STATE OF CALIFORNIA GAVIN NEWSOM, *Governor*

PUBLIC UTILITIES COMMISSION

505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

Transmitted via e-mail

January 11, 2021

Mr. Kirk Knudsen, President
Sierra Park Water Company, Inc.
P. O. Box 424
Miwuk Village, CA 95346

Dear Mr. Knudsen:

Final Report Transmittal Letter—Review of Sierra Park Water Company, Inc.'s 2019 Annual Report for the period of January 1, 2019 through December 31, 2019

The Utility Audits Branch (UAB) of the California Public Utilities Commission (CPUC) has completed its review of Sierra Park Water Company, Inc.'s (SPWC) regulatory basis financial statements in the 2019 Annual Report filed with the CPUC, which comprise the balance sheet as of December 31, 2019 and related statements of income and retained earnings. The final review report is enclosed.

SPWC's response to the draft report findings are incorporated into this final report. SPWC agreed with the review findings. We will post the final review report on our website at https://www.cpuc.ca.gov/utilityaudits/.

Please provide a Corrective Action Plan (CAP) addressing the findings and recommendations by February 25, 2021. The CAP should include specific steps and target dates to correct the findings identified. Please submit the CAP to the Utility Audits Branch at UtilityAudits@cpuc.ca.gov, with a copy to Bruce DeBerry, Program Manager of Water Division, at Bruce.DeBerry@cpuc.ca.gov.

We appreciate SPWC's assistance and cooperation during the engagement, and your willingness to implement corrective actions. If you have any questions regarding this report, please contact Raymond Yin, Program and Project Supervisor, at (415) 703-1818.

Sincerely,

Angie Williams

Angie Williams, Director
Utility Audits, Risk and Compliance Division

cc: Lael Potter, Compliance Administrator, SPWC
Rachel Peterson, Executive Director, CPUC
Saul Gomez, Deputy Executive Director, Office of the Commission, CPUC
Lucian Filler, Deputy Executive Director, CPUC
Masha Vorobyova, Assistant Director, UAB
Bruce DeBerry, Program Manager, Water Division
Raymond Yin, Program and Project Supervisor, UAB
Khusbindar Kaur, Senior Management Auditor, UAB
Sharmin Wellington, Public Utilities Regulatory Analyst V, UAB

REVIEW OF FINANCIAL STATEMENTS

Sierra Park Water Company, Inc.

For the Year Ended December 31, 2019

Utility Audits, Risk and Compliance Division
Utility Audits Branch
January 11, 2021

MEMBERS OF THE TEAM

Angie Williams, Director

Masha Vorobyova, Assistant Director

Raymond Yin, CPA
Program and Project Supervisor

Khusbindar Kaur, CPA
Lead

Sharmin Wellington, CPA
Staff

Rimple Bhatti
Staff

A digital copy of this report can be found at:
http://www.cpuc.ca.gov/utilityaudits/

You can contact our office at:
California Public Utilities Commission
Utility Audits, Risk and Compliance Division
400 R Street, Suite 221
Sacramento, CA 95811

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EXECUTIVE SUMMARY

The Utility Audits Branch (UAB) of the California Public Utilities Commission (CPUC) conducted a review of the financial statements of Sierra Park Water Company, Inc. (SPWC) as of December 31, 2019, pursuant to Public Utilities (PU) Code, Sections 314.5, 314.6, 581, 582, and 584 that provides the CPUC the statutory authority to review or audit the books and records of the regulated utilities. We conducted this review in accordance with the standards prescribed under Review Engagements in the Generally Accepted Government Auditing Standards (GAGAS).

SPWC was incorporated in California on March 25, 2013. SPWC is a Class D water utility with 345 flat rate service connections providing service northeast of Sierra Village in Tuolumne County, California. As a regulated water utility, SPWC is required to prepare its financial statements on accrual basis of accounting set forth in the Uniform System of Accounts (USOA) adopted in Decision (D.) 16-11-006 by the CPUC on November 16, 2016, which is a comprehensive basis of accounting other than the generally accepted accounting principles in the United States of America.

The purpose of this review was to obtain limited assurance as a basis for reporting whether we were aware of any material modifications that should be made to the financial statements in order for the statements to be in accordance with the USOA. In conjunction with our review of the financial statements, UAB also reviewed, for regulatory purposes, whether SPWC complied with the following:

a) PU Code Section 818 regarding obtaining CPUC's approval before incurring any long-term debts.
b) Timely filing of the 2019 Annual Report as required by the Water Division Memorandum dated January 7, 2020.

