

**PANOCHÉ DRAINAGE DISTRICT
FIREBAUGH, CALIFORNIA**

FINANCIAL STATEMENTS

**FOR THE YEAR ENDED
FEBRUARY 29, 2020**

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
Panoche Drainage District
Firebaugh, California

Report on the Financial Statements

We have audited the accompanying financial statements of Panoche Drainage District (the "District") as of and for the year ended February 29, 2020, and the related notes to the financial statements, which collectively comprise the District'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 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 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 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 District's preparation and fair presentation of the financial statements to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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Opinions

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

Other Matters

Required Supplementary Information

Management has omitted the management discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated August 10, 2021, on our consideration of the 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 the effectiveness of the District's 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 the District's internal control over financial reporting and compliance.

Price Pange & Company

Clovis, California
August 10, 2021

**PANOCHÉ DRAINAGE DISTRICT
STATEMENT OF NET POSITION
FEBRUARY 29, 2020**

ASSETS

Current assets:

Cash and cash equivalents	\$ 1,692,842
Accounts receivables, net of allowance of \$25,628	717,262
Interest receivable	1,758
Prepaid expense	<u>88,966</u>

Total current assets 2,500,828

Other assets:

Capital assets, net of accumulated depreciation	<u>43,883,119</u>
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Total other assets 43,883,119

Total assets \$ 46,383,947

LIABILITIES

Current liabilities:

Accounts payable and accrued expenses	\$ 5,149,398
Current portion of notes payable	<u>342,009</u>

Total current liabilities 5,491,407

Noncurrent liabilities:

Long-term liabilities	<u>1,177,858</u>
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NET POSITION

Net investment in capital assets	43,883,119
Unrestricted	<u>(4,168,437)</u>

Total net position 39,714,682

Total liabilities and net position \$ 46,383,947

The notes to the basic financial statements are an integral part of this statement.

**PANOCHÉ DRAINAGE DISTRICT
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED FEBRUARY 29, 2020**

OPERATING REVENUES	
SJRIP farming revenue	\$ 1,297,318
Drainage assessment fees	2,529,812
Delinquent accounts charges	151,956
Other District reimbursements	290,971
Fresno County property revenue	232,856
SJRIP participant dues	<u>800,976</u>
Total operating revenues	<u>5,303,889</u>
OPERATING EXPENSES	
SL&DM water authorities' fees	1,392,261
Contract labor and benefits	1,394,157
Custom farming	980,387
Utilities	742,583
Depreciation	1,162,104
Fuel	266,002
Chemicals	197,655
Contract services – Panoche Water District	596,195
Repairs and maintenance	198,987
Supplies and small tools	114,424
Office	5,561
Professional fees	191,513
Wires, structures and gates	246,321
Other	6,698
Assessments and property taxes	184,847
Drainage studies and tests	13,679
Insurance	105,032
Laboratory	8,799
Bad debt expense	<u>19,492</u>
Total operating expenses	<u>7,826,697</u>
Operating income (loss)	<u>(2,522,808)</u>
NONOPERATING REVENUES (EXPENSES)	
Grant revenue	385,170
Interest income	8,392
Interest expense	<u>(23,787)</u>
Nonoperating revenues (expenses)	<u>369,775</u>
Change in net position	(2,153,033)
Net position, beginning of year, restated	<u>41,867,715</u>
Net position, end of year	<u>\$ 39,714,682</u>

The notes to the basic financial statements are an integral part of this statement.

**PANOCHÉ DRAINAGE DISTRICT
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED FEBRUARY 29, 2020**

CASH FLOWS FROM OPERATING ACTIVITIES	
Receipts from customers and others	\$ 5,852,154
Payments to suppliers	<u>(6,602,216)</u>
Net cash provided by (used in) by operating activities	<u>(750,062)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Acquisition of capital assets	(385,170)
Payments on long-term debt	(519,063)
Proceeds from new debt	1,712,930
Interest paid on notes payable	<u>(31,799)</u>
Net cash provided by (used in) by capital and related financing activities	<u>776,898</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
Grants received	<u>385,170</u>
Net cash provided by (used in) by noncapital and financing activities	<u>385,170</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Interest revenue	<u>8,257</u>
Net cash provided by (used in) by investing activities	<u>8,257</u>
Net increase (decrease) in cash	420,263
Cash and cash equivalents, beginning of year	<u>1,272,579</u>
Cash and cash equivalents, end of year	<u><u>\$ 1,692,842</u></u>

The notes to the basic financial statements are an integral part of this statement.

