Pajaro Valley Water Management Agency
Directors Needing Direction

When tillage begins, other arts follow.
The farmers therefore are the founders of human civilization.
Daniel Webster (1782-1852)

Summary

The Pajaro Valley Water Management Agency (PVWMA or Agency), created in 1984, is the primary agency in Santa Cruz County tasked with the resolution of saltwater intrusion into the Pajaro Valley aquifer. This Agency is governed by a seven-member board of directors and has an annual budget of over $10 million.

The problem of saltwater intrusion into the Pajaro Valley aquifer has been recognized for over 60 years, and this issue remains a serious concern for farmers and citizens. "The California State Water Resources Control Board (SWRCB) conducted an extensive investigation on water supply in Santa Cruz and Monterey Counties in 1953. It was concluded that the Pajaro Valley groundwater basin was in a state of overdraft causing saltwater intrusion. By the 1970's, groundwater levels in Watsonville were below sea level the majority of the year. In 1980, the SWRCB identified the Pajaro Valley basin as one of eleven California basins with critical conditions of overdraft. By 2000, 54 square miles of the basin were below sea level."[1]

The Grand Jury's research into the financial stability of PVWMA over the last five years introduced us to an agency that has disregarded annual audit admonishments about procedures needed to protect it from fraud and theft. Investigation into its administrative style revealed an organization which only casually adheres to written policies and has an absence of leadership on the part of the Board of Directors.

Background

In 1980, the State Department of Water Resources named the Pajaro Valley basin one of 11 water basins in California with critical conditions of overdraft, "the condition of the groundwater basin where the average annual amount of water extracted exceeds the average annual supply of fresh water to the basin." In response, then-State Senator Henry Mello introduced legislation in 1984 to create the PVWMA, and it was approved by local voters in the November 1984 election.[2] The threat of insufficient water to support the substantial agricultural production of the Pajaro Valley is made worse by the risk of seawater intrusion into the wells of coastal farmers as a consequence of the overdraft.[3]

In June 1998, local voter initiative Measure D restricted the maximum augmentation (pumping of groundwater) fee to $50 per acre-foot.[4] Beginning in 2002, the Agency increased this fee several times and since then has been the subject of multiple lawsuits related to fee increases. The most damaging litigation was a 2007 appellate court ruling compelling the Agency to reduce the augmentation fee from $160 to $80 per acre-foot, and requiring the PVWMA to refund $13.5 million in excess fees collected between 2003 and 2007.[5] The refunds were paid over three years from 2008 to 2011. An August 3, 2011 PVWMA press release stated: "PVWMA made the final payout of $1,270,000 in refunds this week and is finished paying the total of $11,264,705 agreed to in a court settlement. Key to the survival of the agency while financially hamstrung from the rates reduction and refunds was the willingness of several agricultural entities to take credits against future water use, rather than an actual payout."[6] These credits totaled almost $2,200,000.

Given the financial costs of resolving this lawsuit, we were interested to see an article in the Santa Cruz Sentinel that PVWMA had been awarded a grant of $4 million from the U.S. Bureau of Reclamation's Title XVI Water SMART program.[7] In order to better understand its financial position, we reviewed the Agency's annual audits from fiscal year 2007-08 through 2011-12. The recommendations included in these audits raised concern that the Agency did not have adequate accounting procedures to protect itself from fraud, mismanagement, and further litigation expenses.

Scope

The Grand Jury examined the third-party audits of PVWMA from 2007-08 through 2011-12 and also looked at Board meeting minutes and Agency correspondence related to those audits. We interviewed staff and Board members of PVWMA, inquiring specifically about the Agency's review of, and response to, the findings of the auditors. In addition, we looked at what information was available on its website and attended regular meetings of the PVWMA Board of Directors.

Investigation

Initially, the Grand Jury became interested in PVWMA Board's responses when the Agency's third-party auditors, Bartlett, Pringle & Wolf (BP&W), noted that the same issues were left unresolved three to five years in a row. We examined the Agency's financial statements as well as the auditors' reports on them. This led us to inquire into the Board's oversight and decision-making processes.

