses and related liabilities. We evaluated the key factors and assumptions used to develop the sensitive accounting estimates described above in determining that they are reasonable in relation to the financial statements taken as a whole.

*Financial statement disclosures*

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. There were no particularly sensitive financial statement disclosures.

The financial statement disclosures are neutral, consistent, and clear.

***Difficulties Encountered in Performing the Audit***

We encountered no significant difficulties in dealing with management in performing and completing our audit.

***Uncorrected Misstatements***

Professional standards require us to accumulate all misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. Management did not identify and we did not notify them of any uncorrected financial statement misstatements.

***Corrected Misstatements***

The attached schedule summarizes all misstatements (material and immaterial) detected as a result of audit procedures that were corrected by management.

***Disagreements with Management***

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditors' report. No such disagreements arose during our audit.

***Management Representations***

We have requested certain representations from management that are included in the management representation letter dated February 28, 2018.

***Management Consultations with Other Independent Accountants***

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the entity's financial statements or a determination of the type of auditors' opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

***Significant Issues Discussed With Management Prior To Engagement***

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to engagement as the entity's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our engagement.

***Other Audit Findings or Issues***

Audit standards require that we communicate to you any internal control related matters and any other audit findings or issues that are, in our professional judgment, significant and relevant to those charged with governance in overseeing the financial reporting process. We have discussed this matter with management and are communicating this finding to you as follows:

- As described in Note 4 to the financial statements and as noted above, the Watermaster reports its activities on a full accrual basis. During the year ended December 31, 2017, the Watermaster included revenue and expenses that were related to December 31, 2016 which resulted in a prior year restatement of net position. In addition, we noted that the Watermaster did not have a procedure or method wherein complete monthly closing procedures were in place to ensure that revenue and expenses are recorded in the right period. This resulted in numerous audit adjustments for the period under audit. We recommended that the Watermaster adopt such procedures to ensure that financial statements are accurate and free of material errors and included this finding in the financial statements.

***Other Information in Documents Containing Audited Financial Statements***

With respect to the required supplementary information (RSI) accompanying the financial statements, we made certain inquiries of management about the methods of preparing the RSI, including whether the RSI has been measured and presented in accordance with prescribed guidelines, and whether there were any significant assumptions or interpretations underlying the measurement or presentation of the RSI. We compared the RSI for consistency with management's responses to the foregoing inquiries, the basic financial statements, and other knowledge obtained during the audit of the basic financial statements. Because these limited procedures do not provide sufficient evidence, we did not express an opinion or provide any assurance on the RSI.

This communication is intended solely for the information and use of the Board of Directors and management of the Hemet-San Jacinto Watermaster and is not intended to be, and should not be, used by anyone other than these specified parties.



**CliftonLarsonAllen LLP**  
Glendora, California  
February 28, 2018

**HEMET- SAN JACINTO WATERMASTER**

**REPORT ON AUDIT OF FINANCIAL STATEMENTS**

**December 31, 2017**

**HEMET- SAN JACINTO WATERMASTER**

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**December 31, 2017**

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## INDEPENDENT AUDITORS' REPORT

Board of Directors  
Hemet-San Jacinto Watermaster  
Corona, California

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Hemet-San Jacinto Watermaster (the "Watermaster") as of and for the year ended December 31 2017, and the related notes to the financial statements, which collectively comprise the Watermaster's basic 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 control 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 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 policies and procedures of the *State Controller's Office of Local Government Fiscal Affairs Minimum Audit Requirements for California Special Districts*, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 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 Watermaster'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 Watermaster'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.

## INDEPENDENT AUDITORS' REPORT

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 Watermaster as of December 31, 2017, and the respective changes in its financial position and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

### **Emphasis-of-Matter**

#### *Correction of an Error*

As described in Note 4 to the financial statements, certain assessment revenues and operating expenses should have been reported in prior reporting periods. The Watermaster has corrected the errors by recording the amounts to the proper period and adjusting the amount previously reported in net position. Our opinion is not modified with respect to that matter.