**PANOCHÉ DRAINAGE DISTRICT
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED FEBRUARY 29, 2020
(Continued)**

**Reconciliation of Operating Income (Loss) to Net Cash Provided
(Used) by Operating Activities:**

Operating income (loss)	\$ (2,522,808)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:	
Depreciation expense	1,162,104
Bad debt expense	19,492
(Increase) decrease in accounts receivable	548,265
(Increase) decrease in prepaid expense	(10,130)
Increase (decrease) in accounts payable and accrued expense	<u>53,015</u>
 Net cash provided (used) by operating activities	 <u>\$ (750,062)</u>

Supplemental Disclosure of Cash Flow Information

Cash paid for interest (net of amount capitalized)	<u><u>\$ 31,799</u></u>
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The notes to the basic financial statements are an integral part of this statement.

**PANOCHÉ DRAINAGE DISTRICT
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED FEBRUARY 29, 2020**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Reporting Entity

Panoche Drainage District (the “District”) was organized October 1, 1957, under the provisions of the Water Act of 1903 to provide for the water for certain agricultural lands, other than swamp and overflow lands, located in Fresno and Merced Counties. The District operates as a nontaxable state governmental entity and is governed by its own Board of Directors elected by users from Panoche, Eagle Field, Oro Loma and Mercy Springs Water Districts.

Basis of Presentation and Accounting

The financial statements of the District are presented using the full accrual method of accounting and conform to accounting principles generally accepted in the United States of America and with the policies and procedures of the office of the State Controller, State of California.

The accounts of the District are organized based on a proprietary fund type; specifically, an enterprise fund. The activities of this fund are accounted for with a set of accounts that comprise the District’s assets, liabilities, net position, revenues and expenses. Enterprise funds account for activities (i) that are financed with debt that is secured solely by a pledge of the net revenue from fees and charges of the activity; or (ii) that are required by law or regulation that the activity’s costs of providing services, including capital costs (such as depreciation or debt service), be recovered with fees and charges, rather than with taxes or similar revenue; or (iii) that the pricing policies of the activity establishes fees and charges designated to recover its costs, including capital costs (such as depreciation or debt service).

The accounting and financial reporting treatment applied to the District is determined by its measurement focus. The transactions of the District are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations are included on the statement of net position. Net position (i.e., total assets less total liabilities) are segregated into net investment in capital assets, restricted and unrestricted components.

Budgetary Procedures

The District operates under a budget prepared and approved by the Board of Directors. The budget is prepared on a detailed line-item basis. Revenue is budgeted by use (services and supplies, other charges, drainage supply and contingencies). Once approved, the Board of Directors may amend the adopted budget when unexpected modifications are required in estimated revenues and expenditures or expenses.

The District follows these procedures in establishing the budgetary data: (a) prior to the beginning of the year, the budget is legally enacted through passage of a resolution and (b) budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America, except that loan and bond proceeds are treated as other financial sources, and loan and bond principal payments and fixed asset purchases are treated as expenditures.

Assets, Liabilities and Net Position

Cash and Cash Equivalents

For purposes of the statement of cash flows, the District considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents.

Receivables

All receivables are reported at their gross value and, where appropriate, are reduced by the estimated portion that is expected to be uncollectible.

**PANOCHÉ DRAINAGE DISTRICT
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED FEBRUARY 29, 2020**

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Assets, Liabilities and Net Position (Continued)

Capital Assets

Capital assets (fixed assets) are stated at historical cost, except for donated assets, which are stated at fair value on the date donated. It is the policy of the District to capitalize all property, plants and equipment (except equipment with a cost of less than \$5,000). Costs of assets sold or retired are eliminated from the accounts in the year of disposition, and the resulting proceeds, if any, are recorded as proceeds of sales in the applicable fund. Depreciation is recorded on enterprise fund fixed assets using the straight-line method. The estimated useful life for the irrigation distribution system of the District is 50 years.

Operating Revenue and Expense

Operating revenues and expenses consist of those revenues that result from ongoing principal operations of the District. Operating revenues consist primarily of charges for services and farming revenues. Nonoperating revenues and expenses consist of those revenue and expense items that are related to financing and investing type of activities and results from nonexchange transactions or ancillary activities. When an expense is incurred for purposes for which there are both restricted and unrestricted net position available, it is the District's policy to apply those expenses to restricted net position to the extent such are available and then to unrestricted net position.