Review of Third-Party Audits

In examining the third-party audits, we were struck by how often the same shortcomings were noted year after year. These fell into two categories: Material Weaknesses and Control Deficiencies.

Recurring Material Weaknesses

The auditor's definition of a Material Weakness is "a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control."[8] If a Material Weakness contributed to a material misstatement of the financial statements, it could give an unrealistic picture of PVWMA's financial condition. This could jeopardize the Agency's ability to obtain further funding.

The total number of Material Weaknesses noted by the auditors in the last five audits was:

- 2007-08: 6
- 2008-09: 3
- 2009-10: 6
- 2010-11: 1
- 2011-12: 4

The recurring Material Weaknesses are shown in the table below. As with the Material Weaknesses themselves, many of the management responses shown in Appendix A are repeated year after year. In each year, management responded that it would address the issues, but the auditors determined that it had not done so.

Table 1. Recurring Material Weaknesses

Material Weakness	2007-08	2008-09	2009-10	2010-11	2011-12
Bank statements and Bank Reconciliations not reviewed by a second person	X	X	X		X
Inaccurate Recording of Grant Revenue in governmental funds and government-wide financial statements	X		X	X	X
Journal Entry not reviewed by a second person	X	X	X		X
Noncompliance with 1999 Certificates of Participation Debt Covenants	X	X	X		*

* Not listed as a Material Weakness in 2011-12, but further recommendations made: calculate quarterly vs. semi-annually, incorporate into budget process, present to Board of Directors.

The last Material Weakness in the above table relates to the 1999 Certificates of Participation in which the Agency has agreed to fix, prescribe, and collect rates and charges for water service which will be at least sufficient to yield net revenue equal to 125% of the debt service payable in a fiscal year.

The achievement of eliminating all but one Material Weakness in the 2010-11 audit was credited by the auditors to the Administrative Services Manager (ASM) working at the Agency at that time.[9] However, the Agency decided not to retain that ASM in early 2012, leaving the position vacant until the current ASM was hired in October of that year.

A complete list of the auditors' findings, and management's responses, may be found in Appendix A.

Recurring Control Deficiencies

In addition to the Material Weaknesses noted above, the auditors also identified, via letters to management separate from the audits (Separate Letters), a number of recurring Control Deficiencies. The auditors state that a Control Deficiency 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 misstatements on a timely basis."[8] One Director referred to these Deficiencies as "not important enough to rise to the level of a[n audit] finding."

Although there were several, we chose to focus on only two of the Control Deficiencies: segregation of duties and control of credit cards.

1. <u>Segregation of Duties</u>

The auditors noted that because so few individuals are involved in the majority of accounting and financial duties, there is a lack of internal control over duties that are usually segregated. The auditors recommended additional supervision and periodic review procedures in order to alleviate this deficiency.

The auditors recommended that PVWMA should be segregating duties to address the following problems:

- The person who is responsible for processing of payroll also reconciles the payroll accounts, distributes the payroll checks and accounts for payroll checks
- Materials and supply orders are received by the same person who places the orders
- Deposits are prepared by the same person who opens the mail and prepares the cash receipt listings
- Customer invoices for non-metered water usage are reviewed by the person who prepares them
- Client master file changes are made by the same person who processes customer billings and are not approved by a supervisor[10]

- In the 2007-08 audit, another item was included in this list: “the Customer Service Representative has access to cash receipts, posts receipts to customer accounts and can write off customer accounts.”[10]

The auditors’ assessment of management’s actions, if any, to improve these areas:

- 2008-09: “During the year no additional procedures were put into place to segregate these duties.”[11]
- 2009-10: “During the year the duties of preparing the deposit and preparing the cash receipts listing were segregated. There were no changes to who performs the other duties listed above.”[12]
- 2010-11: “There were no changes to who performed the duties listed above.”[13]
- 2011-12: “There were no changes to who performed the duties listed above.”[14]

2. <u>Control of Credit Cards</u>

In 2012, after years of admonitions by the auditors regarding credit card controls, PVWMA found itself actually being defrauded through misuse of its credit cards.
In the 2008-09 fiscal year, the auditors stated the following: “During our testing of expenses paid by credit card we noted that credit card statements were not reviewed and approved by management personnel or a member of the Board of Directors. Additionally, we noted one credit card statement that did not have adequate supporting documentation to substantiate the charges. We suggest that additional procedures be put into place so that all credit card statements are approved by a member of management, and that the General Manager’s credit card charges be approved by a member of the Board of Directors.”[11]

The auditors’ follow-up statements regarding this Deficiency in the 2009-10[12] and 2010-11[13] fiscal years were as follows: “During the current year audit we noted no changes to procedures related to approval of credit card statements and noted several instances where credit card charges were not substantiated with proper documentation.”