### **Other Matters**

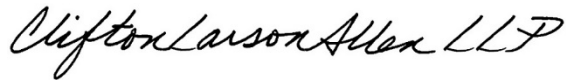
#### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis 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.

## INDEPENDENT AUDITORS' REPORT

### Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated February 28, 2018 on our consideration of the Watermaster'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 solely 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 effectiveness of Watermaster's 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 Watermaster's internal control over financial reporting and compliance.



CliftonLarsonAllen LLP  
Glendora, California  
February 28, 2018



**BOARD OF DIRECTORS**

**HEMET-SAN JACINTO WATERMASTER**

**BOARD OF DIRECTORS**

**December 31, 2017**

Linda Krupa

Rick Hoffman

Philip E. Paule

Andrew Kotyuk

Bruce Scott

Chair

Vice-Chair

Secretary/Treasurer

Member

Member

# HEMET- SAN JACINTO WATERMASTER

## MANAGEMENT DISCUSSION AND ANALYSIS

December 31, 2017

This discussion and analysis of Hemet-San Jacinto Watermaster's (the "Watermaster") financial performance provides an overview of the Watermaster's financial activities for the fiscal year ended December 31, 2017. Please read it in conjunction with the Watermaster's financial statements, which immediately follow this section.

### Introduction and Background

The Hemet-San Jacinto Watermaster (Watermaster) was formed on April 18, 2013 in a judgement by the Riverside County Superior Court (case number 1207274). The function of the Watermaster is to monitor groundwater production, levy replenishment assessments, monitor water transfers, and establish future same yields to ensure one long-term sustainability of the basins within the Management area. The participating municipal agencies are the Eastern Municipal Water District, the Lake Hemet Municipal Water District, and the cities of Hemet and San Jacinto. The stipulated judgement establishes and prioritizes water rights, provides a physical way to eliminate overdrafts, and protects the water rights of the Soboba Band of Luiseño Indians.

The Watermaster, established by the Stipulated Judgment, is a board composed of one elected official and one alternate selected by each of the Public Agencies and one Private Pumper representative and one alternate selected by the participating Private Pumpers. The Stipulated Judgment also provides for a Technical Advisory Committee (TAC) composed of such managerial and technical representatives from the individual parties. Day to day activities are managed by the Advisor to Watermaster (Advisor). The Advisor is responsible for the administration and operations of the Management Plan Area under the provisions of the Stipulated Judgment and evaluates and analyzes data collected in the Management Area, develops conclusions based thereon, and makes recommendations to the Watermaster Board. The Watermaster retains independent legal counsel to provide such legal series as the Watermaster may direct.

The powers and duties of the Watermaster include making rules and regulations necessary for its own operations as well as for the operation of the Water Management Plan (Plan) and the Stipulated Judgment; the implementation of the Physical Solution; development and implementation of the Plan; planning and constructing facilities to accomplish the goals of the Stipulated Judgment; purchase of water for recharge; data collection; levying, billing and collection of all assessments provided for under the Stipulated Judgment; record keeping; and reporting to the Court.

### Financial Highlights

- Total assets increased as of December 31, 2017 by \$104,975 compared to 2016 and consisted of cash and accounts receivable.
- Total liabilities increased as of December 31, 2017 by \$292,014 compared to 2016 and consisted of accounts payable and accrued expenses.
- The Watermaster ended the year with a net position of \$984,180, a decrease from 2016 of \$187,039.

## HEMET- SAN JACINTO WATERMASTER

### MANAGEMENT DISCUSSION AND ANALYSIS

December 31, 2017

- For the year ended December 31, 2017, the Watermaster recorded a decrease in net position of \$233,615 from operations compared to a decrease in net position of \$31,245 for the year ended December 31, 2016.
- Current year assessments were \$514,165, offset by prior year assessment credits of \$46,062, resulting in operating revenues of \$468,103.
- Operating expenses were \$701,718.
- For the year ended December 31, 2017, the Watermaster recorded a decrease in net position of \$232,172 from operations compared to a decrease in net position of \$31,245 for the year ended December 31, 2016.
- The Watermaster recorded a prior year adjustment to net position which increased beginning net position by \$45,133. (See note 4 to financial statements).