Net Position

Net position comprises the various net earnings from operating income, nonoperating revenue, expenses and capital contributions. Net position is classified in the following three components:

Net investment in capital assets – This component of net position consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction or improvements of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent process is not included in the calculation of net investment in capital assets. Rather, that portion of the debt is included in the same net components as the unspent proceeds.

Restricted – This component of net position consists of constraints imposed by creditors (such as through debt covenants), grantors, contributors or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted – This component of net position consists of net position that does not meet the definition of restricted or net investment in capital assets.

Estimates

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

**PANOCHÉ DRAINAGE DISTRICT
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED FEBRUARY 29, 2020**

NOTE 2 – CASH AND CASH EQUIVALENTS

Unrestricted cash and cash equivalents as of February 29, 2020 consist of the following:

Cash in Fresno County Treasury	\$ 129,981
Cash in bank – business checking and savings	1,042,908
Local Agency Investment Fund	<u>519,953</u>
 Total cash and cash equivalents	 <u>\$ 1,692,842</u>

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 District maintains its cash balances in one financial institution: Rabobank, N.A. The balances are insured by the federal deposit insurance corporation up to \$250,000.

The District's deposits as of February 29, 2020, were entirely covered by federal depository insurance or otherwise collateralized. The Government Code of the State of California requires California financial institutions to secure District deposits by pledging government securities as collateral.

The market value of pledged securities must equal at least 110 percent of the District's deposits. California law also allows financial institutions to secure the District's deposits by pledging first deed of mortgage notes having a value of at least 150 percent of the District's total deposits.

Investments Authorized

The District strives to maintain the level of investment of idle funds as near to 100 percent as possible and operates its pooled idle cash investments under the Prudent Investor Standard. This affords a broad spectrum of investment opportunities so long as the investment is deemed prudent and is permissible under currently effective legislation of the State of California and other imposed legal restrictions. Permitted investments are identified in Section 53635 of the Government Code of California. Criteria for selecting investments and the absolute order of priority are safety, liquidity and yield. The primary basic premise underlying the District's investment policy is to insure the safety of principal and to provide funds when needed. A high dollar yield on investments, though important, ranks third in the priority of investment strategy.

Investment maturities are selected to anticipate cash needs, thereby obviating the need for forced liquidation and the accompanying loss of interest income.

The District operates its investment program with many Federal, State and self-imposed constraints. It does not buy stocks; it does not speculate; and it does not deal in futures, options or security loan agreements. Longer-term investments (over one year) are generally limited to maturities of five years or less.

To maximize investment income, the District uses all available, economically feasible investment aids. Economic conditions and various money markets are monitored to assess the probable course of interest rates.

**PANOCHÉ DRAINAGE DISTRICT
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED FEBRUARY 29, 2020**

NOTE 2 – CASH AND INVESTMENTS (Continued)

Local Agency Investment Fund (LAIF)

The District participates in an external investment pool, as defined by the Government Accounting Standards Board (GASB) Statement No. 31, by way of its funds on deposit in the Local Agency Investment Fund (LAIF) managed by the State of California Treasurer and is not registered with the Securities and Exchange Commission. These funds are pooled with those of other agencies in the State and invested in accordance with State guidelines. The value of the District's shares in the LAIF that may be withdrawn is determined on an amortized costs basis, which may be different from the fair value of the District's position in the pool. The District's portion of the February 29, 2020 balance was \$519,953.

Cash in Fresno County Treasury

The District maintains cash deposits with the Fresno County Auditor-Controller/Treasurer and voluntarily participates in the common investment pool of the County. The fair value of the District's investment in the pool is reported in the accompanying financial statements at amounts based upon the District's pro-rata share of the fair value provided by the County Treasurer for the entire portfolio. The balance available for withdrawal is based on the accounting records maintained by the County Treasurer and is recorded on the amortized cost basis. Because the District's deposits are maintained in a recognized pooled investment fund under the care of a third party, and because the District's share of the pool does not consist of specific, identifiable investment securities owned by the District, no disclosure of the individual deposits and investments or related custodial credit risk classifications is required. In accordance with applicable state laws, the Fresno County Treasurer may invest in derivative securities with the State of California. However, at February 29, 2020, the Fresno County Treasurer has represented that the Pooled Investment Fund contained no derivatives or other investments with similar risk profiles. The District's portion of the February 29, 2020 balance was \$129,981.