Finally, the auditors stated in their 2011-12 report: “During the year, management identified fraudulent charges on one of PVWMA’s gasoline credit cards.”[14] The fraudulent charges occurred when the designated staff person failed to follow the established procedure of having the gas charges approved by the Senior Operations Supervisor (SOS) each month. Early in 2012, the SOS noticed that some of the charges were for a diesel vehicle even though none of PVWMA’s company vehicles used diesel fuel. Past records of diesel fuel fill ups dated back to June 2009.[15] Upon further investigation with the gas company, photo records of the license plates of the vehicles being fueled led the authorities to the culprits, one of whom was a PVWMA employee. The charges for the unauthorized gas totaled close to $5,000.

The auditors continued, “We also noted the General Manager’s card was approved only by the General Manager. In addition, we noted instances where the Costco card was only approved by the former Accounts Payable Clerk. Lastly, we noted instances where credit card charges were not substantiated with proper documentation. It is our understanding PVWMA is currently implementing new procedures related to credit cards."[14]

The Agency Act

In light of the auditors' focus on the Agency's debt and whether it was in compliance with the covenants to the bondholders, we examined the Long Term Debt section of each year's audits. We became very concerned that the $41+ million in debt listed in the 2011-12 audit may not be in compliance with the Pajaro Valley Water Management Agency Act (Agency Act) that created the PVWMA in 1984. Section 511 of this Act limits outstanding debt to $300,000 with the financial obligation not to exceed five years.[2]

The Long Term Debt section in the 2011-12 audit itemizes these debts. All of the $41,491,599 total borrowing falls beyond the five-year limit of maturation.[16]

Table 2. Bonds and Notes

Amount	Name	Payment schedule
$19,725,000	Bond payable Certificates of Participation 10/20/99	Principal payments are due in 29 annual installments through 3/1/29 with interest due semi-annually at rates ranging from 3.5 to 5.75%
$11,650,000	Note Payable #1 State Water Resources Control Board (SWRCB) 12/24/99	Note payable in 29 installments of $763,561 with interest of 2.7%. Final payment due 12/17/22
$6,214,989	Note Payable #2 SWRCB 11/21/03	Payable in 29 installments of $414,486 with interest of 2.7% ending 11/21/23
$3,511,446	Note payable Department of Water Resources (DWR) 6/15/05	From 4/1/08 to 2/23/12 note is payable in semi-annual installments of principal and interest in the amount of $111,049 with interest at 2.4%, final payment 9/30/27
$390,164	DWR 2/24/12	Commencing with the payment due on 4/1/12, the note is payable in semiannual installments of principal and interest in the amount of $125,708, with interest at 2.4% with final payment on 9/30/27

Interviews with Directors and Staff

Given that the auditors raised the same issues several years in a row, we were interested in the Agency's process for responding to the findings in the audits. We interviewed Board members and staff to learn what actions the Agency had taken in response to the audit findings.

We first learned that the Agency's Administrative/Finance Committee (Admin/Fin) is the key player in PVWMA's audit activities. This committee consists of three Board members, with the General Manager as an *ex officio* member. When the Agency receives materials from the auditors, the staff delivers them directly to the Admin/Fin members. It is this committee's responsibility to discuss the audit and to make any recommendations to the Board of Directors concerning the audit.

Because of this committee's key role, the Grand Jury requested "correspondence between the staff and the Board of the Agency related either to the topics of the separate letters or to the deficiencies noted in the audit report itself." We received copies of the December 15, 2010, September 19, 2012, and November 14, 2012 Board minutes, but no correspondence. Nearly all of the few references to the audit in both the Admin/Fin and the Board of Directors' minutes were single sentence statements that the committee recommended approval of the audit, or that the Board had approved the audit.