#### Financial Management and Control

The Watermaster is responsible for establishing and maintaining an internal control structure designed to ensure that assets are protected from loss, theft or misuse and to ensure that adequate accounting data are compiled to allow for preparation of financial statements in conformity with US generally accepted accounting principles (US GAAP).

CliftonLarsonAllen LLP, Certified Public Accountants, performs an independent audit examination of the financial statements in accordance with generally accepted auditing standards (GAAS).

#### Basic Financial Statements

Financial statements are prepared in conformity with US GAAP and include amounts based upon reliable estimates and judgments. The financial statements include the Statement of Net Position; Statement of Revenues, Expenses and Change in Net Position; and the Statement of Cash Flows. The statements are accompanied by footnotes to clarify unique accounting policies and other financial information and required supplementary information. The assets, liabilities, revenues, and expenses are reported on a full-accrual basis.

The **Statement of Net Position** presents information on all assets and liabilities, with the difference between the two representing net position. Assets and Liabilities are classified as current or non-current. Changes within the year in total net position as presented on the Statement of Net Position are based on the activity presented on the Statement of Revenues, Expenses and Change in Net Position.

# HEMET- SAN JACINTO WATERMASTER

## MANAGEMENT DISCUSSION AND ANALYSIS

December 31, 2017

The **Statement of Revenues, Expenses and Change in Net Position** presents information showing total revenues versus total expenses and how net position changed during the fiscal year. All revenues earned and expenses incurred during the year are required to be classified as either “operating” or “non-operating.” For the current year, all expenses incurred are considered to be operating. All revenues and expenses are recognized as soon as the underlying event occurs, regardless of timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in the disbursement or collection of cash during future fiscal years (e.g., the expense associated with changes in claim liability involving cash transactions beyond the date of the financial statements).

The **Statement of Cash Flows** presents the changes in the cash and cash equivalents during the fiscal year. This statement is prepared using the direct method of cash flow. The statement breaks the sources and uses of cash and cash equivalents into two categories:

- Operating activities
- Investing activities

The routine activities appear in the operating activities, while receipts from investments comprise the investing activities.

The **Notes to the Financial Statements** provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes describe the nature of operations and significant accounting policies as well as clarify unique financial information.

### Condensed Financial Statements

#### Condensed Statement of Net Position

	<u>2017</u>	<u>2016</u>	<u>Change</u>
Total Assets	<u>\$ 1,471,066</u>	<u>\$ 1,366,091</u>	<u>\$ 104,975</u>
Total Liabilities	<u>\$ 486,886</u>	<u>\$ 194,872</u>	<u>\$ 292,014</u>
Net Position			
Unrestricted	<u>\$ 984,180</u>	<u>\$ 1,171,219</u>	<u>\$ (187,039)</u>
Total Net Position	<u>\$ 984,180</u>	<u>\$ 1,171,219</u>	<u>\$ (187,039)</u>

Total assets increased by \$104,975 primarily due to an increase in accounts receivable that was offset by a decrease in cash. Total liabilities increased \$292,014, primarily due to an increase in

**HEMET- SAN JACINTO WATERMASTER**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
**December 31, 2017**

accrued liabilities for expenses related to the initiation of two new studies including the Storage Program Evaluation and the Video Inspection of Well Casings project as well as accruals for In-Lieu Monitoring Program Support and additional Mapping Application Development.

Net position may serve over time as a useful indicator of a government's financial position. In the case of the Watermaster, assets of the Watermaster exceeded liabilities by \$984,180 for the year ended December 31, 2017, reflecting a decrease in net position of \$187,039 compared to 2016.