Credit Rate Risk

Credit rate 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. At February 29, 2020, the LAIF managed by the State of California and the Fresno County investment pool were not rated.

Concentration of Credit Rate Risk

The investment policy of the District contains no limitations on the amount that can be invested in any one issuer beyond that stipulated by the California Government Code. Investments in any one issuer (other than U.S. Treasury securities, mutual funds, and external investment pools) did not exceed 5 percent or more of total District investments.

Fair Value

LAIF and The Fresno County Treasury investment pools invest in numerous types of investments ranging all levels in the fair value hierarchy, and, accordingly, are not investment types that can be categorized in any particular level in the fair value hierarchy.

**PANOCHÉ DRAINAGE DISTRICT
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED FEBRUARY 29, 2020**

NOTE 3 – ACCOUNTS RECEIVABLE

Accounts receivable consists of the following at February 29, 2020:

Participants' dues – San Joaquin River Improvement Project	\$	169,940
Drainage service charges		107,357
Other drainage activities charges		80,423
Grants		385,170
Allowance for doubtful accounts		<u>(25,628)</u>
 Total accounts receivable	 \$	 <u>717,262</u>

NOTE 4 – CAPITAL ASSETS

Following is a summary of activity affecting capital assets for the year ended February 29, 2020:

	Balance Mar 1, 2019	Additions	Transfers	Balance February 29, 2020
Nondepreciable assets:				
SJRIP land	\$ 27,803,183	\$ -	\$ -	\$ 27,803,183
Construction in progress	<u>-</u>	<u>385,170</u>	<u>-</u>	<u>385,170</u>
Total nondepreciable assets	<u>27,803,183</u>	<u>385,170</u>	<u>-</u>	<u>28,188,353</u>
Depreciable assets:				
SJRIP land improvements	20,254,903	-	-	20,254,903
Buildings and improvements	1,761,414	-	-	1,761,414
Equipment	1,653,009	-	-	1,653,009
GDMIP land improvements	<u>787,606</u>	<u>-</u>	<u>-</u>	<u>787,606</u>
Total capital assets, being depreciated	<u>24,456,932</u>	<u>-</u>	<u>-</u>	<u>24,456,932</u>
Less accumulated depreciation	<u>(7,600,062)</u>	<u>(1,162,104)</u>	<u>-</u>	<u>(8,762,166)</u>
Total capital assets, being depreciated, net	<u>16,856,870</u>	<u>(1,162,104)</u>	<u>-</u>	<u>15,694,766</u>
Total capital assets	<u>\$ 44,660,053</u>	<u>\$ (776,934)</u>	<u>\$ -</u>	<u>\$ 43,883,119</u>

Depreciation expense for the year ended February 29, 2020 was \$1,162,104.

**PANOCHÉ DRAINAGE DISTRICT
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED FEBRUARY 29, 2020**

NOTE 5 – ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Following is a summary of accounts payable and accrued expenses as of February 29, 2020:

Trade payables	\$ 343,034
Due to Panoche Water District	<u>4,806,364</u>
 Total accounts payable and accrued expenses	 <u>\$ 5,149,398</u>

NOTE 6 – LONG-TERM LIABILITIES

Following is a summary of noncurrent (long-term) liabilities for the year ended February 29, 2020:

Note payable to Panoche Water District, with monthly payment of \$17,419 including principal and interest at 1.75%, maturity March 2024	\$ 806,937
Note payable to Panoche Water District, with monthly payment of \$12,810 including principal and interest at 3%, maturity February 2025	<u>712,930</u>
Total long-term debt	1,519,867
Less: Amounts due within one year	<u>(342,009)</u>
Total long-term debt, due after one year	<u>\$ 1,177,858</u>

Total maturities on long-term debt are as follows at February 29, 2020:

2021	\$ 342,009
2022	310,034
2023	345,629
2024	370,941
2025	<u>151,254</u>
	 <u>\$ 1,519,867</u>

State Water Resources Control Board (SWRCB) – Ag Water Loan Program (ADLP #2)

The District has contracted with SWRCB to borrow a maximum of \$4,000,000 (Phase 2) for the purpose of purchasing sprinkler, gated pipe and drip irrigation equipment for lease to District landowners. The revenue plan in place by the District will ensure that the lease payments received from the landowners will cover the entire amount of the costs of this program. Payments on the obligation were due in 13 annual installments of \$341,834, including interest at the rate of 2.40 percent per annum. During the year ended February 29, 2020, the District paid the debt in full.