Moreover, in reading the minutes of the Admin/Fin meetings, we found virtually no references to any discussion about the Material Weaknesses and Deficiencies in each audit. The February 11, 2009 minutes and January 19, 2010 minutes read almost identically: "The committee received a presentation of the results of the Agency's external audit from Bartlett, Pringle & Wolf (BP&W) . . . for the fiscal year 2007-2008 and 2008-2009 . . . BP&W also presented their findings and the Agency's management response. There was discussion amongst the committee and a member of the public regarding internal controls. BP&W stated that new rules require audit firms to apply more rigor in their engagements. The committee voted unanimously to accept the FY 2007-2008 and 2008-2009 audit documents. The audited financial statements will be presented to the Board of Directors at . . . [its next] meeting."

We interviewed two staff members who were present at these meetings but neither could recall details of the discussions. We asked if these discussions of internal controls were a regular part of each year's audit and both responded that they "thought they were." On the other hand, two of the Board members we interviewed were unaware of the Separate Letters and reported little discussion of Material Weaknesses or Deficiencies taking place in either the Admin/Fin or in the Board of Directors' meetings. One staff member said they assumed whatever discussion was had in the Admin/Fin somehow made its way to the Board since the Committee is comprised of three Board members. Then we asked another staff member if the entire Board receives copies of both the letters itemizing Material Weaknesses and Findings, and the Separate Letters discussing the Deficiencies. The response was that they were unsure how the Board receives the letters since there had been three to four different people distributing audit material to the Board since 2008. This interviewee stated that "the Board should have received the letters." It appears that there has been little, if any, information regarding these audit details reaching the full Board.

Still unclear as to what the Board's process was for reviewing the results of an audit, we asked Board members directly why these deficiencies had persisted for five years without correction. We received a variety of responses. Each Director brought a different viewpoint regarding audits to the Board. Some comments:

- (regarding the deficiencies) " . . . same old bunch of statements . . . such minute findings, just searching for something wrong"
- (regarding the audit) "It's pretty snoozy stuff. The auditor's terminology is confusing."

A commonly-stated viewpoint was that the Board members knew about these deficiencies but were resigned to the fact that nothing could be done to correct these issues without additional staffing. In 2008, the administrative side of the PVWMA had been cut from seven to three people, not including the ASM position which has been staffed for only 21 months during the last five years. The Board members with this viewpoint had been operating in a crisis mode dealing with vast amounts of litigation over the years. One stated, "We were being litigated off the planet." They felt that such auditor recommendations as a second person to review bank statements or segregation of duties was beyond the ability or time constraints of the three people remaining on the administrative staff.

We asked one interviewee to explain the 1999 Debt Covenants that the auditors recommended be reviewed semi-annually. The response was that the Agency had agreed to "collect rates which will be at least sufficient to equal 125% of the debt service payable in the fiscal year." They also stated that the review was done "sort of semi-annually" and that, in some years, the 125% bond covenant probably was not met because some of the revenues were used to pay augmentation fee refunds. When we asked if a temporary person could have performed this analysis, one Director stated that staff would not consider this a priority until "the Board decides it's a major problem." This statement indicated that the staff would not correct these problems without instruction from the Board of Directors.

At the other end of the spectrum, another Director was appalled to learn from the Grand Jury that these auditor-identified deficiencies had been happening repeatedly over the last five years. This Board member believed that these deficiencies should have been more thoroughly addressed in the Admin/Fin and the discussion passed on to the Board in their annual audit review. Two of the Board members we interviewed stated they had never been informed about the Separate Letters. One Director stated that any such abbreviated discussions in the Admin/Fin ended with the GM promising to take care of everything.

When we asked who writes the Management Responses to the auditors' Findings about Material Weaknesses, we were given a variety of responses. One interviewee stated that the GM wrote the responses while another told us that the Financial Analyst and a part-time contract person had written some of the responses. When we asked staff members if the Board sees the responses before they are sent to the auditors, the reply was "No, I don't think so."