**Condensed Statements of Revenues Expenses and Change in Net Position**

	<u>2017</u>	<u>2016</u>	<u>Change</u>
Operating revenues	\$ 514,165	\$ 431,640	\$ 82,525
Prior year assessment credits	(46,062)	-	(46,062)
Non-operating revenues-interest	1,443	1,443	-
Total Revenues	<u>469,546</u>	<u>433,083</u>	<u>36,463</u>
Total Operating Expenses	<u>701,718</u>	<u>464,328</u>	<u>237,390</u>
Change in Net Position	<u>(232,172)</u>	<u>(31,245)</u>	<u>(200,927)</u>
Net Position - Beginning of Year			
Before restatement	1,171,219	1,202,464	(31,245)
Prior year restatement (See Note 2)	<u>45,133</u>	<u>-</u>	<u>45,133</u>
Net Position - Beginning of Year as restated	1,216,352	1,202,464	13,888
Net Position - End of Year	<u>\$ 984,180</u>	<u>\$ 1,171,219</u>	<u>\$ (187,039)</u>

As of December 31, 2017, the Watermaster's total operating expenses exceeded its total revenues, resulting in a decrease in net position of \$232,172, primarily due to expenses associated with the initiation of two new studies including the Storage Program Evaluation and the Video Inspection of Well Casings. In addition, the Watermaster experienced an increase in expenses related to the In-Lieu Monitoring Program Support and additional Mapping Application Development. This was partially offset by an increase in assessment revenues due to an increase in water produced.

In addition, the Watermaster recorded a prior year adjustment which resulted in an increase in net position. See note 4 for further discussion.

**HEMET- SAN JACINTO WATERMASTER**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
**December 31, 2017**

**Operating Revenues:**

Operating revenues for the Watermaster come from municipal agencies based on an administrative assessment. Each municipal agency contributes a \$30 per acre-foot charge levied for each acre-foot of adjusted Base Production Rights pumped.

**Non-operating Revenues:**

Non-operating revenues consist of interest earned on cash held by a financial institution.

**Operating Expenses:**

Operating expenses consist of costs incurred in connection with the monitoring and in-lieu program agreements and advisory services incurred in the operations of the Watermaster as well as other related studies. In addition, the Watermaster incurs general administrative, professional and legal services related to the ongoing activities of the Watermaster which are not part of the advisory services.

**Budgetary Highlights**

The Board of Directors approves the budget and establishes the administrative assessment. The preliminary budget is brought to the February board meeting. Any subsequent changes in assumptions or projections are incorporated in the final budget.

The following summary shows the comparative information and variance of budget versus actual revenues and expenses.

**HEMET- SAN JACINTO WATERMASTER**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
**December 31, 2017**

	Revised /Final Budget	Actual	Variance Favorable/ Unfavorable
<b>Operating Revenues</b>			
Assessments	\$ 514,140	\$ 514,165	\$ 25
Prior year assessment credits	-	(46,062)	(46,062)
<b>Total Operating Revenues</b>	<u>514,140</u>	<u>468,103</u>	<u>(46,037)</u>
<b>Operating Expenses</b>			
In-Lieu program	189,000	189,000	-
Groundwater monitoring	216,220	216,218	2
Advisor	165,000	162,385	2,615
Storage program evaluation	85,000	85,000	-
Database/ mapping	5,250	5,000	250
Legal services	30,000	17,156	12,844
Financial support services	9,000	7,500	1,500
Administrative support	14,000	12,168	1,832
Insurance, supplies and other	7,500	7,291	209
<b>Total Operating Expenses</b>	<u>720,970</u>	<u>701,718</u>	<u>19,252</u>
Net operating loss	<u>(206,830)</u>	<u>(233,615)</u>	<u>(26,785)</u>
<b>Non operating revenues</b>			
Interest	-	1,443	1,443
<b>Change in net position</b>	<u>(206,830)</u>	<u>(232,172)</u>	<u>(25,342)</u>
<b>Net position, beginning of period</b>	1,171,219	1,171,219	-
Prior year restatement (See Note 3)	-	45,133	45,133
<b>Net position beginning of period, as restated</b>	<u>1,171,219</u>	<u>1,216,352</u>	<u>45,133</u>
<b>Net position, end of period</b>	<u>\$ 964,389</u>	<u>\$ 984,180</u>	<u>\$ 19,791</u>