**PANOCHÉ DRAINAGE DISTRICT
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED FEBRUARY 29, 2020**

NOTE 7 – COMMITMENTS AND CONTINGENCIES

Litigation

The District is currently under investigation by the United States Attorney's Office, the Federal Bureau of Investigation, the Internal Revenue Service, Criminal Investigations Division and the United States Bureau of Reclamation/Office of the Inspector General of the Department of the Interior ("OIG"). The investigation involves general financial and accounting controls of the District, and more particularly, of the Panoche Water District, including examining whether personnel of the Water District may have misused District credit cards for personal, rather than business, expenses. Also, the investigation is reviewing issues concerning whether certain payments for housing, utilities and other housing-related expenses paid to Panoche Water District employees who were assigned to Drainage District activities were appropriately treated as business, rather than personal expenses benefiting the employees. The Panoche Water District has adopted and implemented written policies and adopted an Ethics & Compliance Program to address these issues, and the Drainage District does not have information sufficient to conclude if claims or litigation against either District or any individuals will result or if the claims were asserted, the likely outcome, or the range of the District's liability.

The District is also under investigation by the Civil Division of the United States Attorney's Office in conjunction with the OIG relating to financial assistance agreements between the Bureau of Reclamation and the District. Those grants were suspended in April 2017, and there have been no further invoices to the grants. The District understands that this investigation is focused on potentially false claims relating to these federal grants and may in part be focused on employee compensation invoiced by Panoche Water District for work provided on grant projects, as well as on Panoche Drainage District claims for reimbursement for equipment and inventory. The investigation also appears to include an examination of the revenue generated from the crops developed through the grant programs. The District and the Panoche Water District are seeking a resolution of the Federal Civil Investigation. The grants form part of the basis for resolution, and the District does not anticipate that the government has additional claims under the grant suspension outside of the resolution that are probable of assertion.

A separate audit by the OIG of the District's performance of obligations under a cooperative agreement for the federally owned Drainage Treatment Plant resulted in the issuance of Final Audit Report R2017-WR-0048, July 2018, which identified \$20,077 of the audited costs as unsupported and \$193,814 as unallowable, for a total of \$213,891 in questioned costs. On June 26, 2020, the District received the Bureau of Reclamation's Final Determination Regarding Panoche Drainage District Report No. 2017-WR-048, Findings 1-17; Cooperative Agreement R1AC00087, as a result of which Reclamation determined that instead of \$213,891 in costs questioned as unallowable or unsupported, only \$2,937 was in fact unallowable or unsupported and of that, the District had credited Reclamation with \$751, leaving \$2,186 owed by the District to Reclamation. That amount was paid on July 17, 2020, the bank account for the Cooperative Agreement was closed, and the District anticipates no further action.

The Drainage District understands that the Water District or certain individuals previously or currently associated with the Water or Drainage Districts have been investigated by the California Department of Justice. On February 20, 2018, the Department filed a criminal complaint against the former General Manager, Office Manager and Manager of the District's San Joaquin River Improvement Project alleging, in relevant part, conspiracy and embezzlement and misappropriation of public resources. On February 21, 2019, the former General Manager and former Office Manager were each ordered to be held over for trial on counts of embezzlement and misappropriation of public funds relating to the Panoche Water District. However, charges against the former Manager of the Drainage District's San Joaquin River Improvement Project, were dropped. No charges were instituted against the Drainage District itself or its Board of Directors and the District does not anticipate that any such charges will be instituted.