Given that the Board did not seem to have a policy or procedure in place for responding to its annual audit, we decided to see if that applied to other areas. One area of policy in which we sought clarity was the discrepancy between the Agency's reported long-term debt and the borrowing limits set for PVWMA in Section 511 of the Agency Act, which reads:

> *The Agency may, by resolution adopted by the board, issue negotiable Promissory notes to acquire funds for any agency purpose or purposes. Any issue of promissory notes shall bear interest at a rate not exceeding 10 percent per year and shall mature over a period not exceeding five years from the date thereof. The aggregate principal amount of such notes outstanding at any one time shall not exceed three hundred thousand dollars ($300,000).*[2]

When we asked Board members how the $41 million in notes and bonds in the Long Term Debt section of the audit were authorized, one Board member said "To me 'promissory note' is just a phrase. I don't believe it applies. It's not like notes that are long-term." Other members of the Board and staff stated that the Agency's legal counsel advised them that these loans were in compliance with the Agency Act. According to the agency, compliance is based on Section 510 which reads in part:

> *The agency may do any of the following:*
> *(a) Enter into contracts and employ and retain personal services. The board may cause construction or other work to be performed or carried out by contracts or by the agency under its own supervision.*[2]

Some Directors said that there had been discussion at the Board level regarding changes to the Agency Act to eliminate such conflicting portions of the Act, such as section 510 conflicting with 511 in regard to long-term debt. The legal counsel for PVWMA also advised that some portions of the Agency Act conflict with Proposition 218, the Right to Vote on Taxes Act (Prop 218) requirements and need to be corrected to be in compliance with that legislation. In order to change the Agency Act, the changes would need to be submitted to the local voters for a majority vote. However, one interviewee said, "The Act needs updating but farmers in the valley don't trust the Agency and would not vote for any changes."

We also asked both Board and staff members about the relationship between the Board and staff and who has the final say in fiscal matters. Most responded that the Board sets policy and the staff handles day-to-day operations. In one case, however, we found that in the absence of a regularly-enforced policy, the staff had established its own practices. At the October 24, 2012 Board of Directors meeting, the Board was asked to approve a resolution that read, in part, "To increase the GM's contracting authority from $10,000 to $25,000, *consistent with the long established and accepted practice at the Agency."* [emphasis added] From the wording of the discussion, it appeared that the GM and legal counsel had been under the impression that the GM's limit had been $25,000 ever since the establishment of the first Purchasing and Check Signing Policy in 2003.[17]

From this same meeting came these notes: "A review of the Purchasing and Check Signing Policy by the General Manager and Counsel revealed that, in fact, the General Manager's authority to enter into a contract to purchase services or labor is limited to $10,000, not $25,000." Despite the 2003 policy, the Board had regularly authorized payments on these contracts via the approval of checks presented to the Board at their meetings. This proposed amendment triggered a heated response from one of the Directors in a memo to other Board members. "I . . . have never been informed, nor in any way made aware, that it has been **policy** for any General Manager to brazenly ignore any policy established by a resolution of the Board; in this case Resolution 2003-09."[17] [18] The Grand Jury shares that director's concern that, rather than confront the GM for these actions, the Board merely increased the approval level to match the *de facto* one. That is, when the Board found that staff was not following its own rules, the Board simply changed the rules.

The Director followed his memo with a request that the GM provide the Board with a list of "all contracts not submitted to the Board for approval." Upon reviewing the list, he noticed that there was no contract listed for a regularly employed consultant to whom the agency had made payments in the past year of nearly $25,000. (These payments were listed on the check register given to the Board for approval at its regular meetings.) This Director observed, "I have no way of knowing, or finding out, how many other contracts, entered into by the GM, have been omitted, or whether serial contracts were executed to avoid the $25,000 *established practice* limitation."[18] As a result, he requested that the Board "employ a qualified CPA to conduct a full forensic examination of the agency financial records and procedures, and submit a report to the Board including recommendations for changes that would allow the Board to exert the financial oversight required for it to maintain its required fiduciary responsibility."[18]

Had the Board of Directors seen the January 6, 2011 contract letter for the consultant mentioned above, they would have noted that it states that "Payment to consultant for services rendered under this Letter Agreement shall not exceed *ten thousand dollars ($20,000)* [sic][emphasis added]." A second Letter Agreement of October 18, 2011 for this same consultant states "This letter revises Paragraph 3 in the 1/6/11 agreement . . . to increase the maximum payment from *$20,000 to $25,000* [emphasis added]." Since the agreement with this consultant occurred before the October 24, 2012 Board meeting that raised the approval limit, any of these authorizations beyond $10,000 required Board approval. In addition, while the staff was preparing a Contract Commitments spreadsheet in April 2012 for the Admin/Fin meeting, the GM directed staff to remove this consultant's contract and fee information before the spreadsheet was presented.