**HEMET- SAN JACINTO WATERMASTER**  
**MANAGEMENT DISCUSSION AND ANALYSIS**  
**December 31, 2017**

**Description of Facts or Conditions that are expected to have a Significant Effect on Financial Position or Results of Operations**

Management is unaware of any facts or conditions which could have a significant impact on the Watermaster's current financial position or foreseeable operating results. The Watermaster is currently recording operating expenses in excess of assessment revenues and is utilizing reserve funds to meet its obligations. Management of the Watermaster anticipates future increases to the per acre-foot charge levied administrative assessment. In addition, the Watermaster will continue to evaluate the feasibility of various monitoring and program studies in order to commit resources in line with assessment revenue.

**Contacting the Watermaster Financial Management**

*The financial report contained herein is designed to provide a general overview of the finances, activities and operations of the Watermaster. To obtain additional information, please feel free to contact the Hemet- San Jacinto Watermaster at (714) 794-5520.*

## **FINANCIAL SECTION**

**HEMET- SAN JACINTO WATERMASTER**

**STATEMENT OF NET POSITION**

**December 31, 2017**

**ASSETS**

	<u>2017</u>
<b>Current Assets</b>	
Cash and cash equivalents	\$ 1,239,074
Accounts receivable	<u>231,992</u>
<b>Total Assets</b>	<u><u>\$ 1,471,066</u></u>

**LIABILITIES AND NET POSITION**

<b>Current Liabilities</b>	
Accounts payable	\$ 38,709
Accrued liabilities	<u>448,177</u>
<b>Total Liabilities</b>	<u>486,886</u>
<b>Net Position</b>	
Unrestricted	<u>984,180</u>
<b>Total Net Position</b>	<u>984,180</u>
<b>Total Liabilities and Net Position</b>	<u><u>\$ 1,471,066</u></u>

See accompanying notes to the financial statements.

## HEMET- SAN JACINTO WATERMASTER

### STATEMENT OF REVENUES, EXPENSES AND CHANGE IN NET POSITION For the Year Ended December 31, 2017

	<u>2017</u>
<b>Operating Revenues</b>	
Assessments	\$ 514,165
Prior year assessment credit	<u>(46,062)</u>
<b>Total Operating Revenues</b>	<u>468,103</u>
<b>Operating Expenses</b>	
In-Lieu program	189,000
Groundwater monitoring	216,218
Advisor	162,385
Storage project evaluation	85,000
Database/ mapping	5,000
Legal services	17,156
Financial support services	7,500
Administrative support	12,168
Insurance, supplies and other	<u>7,291</u>
<b>Total Operating Expenses</b>	<u>701,718</u>
Net operating loss	<u>(233,615)</u>
<b>Non operating revenues</b>	
Interest	<u>1,443</u>
<b>Change in net position</b>	<u>(232,172)</u>
<b>Net position, beginning of period</b>	1,171,219
Prior year restatement (See Note 4)	<u>45,133</u>
<b>Net position beginning of period, as restated</b>	<u>1,216,352</u>
<b>Net position, end of period</b>	<u><u>\$ 984,180</u></u>

See accompanying notes to the financial statements.

# HEMET-SAN JACINTO WATERMASTER

## STATEMENT OF CASH FLOWS For the Year Ended December 31, 2017

	<u>2017</u>
<b>Cash Flows from Operating Activities</b>	
Receipts from customers	\$ 309,643
Payment to suppliers and vendors	<u>(438,103)</u>
<b>Net cash used by operating activities</b>	<u>(128,460)</u>
<b>Cash Flows from Investing Activities</b>	
Interest Received	<u>1,443</u>
<b>Net cash provided by investing activities</b>	<u>1,443</u>
<b>Net decrease in cash</b>	(127,017)
<b>Cash and cash equivalents, beginning of period</b>	<u>1,366,091</u>
<b>Cash and cash equivalents, end of period</b>	<u><u>\$ 1,239,074</u></u>
<b>Reconciliation of net operating loss to net cash used by operating activities</b>	
Net operating loss	\$ (233,615)
Adjustments:	
Increase in accounts receivable	(158,460)
Decrease in accounts payable	(184,562)
Increase in accrued expenses	<u>448,177</u>
<b>Net cash used by operating activities</b>	<u><u>\$ (128,460)</u></u>

See accompanying notes to the financial statements.