**PANOCHÉ DRAINAGE DISTRICT
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED FEBRUARY 29, 2020**

NOTE 7 – COMMITMENTS AND CONTINGENCIES (Continued)

Litigation (Continued)

Finally, in 2018, the United States Environmental Protection Agency (USEPA) issued a Notice of Suspension to Panoche Water District and Panoche Drainage Districts, suspending the Districts from participation in federal contracts and assistance activities. Upon the District's request to convert the Notice of Suspension to an Order to Show Cause, the acting EPA Suspending and Debarring Official ("SDO") terminated the Districts' suspension and issued a Show Cause Notice based on substantially the same underlying concerns as the initial Notice of Suspension. The Districts responded to the EPA's concerns as stated in the terminated Notice of Suspension and Show Cause Notice, and detailed the steps they had taken as of June 2018 to remedy the circumstances that served as bases for the Notice of Suspension. The Districts also responded to what the EPA later characterized as outstanding concerns, following which, while the Districts understand the EPA reserves its rights to take action based upon new information, the Districts do not anticipate any further action by the EPA, continue to implement the mitigation policies and practices reported to EPA, and continue to be eligible for federal contracts and assistance agreements.

Going Concern

As indicated in the accompanying financial statements, the District showed a decrease in net position of \$1,941,535 during the year ended February 29, 2020. As of that date, the District's current liabilities exceeded its current assets by \$2,990,580. The majority of the current liabilities stem from related-party transactions that have accumulated over the years and can be categorized into two areas: the San Joaquin River Water Quality Improvement Project (SJRIP) specific costs and the Panoche Drainage District (PDD) specific costs. The liabilities related to the SJRIP primarily stem from its service rate being set too low from the fiscal year ending 2018 through 2020, thereby creating a need for cash. This was a period of significant transition for the SJRIP as a new District management team was established, revenues from grants ceased, and governance and financial responsibility for the SJRIP was being transformed through the formation of a new joint-powers authority, the Grassland Basin Authority. The joint powers agreement was signed in June 2019. During this transition period, services to the District and SJRIP continued to be provided by the Panoche Water District. While cognizant of the growing liability, as the largest entity dependent upon the essential drainage management service provided by the SJRIP, and in the interest of facilitating the transition to the joint-powers authority, the Water District, by providing labor and other management services to the SJRIP on a reimbursement basis, allowed the accumulation of the outstanding current liabilities as the SJRIP could not meet its reimbursement obligations as and when they fell due. Following the example of the 2019 repayment agreement between the District and the Water District, the District is working with the Grassland Basin Authority to establish a process to validate the liability and a repayment schedule. Management expects an agreement with the Grassland Basin Authority to be executed prior to the end of the current 2022 fiscal year. As for costs directly related to the PDD, management has set drainage service rates to adequately cover the annual operating expenses. In addition, in cooperation with the Water District, management has reduced operational expenses by reducing the workforce and improving maintenance and cost allocation practices. These efforts, coupled with revenues from Fresno County property tax funds and reimbursement of Proposition 84 state grant expenditures will allow the District to make payments towards the outstanding liabilities without compromising its current liquidity position. Successful implementation of these ongoing efforts will result in the District continuing as a going concern. The financial statements do not include any adjustments that might be necessary if the District is unable to continue as a going concern.

NOTE 8 – RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction to assets; errors and omissions; injuries to employees; and natural disasters. The District is self-insured for the first \$2,500 in claims paid for automobile and general liability claims. The District is a member of the Association of California Water Agencies (ACWA) Joint Powers Insurance Authority (the "Authority"). The Authority was created to formulate, develop, and administer a program of self-insurance for its members. The District pays an annual premium to the Authority for automobile and general liability insurance. The District accounts for premiums paid as a pooling of risk arrangement and thus expense premiums as they are paid. The Authority has the right to make retrospective adjustments to premium deposits based on actual claims paid.

**PANOCHÉ DRAINAGE DISTRICT
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE YEAR ENDED FEBRUARY 29, 2020**

NOTE 9 – PRIOR PERIOD ADJUSTMENT

In the prior year, as a result of an accounting error, the District did not recognize \$211,499 of drainage revenue. Accordingly, the District is increasing its beginning net position balance to account for this revenue.

Net position, as previously reported:	\$ 41,656,216
Increase in drainage revenue	<u>211,499</u>
Net position, beginning of year, restated	<u>\$ 41,867,715</u>

NOTE 10 – RELATED ORGANIZATIONS

The District's Governing Board presides as the Panoche Water District's Governing Board, Panoche Water District is a separate Special District organized to furnish irrigation water to District land in Fresno and Merced Counties, California. A separate audit is performed for Panoche Water District and financial information of Panoche Water District can be obtained by writing to the Panoche Water District's Controller at 52027 W. Althea Avenue, Firebaugh, CA 93622.

The District reimburses Panoche Water District for the cost of providing the District with personnel and other services. The total amount charged to the District by Panoche Water District for the year ended February 29, 2020 was approximately \$1,991,000.