These interviews gave us a picture of a Board that was disengaged or uninformed. We came away with the impression that the staff is selective in the information shared with the Board as evidenced by the lack of information discussed regarding the audits' Material Weaknesses and Deficiencies. Without Board oversight, the staff has adopted its own procedures, examples of which are the contract approval level and credit card issues noted above. One interviewee stated: "The GM receives no hard questions from the Board and what she asks for is routinely approved."

Board Meeting Observations

With our focus on the auditors' recommendations for internal control improvements concerning the Material Weaknesses and Deficiencies, we attended the November 14, 2012 Board meeting to observe the process by which the Board reviews and approves the annual audits. Two Board members stated that they had received the thick agenda packet only hours before the meeting and that this was a continuing problem. During the meeting, there was no discussion from the Board or public regarding the audit.

The majority of that meeting concerned the presentation of the draft of the new Basin Management Plan by Carollo Engineers. Although the consultant presenting the draft was careful to say that he was not asking for a decision to be made that evening, one Board member called for a vote to accept the draft and directed the staff to proceed with stakeholder meetings. Since this presentation was agendized as "Receive update on the Draft Basin Management Plan" rather than "Consider approval of Draft etc.", one Director objected to such action outside of the Agency's regular process wherein only "Consider Approval" items are eligible to be voted upon. Nevertheless, the agency counsel and another Director pressed forward with the vote.

Findings

F1. The Board of Directors has not been acting on the Material Weaknesses or Control Deficiencies listed in each audit for the last five years.

F2. The PVWMA minutes and agenda materials fail to document whether the Administrative/Finance Committee has been forwarding or initiating any discussion regarding the Material Weaknesses or Control Deficiencies in their audit recommendations to the Board in the last five years.

F3. The Agency's 2011-12 audit shows the PVWMA Long Term Debt to be over $41 million, which does not appear to comply with Section 511 of their Agency Act limiting outstanding debt to $300,000.

F4. The Grand Jury's investigation revealed numerous instances of Agency failure to properly define and carry out roles of staff and Board of Directors.

Recommendations

R1. The Board of Directors should direct the staff to correct Material Weaknesses and Deficiencies before the following year's audit and provide a review of the corrections to the Board.

R2. The Board should direct the Administrative/Finance Committee to include discussion of auditor-reported Material Weaknesses or Deficiencies of any type in its annual recommendations to the Board.

R3. The Board should address the apparent conflict between the Agency's current debt and the limits set in the Agency Act.

R4. The Board should employ a qualified CPA to conduct a full forensic examination of the Agency financial records and procedures, and submit a report to the Board recommending changes guiding the Board to exert the financial oversight for its required fiduciary responsibility.

Commendations

C1. During our investigation a new ASM was hired in October 2012. Our main question in this investigation had been, why are these audit deficiencies that undermine the control of this critical agency so frequently unaddressed? The most common response was "we're short-staffed." Our recent interviews have revealed to us that the new ASM is working on the following:

Table 3. Progress on Addressing Weaknesses

Issues in this Grand Jury investigation	**Current status**
Material Weaknesses	
Reviewing Journal Entries	in progress
Reviewing Bank Statements and Reconciliations	in progress
1999 Bond Covenant part of quarterly budget	completed
Recording of Grant Revenue	in progress
Deficiencies	
Government wide accounting practices	in progress
Reviewing Credit Card receipts	in progress

C2. One Director is calling for re-review of the auditors' Findings and Deficiencies from past audits. We commend these efforts and look forward to the audit results for fiscal year 2012-13.