# HEMET-SAN JACINTO WATERMASTER

## NOTES TO THE FINANCIAL STATEMENTS For the Year Ended December 31, 2017

### **NOTE 1: ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES**

#### **Nature of Operations**

The Hemet-San Jacinto Watermaster (Watermaster) was formed on April 18, 2013 in a judgement by the Riverside County Superior Court (case number 1207274). The function of the Watermaster is to monitor groundwater production, levy replenishment assessments, monitor water transfers, and establish future same yields to ensure one long-term sustainability of the basins within the Management area. The participating municipal agencies are the Eastern Municipal Water District, the Lake Hemet Municipal Water District, and the cities of Hemet and San Jacinto. The stipulated judgement establishes and prioritizes water rights, provides a physical way to eliminate overdrafts, and protects the water rights of the Soboba Band of Luiseño Indians.

#### **Basis of Accounting and Measurement Focus**

The Watermaster 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. 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 flows take place.

Operating revenues and expenses, such as Watermaster assessments result from exchange transactions associated with the principal activity of the Agency. Exchange transactions are those in which each party receives and gives up essentially equal values. The principal operating revenues of the Watermaster are regulatory assessments to participating municipal water right holders.

#### **Fund Accounting**

The accounts of the Watermaster are organized on the basis of an enterprise fund, the operations of which are accounted for with a set of self-balancing accounts that comprise its assets, liabilities, net position, revenues and expenditures. The Watermaster's resources are allocated to and accounted for based upon the purpose for which they are spent and the means by which spending activities are controlled. Net position is categorized as net investment in capital assets, restricted, and unrestricted.

***Net Investment In Capital Assets*** - This category groups all capital assets 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. By order of the Stipulated Judgment, the Watermaster may not invest in any infrastructure. As of December 31, 2017, the Watermaster did not have any net investment in capital assets.

# HEMET-SAN JACINTO WATERMASTER

## NOTES TO THE FINANCIAL STATEMENTS For the Year Ended December 31, 2017

### **NOTE 1: ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES**

***Restricted Net Position*** - This category presents external restrictions imposed by creditors, grantors, contributors, or laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation. As of December 31, 2017, the Watermaster did not have any restricted net position.

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

The Watermaster considers restricted amounts to have first been spent when an expenditure is incurred for purposes for which both restricted and unrestricted net position are available.

#### **Cash and Cash Equivalents**

Cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition. Cash and cash equivalents at December 31, 2017 consisted of cash deposited with a financial institution.

#### **Accounts Receivable**

The Watermaster considers accounts receivable to be fully collectible. Receivables are assessments due from participating municipal agencies.

#### **Classification of Revenues**

Operating revenues in the proprietary funds are those revenues that are generated from the primary operations of the fund. All other revenues are reported as non-operating revenues.

Operating revenues consist of administrative assessment fees from municipal agencies. Each municipal agency currently contributes \$30 per acre-foot charge levied for each acre-foot of adjusted Base Production Rights pumped.

Non- operating revenues consist of interest earned.

Operating expenses are those expenses that are essential to the primary operations of the fund.

#### **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.

**HEMET-SAN JACINTO WATERMASTER**

**NOTES TO THE FINANCIAL STATEMENTS  
For the Year Ended December 31, 2017**

**NOTE 2: CASH AND INVESTMENTS**

On December 31, 2017, the Watermaster had cash held in deposit accounts in a financial institution of \$1,253,557. Cash and investments are presented in the accompanying basic financial statements as cash and cash equivalents of \$1,239,074.