NOTE 11 – CONTINGENCY

On March 11, 2020, the World Health Organization declared the outbreak of a coronavirus (COVID-19) a pandemic. Accordingly, some functions of the District's operations have been limited to protect the health and safety of its employees. The financial impact that could occur as a result of the pandemic is unknown at this time.

NOTE 12 – SUBSEQUENT EVENTS

Management has evaluated and concluded that there are no subsequent events that have occurred from February 29, 2020 through the date the financials were available to be issued at August 10, 2021, that would require disclosure or adjustment.

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OTHER AUDITOR'S REPORT

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Directors of
Panoche Drainage District
Firebaugh, California

We have audited, in accordance with the 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 Panoche Drainage District (the "District"), as of and for the year ended February 29, 2020, and the related notes to the basic financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated August 10, 2021.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the District'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 the 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the 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*.

570 N. Magnolia Avenue, Suite 100
Clovis, CA 93611

tel 559.299.9540

fax 559.299.2344

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 District'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 District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Price Page & Company

Clovis, California
August 10, 2021

FINDINGS AND QUESTIONED COSTS

**PANOCHÉ DRAINAGE DISTRICT
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED FEBRUARY 29, 2020**

SECTION I – SUMMARY OF AUDITOR’S RESULTS

Financial Statements

Type of auditor's report issued:	Unmodified
Internal control over financial reporting: Material weaknesses identified?	_____ Yes <u> X </u> No
Significant deficiencies identified that are not considered to be material weaknesses?	_____ Yes <u> X </u> No
Noncompliance material to financial statements noted?	_____ Yes <u> X </u> No

SECTION II – FINANCIAL STATEMENT FINDINGS

None reported.

**PANOCHE DRAINAGE DISTRICT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED FEBRUARY 29, 2020**

FINANCIAL STATEMENT FINDINGS

Finding 2019-001 Financial Close and Reporting Process (Significant Deficiency)

Condition:

The District did not properly record receivables, revenues, expenses and capital assets during the year-end closing process. During our audit, we identified these errors and proposed the necessary accounting entries to correct the balances of these accounts.

Criteria:

A strong system of internal control and management review requires that general ledger account balances be properly reconciled to a subsidiary ledger or other adequate supporting documentation on a periodic basis, as well as during the year-end financial close process. Management is responsible for maintaining its accounting records in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP).

Cause:

Internal control over the year-end financial reporting process were not properly designed and were not placed in operation.

Effect:

As a result of this condition, payables, receivables, expenses, revenues and net position were initially materially misstated. Specifically, the misstatements were as follows:

- Prepaid expenses – overstated by \$322,880.
- Expenses – SJRIP – dues – understated by \$322,880
- Revenue – SJRIP PRJ – crops and rent – overstated by \$56,579
- Accounts receivable – drainage – SJRIP – overstated by \$56,579.
- Depreciation expense – overstated by \$399,594
- Accumulated depreciation – overstated by \$399,594.
- Account receivable – grant – understated by \$142,759
- Rabobank, N.A., cash account – overstated by \$142,759.

Recommendation:

We recommend that the District create a year-end financial closing checklist that includes the necessary steps, in detail, that should be undertaken at year-end to ensure proper reconciliation and reporting of all significant account balances.

Current Status as of February 29, 2020:

Implemented.

**PANOCHE DRAINAGE DISTRICT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED FEBRUARY 29, 2020
(Continued)**

FINANCIAL STATEMENT FINDINGS (Continued)

Finding 2019-002 Accounts Receivable Reconciliation (Significant Deficiency)

Condition:

The District did not reconcile receivables recorded in the STORM billing system to the general ledger accounting system (SAGE) on a monthly basis.

Criteria:

A strong system of internal control and management review requires that general ledger account balances be properly reconciled to a supplemental billing accounting system on a periodic basis, as well as during the year-end financial close process. Management is responsible for maintaining its accounting records in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP).

Cause:

Internal control over the accounts receivable reconciliation process were not properly designed and were not placed in operation.

Effect:

Not determined.

Recommendation:

We recommend that the District create a monthly financial closing checklist that includes the necessary steps, in detail, that should be undertaken on a monthly basis to ensure proper reconciliation of accounts receivable records.

Current Status as of February 29, 2020:

Implemented.