Responses Required

Respondent	Findings	Recommendations	Respond Within/ Respond By
Board of Directors, Pajaro Valley Water Management Agency	F1- F4	R1- R4	90 days October 1, 2013

Definitions

- **Admin/Fin:** The Administrative/Finance Committee of the Pajaro Valley Water Management Agency.
- **Agency Act:** State legislation that created the PVWMA and directs its policies and procedures.
- **ASM:** Administrative Services Manager.
- **BP&W:** The Agency's external auditors Bartlett, Pringle and Wolf.
- **Control Deficiency:** A Control Deficiency exists when the design or operation of a control does not allow management or employees, in the course of performing their assigned functions, to prevent or detect misstatements on a timely basis.
- **GM:** General Manager.
- **Material Weakness:** A significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.
- **Proposition 218:** *Right to Vote on Taxes Act* - This Act added Articles XIIIC and XIIID to the California Constitution. It states in part: "*Except for fees or charges for sewer, water, and refuse collection services, no property related fee or charge shall be imposed or increased unless and until that fee or charge is submitted and approved by a majority vote of the property owners of the property subject to the fee or charge or, at the option of the agency, by a two-thirds vote of the electorate residing in the affected area.*"[19]
- **PVWMA:** *Pajaro Valley Water Management Agency* - A state chartered water management district formed to efficiently and economically manage existing and supplemental water supplies in order to prevent further increase in, and to accomplish continuing reduction of, long term overdraft.
- **Separate Letters:** Auditors' letter to management discussing recommendations for improvement of Control Deficiencies.
- **SOS:** Senior Operations Supervisor.
- **1999 Certificate of Participation Debt Covenants** - The 1999 Certificate of Participation is a bond, or debt instrument, that was issued in 1999 by PVWMA in order to raise money for the Agency. Within the bond are covenants

(agreements) specifying how the money is raised, spent, and repaid to the bond buyers. One of the covenants in this bond states that PVWMA will collect charges related to water service that will be at least sufficient to yield net revenue equal to 125% of the debt service (interest charges) on the bond payable each year.

Sources

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9. Bartlett, Pringle & Wolf. 2011. "2010-2011 PVWMA Annual Audit." Separate Letter to Management. Dated September 18, 2012. Pages 33 & 34. [Excerpt from Separate Letter to Management - *"During the audit, we noted that the Administrative Services Manger is reviewing the bank statements and bank reconciliations each month, . . . is reviewing debt covenants, . . . is reviewing all journal entries, . . .is reviewing the bank statements and bank reconciliations each month."*]

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[Excerpt from Section B: Professional Services - *"This Purchasing and Check Signing Policy grants authority to PVWMA's General Manager to purchase or enter into contract to purchase services or labor under the following guidelines: Professional Services*
(1) If the amount is $10,000 or less, and is either budgeted or there are emergency circumstances, but only after appropriate price comparisons have been obtained; or
(2) If the amount is greater than $10,000, or is unbudgeted, then only with the prior approval of PVWMA's Board of Directors."]

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Appendix A: Summary of Auditors' Findings of Material Weaknesses

The following tables present the auditor's Findings and management's Responses as written in the original audits.

Table A-1. Material Weakness: Review of Bank Statements and Reconciliations

Year of Audit	Auditor’s Findings	Management Response
2007-08	Finding 08-6 “The Bank Statements and Bank Reconciliations are not reviewed by someone other than the person who prepares them. We suggest that someone independent of the cash disbursement or bank reconciliation function receive the bank statements unopened and review the cancelled checks. Additionally, we suggest that someone other than the person who prepares the bank reconciliations review and approve the reconciliation.”	“The General Manager will receive and periodically review the bank statements. The General Manager will review and approve the bank reconciliations on a monthly basis.”
2008-09	Finding 09-3 “The bank reconciliations are not reviewed by someone other than the person who prepares them. We suggest that someone other than the person who prepares the bank reconciliations review and approve the reconciliations.”	“The General Manager will review and approve the bank reconciliations on a monthly basis.”
2009-10	Finding 10-3 same as 09-3	“When hired, the Administrative Services Manager will review and approve bank reconciliations.”
2009-10	Finding 10-5 “Bank statements are not reviewed by someone other than person who prepares the bank reconciliation. We suggest someone other than the person who prepares the bank reconciliations receive the unopened bank statements and review them for propriety of transactions.”	“When hired, the Administrative Services Manager will receive the unopened bank statements and review them for propriety.”