**Investments Authorized by the California Government Code and the Watermaster's Investment Policy**

The table shown herein identifies the investment types that are authorized by the Watermaster in accordance with the California Government Code. The table also identifies certain provisions of the California Government Code that address interest rate, credit risk and concentration of credit risk.

<u>Authorized Maximum Investment type</u>	<u>Maximum Maturity</u>	<u>Maximum Percentage of Portfolio</u>	<u>Maximum Investment in One Issuer</u>
U.S Treasury Obligations	5 years	None	None
U.S Agency Securities	5 years	None	None
Negotiable Certificates of Deposit	5 years	30%	\$ 250,000
California Local Agency Investments Fund (LAIF)	N/A	None	None

**Investment Valuation**

Investments are measured at fair value on a recurring basis. Recurring fair value measurements are those that the GASB requires or permits in the statement of net position at the end of each reporting period. Fair value measurements are categorized based on the valuation inputs used to measure an asset's fair value: Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. As of December 31, 2017, the Watermaster had no investments subject to fair value measurements under the fair value hierarchy as described above.

**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 Watermaster'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.



## HEMET-SAN JACINTO WATERMASTER

### NOTES TO THE FINANCIAL STATEMENTS For the Year Ended December 31, 2017

#### **NOTE 2: CASH AND INVESTMENTS**

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 government 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. Of the bank balances, up to \$250,000 as of December 31, 2017 is federally insured and the remaining balance is collateralized in accordance with the Code; however, the collateralized securities are not held in the Watermaster's name.

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty (e.g. broker-leader) 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 Code and the Watermaster's investment policy contain legal and 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 (such as the Local Agency Investment Fund).

#### **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. One of the ways that the Watermaster may manage its exposure to interest rate risk is by purchasing a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio matures or comes close to maturity evenly over time as necessary to provide cash flow requirements and liquidity needed for operations.

#### **Credit Risk**

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.

#### **Concentration of Credit Risk**

The investment policy of the Watermaster contains limitations on the amount that can be invested in any one issuer beyond that stipulated by the California Government Code. There are no investments in any one issuer that represent 5% or more of total Watermaster's investments.

#### **NOTE 3: TRANSACTIONS WITH RELATED PARTY**

The function of the Watermaster is to monitor groundwater production, levy replenishment

## HEMET-SAN JACINTO WATERMASTER

### NOTES TO THE FINANCIAL STATEMENTS For the Year Ended December 31, 2017

#### **NOTE 3: TRANSACTIONS WITH RELATED PARTY**

assessments, monitor water transfers, and establish future same yields to ensure one long-term sustainability of the basins within the Management area. One of the participating municipal agencies is the Eastern Municipal Water District (EMWD). In July 2013, the Watermaster entered into an agreement with EMWD wherein EMWD agreed to provide services including administrative, financial and technical support services (the Support Services Agreement). Prior to the establishment of the Watermaster through the Stipulated Judgment entered on April 18, 2013, EMWD had previously entered into agreements with municipal groundwater producers currently parties to the stipulated judgment to provide groundwater and surface water monitoring in the Hemet-San Jacinto Management Area for the years 2004 through 2013.

The Support Services Agreement provides that support services requested by the Watermaster shall be set forth in Task Orders and that compensation for the Task Orders shall be based on a Rate Schedule provided by EMWD setting forth the time and material rates and charges then in effect for services provided by EMWD and /or subcontractors. The Agreement terminates on December 31, 2017 unless extended by the mutual agreement of the Watermaster and EMWD.

The Watermaster may utilize other providers for the services currently provided by EMWD. During the year ended December 31, 2017, the Watermaster had accrued expenses of \$405,218 for In-Lieu program and groundwater monitoring services from EMWD. The remaining liability of \$363,177 is included in accrued expenses reported in the accompanying financial statements.

#### **NOTE 4: PRIOR YEAR RESTATEMENT**

The Watermaster 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. Revenues and expenses are recognized on the full accrual basis of accounting. In accordance with Generally Accepted Accounting Principles and under the full accrual method of accounting, revenues are recognized in the accounting period in which they are earned and expenses are recognized in the period incurred. The Watermaster is required to accrue revenue and expenses into the period the revenue is earned or the expenses are incurred, irrespective of cash flow.

For the year ended December 31, 2017, the Watermaster included revenue and expenses that were related to the year ended December 31, 2016. The following adjustment was recorded to properly report the revenues and expenses of the Watermaster for the year ended December 31, 2017.

**HEMET-SAN JACINTO WATERMASTER**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**For the Year Ended December 31, 2017**

**NOTE 4: PRIOR YEAR RESTATEMENT**

Net Position - Beginning of Year	
Before restatement	\$ 1,171,219
Revenue attributed to December 31, 2016	
assessments	73,532
Expenses for operating activities occurring	
as of December 31, 2016	<u>(28,399)</u>
Prior year restatement	<u>45,133</u>
Net Position - Beginning of Year as restated	<u><u>\$ 1,216,352</u></u>

**OTHER INDEPENDENT AUDITOR'S REPORT**



**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**

Board of Directors  
Hemet-San Jacinto Watermaster  
Corona, 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 Hemet-San Jacinto Watermaster (the Watermaster), as of and for the year ended December 31, 2017 and the related notes to the financial statements, which collectively comprise the Watermaster’s basic financial statements, and have issued our report thereon dated February 28, 2018.

**Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Watermaster’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 Watermaster’s internal control. Accordingly, we do not express an opinion on the effectiveness of the Watermaster’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 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.

**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***

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 have not been identified. We identified a deficiency in internal control, as described in the accompanying schedule of findings and responses that we consider to be a material weakness, see finding 2017-001.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Authority’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 non-compliance 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 Authority's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



CliftonLarsonAllen LLP  
Glendora, California  
February 28, 2018

## **FINDINGS AND RESPONSES**

**HEMET-SAN JACINTO WATERMASTER**  
**SCHEDULE OF FINDINGS AND RESPONSES**  
**December 31, 2017**

NOTE: The finding and recommendation listed below includes details about the criteria or specific requirements, the condition, the effect and the cause. The response that follows the finding is the Watermaster's corrective action plan.

**2017-001 RECONCILIATION AND CLOSING PROCESS**

**Finding:** Our audit procedures revealed the lack of a systematic method wherein complete monthly closing procedures take place to ensure that revenues and expenses are accrued into the proper reporting period. A lack of specific closing procedures to ensure proper accruals may ultimately cause significant errors in the financial records and statements as well as allow possible irregularities, including fraud, to exist and continue without notice. We noted the following deficiencies:

- The accounts receivable balances were not properly identified as of December 31, 2017 and December 31, 2016, resulting in incorrect revenue recognition for 2017 and a prior year restatement for 2016. As a result, accounts receivable balances were not properly recorded.
- The accounts payable balances were not properly identified as of December 31, 2017 and the December 31, 2016 accounts payable balances were not properly reversed, resulting in expense recognition in the wrong periods. As a result, accounts payable balances were not properly recorded.

This condition resulted in a prior year restatement of net position and correction of misstatements in the current year financial statements.

**Recommendation:** Establish a system of closing procedures to ensure revenue and expenses are recorded in the proper period in order to prepare financial statements in accordance with US generally accepted accounting principles that are free from material misstatement.

**Watermaster Response:**

The Advisor will terminate Bell Bookkeeping Services and use Water Resources Engineers services for future bookkeeping activities, after receiving feedback from the Watermaster Board at its February 2018 Board meeting. Water Resources Engineers will establish a system of closing procedures to properly record revenue and expenses in the proper period in order to provide more accurate financial statements.



**HEMET-SAN JACINTO WATERMASTER**

**STATUS OF PRIOR YEAR FINDINGS**

**December 31, 2017**

There were no findings related to the basic financial statements for the year ended December 31, 2016.