Year of Audit	Auditor’s Findings	Management Response
2011-12	Finding 12-3 same as 08-6	“Commencing with the 2012-2013 fiscal year, the Administrative Services Manager will review and approved all bank statements and reconciliations.”

Table A-2. Material Weakness: Recording of Grant Revenue

Year of Audit	Auditor’s Findings	Management Response
2007-08	Finding 08-4 “Grant revenue should only be recorded in governmental funds when the resources are available. During the audit an audit adjustment was made to record deferred revenue for grant income that was not available. Additional controls should be put into place to ensure that grant revenue is properly recorded.”	“Additional controls will be put in place to review grant status at year-end so that grant revenue, grants receivable and deferred revenue are properly recorded in the financial statements.”
2009-10	Finding 10-4 “Grant revenue should be recorded in the governmental funds when the resources are available and when earned in the government-wide financial statements. During the audit, an audit adjustment was made to record grants receivable for amounts received shortly after year end. Additional controls should be put in place to ensure that grant revenue is properly recorded.“	“When hired, the Administrative Services Manager will have the necessary high level accounting skills to review grant transaction and determine if they are in accordance with generally accepted accounting principles.”
2010-11	Finding 11-1 same as 10-4	“The Administrative Services Manager will review grant transactions and ensure all submittals are recorded.”

Year of Audit	Auditor's Findings	Management Response
2011-12	Finding 12-1 same as 10-4	"Commencing with the 2012-2012 fiscal year, the Administrative Services Manager will review all grant transactions and ensure all submittals are recorded."

Table A-3. Material Weakness: Journal Entry Approval

Year of Audit	Auditor's Findings	Management Response
2007-08	Finding 08-5 "Journal entries are not reviewed for accuracy and propriety by someone other than the preparer. To prevent possible misstatement, all entries should be reviewed and approved to ensure accurate recording and reporting of financial information."	"Additional controls will be put in place to ensure that someone other than the preparer will review all journal entries. In addition, the General Manager will review journal entries that are not reoccurring in nature."
2008-09	Finding 09-2 same as 08-5	same as 2007-08
2009-10	Finding 10-2 same as 08-5	"When hired, the Administrative Services Manager will review and approve journal entries."
2011-12	Finding 12-2 same as 08-5	"Commencing with the 2012-2013 fiscal year, the Administrative Services Manager will review and approved all journal entries."

Table A-4. Material Weakness: 1999 Certificates of Participation Covenants

Year of Audit	Auditor's Findings	Management Response
2007-08	Finding 08-3 "We noted that for the 1999 Certificates of Participation, the Agency is required, per bond rate covenants, to collect rates and charges for water service which will be at least sufficient to yield, each fiscal year, net revenues, as defined by the bond covenants, equal to 125% of debt service payable on the bonds for the fiscal year. During our testing, we noted that the Agency was in violation of this covenant for the year ending June 30, 2008. We recommend that the Agency put procedures in place to monitor compliance with debt covenants, communicate with the bond trustee any potential rate covenant violations and obtain waivers, if necessary."	"The Financial Analyst will review the debt covenants on a semi-annual basis to ensure that the Agency is in compliance."
2008-09	Finding 09-1 "During the audit we noted that procedures are not in place to monitor compliance with the 1999 Certificates of Participation Debt Covenants. We recommend that the Agency put procedures in place to monitor compliance with debt covenants, communicate with the bond trustee any potential rate covenant violations and obtain waivers, if necessary."	same as 2007-08
2009-10	Finding 10-1 same as 09-1	"The Agency is presently searching for an Administrative Services Manager who will review the debt covenants on a semi-annual basis to ensure that the Agency is in compliance."

Year of Audit	Auditor's Findings	Management Response
2011-12	No finding, but in the Separate Letter added: "We recommend the Agency calculate the debt covenants at least quarterly and incorporate the debt covenants as a part of the budgeting process. We also recommend the debt covenant calculation is presented to the Board of Directors."	