Based on our review, we are not aware of any material modifications that should be made to SPWC's revised financial statements in order for them to be in accordance with the accounting framework established in the USOA. For the review period, UAB did not note any noncompliance with PU Code Section 818; and SPWC filed its 2019 Annual Report timely in compliance with the CPUC directive from the Water Division. UAB identified seven material misstatements in SPWC's Annual Report originally filed with the CPUC's Water Division, as described in the Appendix A–Review Findings and Recommendations. These findings are summarized below:

- Finding 1: SPWC made reporting errors relating to Water Plant in Service (WPIS) in its Annual Report, as follows: Account 101–WPIS was understated by $172,489, Account 108–Accumulated Depreciation of Water Plant was understated by $166,814, Account 403–Depreciation Expense was overstated by $2,214, Account 105–Construction Work in Progress (CWIP) was understated by $11,769, and Account 211– Other Paid-in Capital (OPIC) was understated by $20,636. In addition, SPWC did not report assets transferred to it by its affiliated company. The Depreciation Expense and Accumulated Depreciation reported in SPWC's Annual Report was not supported by its Depreciation Schedule. SPWC also incorrectly reported a construction project in progress as additions to WPIS instead of CWIP.

- Finding 2: SPWC incorrectly reported a balance of $71,308 in Account 211–OPIC to correct a prior year reporting error in Account 141–Accounts Receivable.

- Finding 3: SPWC did not report $51,360 of receivables due from its affiliated company for employee labor cost reimbursements because the SPWC improperly utilized the cash basis of accounting.

- Finding 4: SPWC improperly reported receivables totaling $40,405 due from an affiliated company for lease easement as Accounts Receivable–Customers in Account 141 instead of as Investments in Affiliated Companies in Account 123.

- Finding 5: SPWC incorrectly reported cost of power to operate its water plant totaling $11,064 in Account 610–Purchased Water, instead of Account 615–Power.

- Finding 6: SPWC improperly recorded income tax refunds for prior year overpayment of federal corporate income taxes totaling $10,480 as a credit (reduction) in Account 410–Federal Corporate Income Tax Expense.

- Finding 7: SPWC did not accrue $2,036 of CPUC Users Fee due to the CPUC as of December 31, 2019. SPWC improperly reported the 2018 CPUC Users Fee as Taxes Other than Income Taxes in Account 408 in the 2019 Annual Report. As a result, Regulatory Commission Expense in Account 688 was understated by $2,036, Accounts Payable in Account 231 was understated by $2,036 and Taxes Other than Income Taxes in Account 408 was overstated by $2,712.

On October 21, 2020, SPWC submitted its revised financial statements to the UAB to correct the material misstatements described in Appendix A of this report. UAB is not aware of any further material modifications that should be made to the revised financial statements. UAB provided a draft review report to SPWC for comments on December 23, 2020. SPWC responded via email dated January 4, 2021, agreeing with the review findings and recommendations. SPWC's response is included in Appendix B of this report.

INDEPENDENT ACCOUNTANT'S REVIEW REPORT

Mr. Kirk Knudsen, President
Sierra Park Water Company, Inc.
P. O. Box 424
Miwuk Village, CA 95346

The Utility Audits Branch (UAB) of the California Public Utility Commission (CPUC) has reviewed the financial statements of Sierra Park Water Company, Inc. (SPWC), which comprise the balance sheet as of December 31, 2019, the related income statement and statement of retained earnings for the year then ended. A review includes primarily applying analytical procedures to management's financial data and making inquiries of SPWC's management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements as a whole. Accordingly, UAB does not express such an opinion.

Management's Responsibility for the Financial Statements

SPWC's management is responsible for the preparation and fair presentation of its 2019 financial statements in accordance with the accounting framework established under CPUC's Uniform System of Accounts (USOA) for Water Utilities. SPWC's management is also responsible for the design, implementation, and maintenance of internal controls relevant to the preparation and fair presentation of its 2019 financial statements that are free from material misstatement, whether due to fraud or error. In addition, SPWC's management is responsible for the development of its policies and procedures to ensure full compliance with applicable regulations and CPUC directives.

Accountant's Responsibility

UAB's responsibility is to conduct the review engagement in accordance with the standards applicable to reviews engagements promulgated by the Generally Accepted Government Auditing Standards (GAGAS) issued by the Comptroller General of the United States. Those standards require us to perform procedures to obtain limited assurance as a basis for reporting whether we are aware of any material modifications that should be made to the financial statements for them to be in accordance with the accounting framework of the USOA. For regulatory purposes, UAB also reviewed whether SPWC complied with PU Code Section 818 to obtain its long-term debts, and whether SPWC timely filed its 2019 Annual Report as required by CPUC's Water Division. We believe that our review provides a reasonable basis for our conclusion.

Accountant's Conclusion

Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in accordance with the accounting framework of the USOA. However, UAB identified seven material misstatements in SPWC's Annual Report originally filed with the CPUC's Water Division, as described in the Appendix A– Review Findings and Recommendations. These misstatements have been corrected in the accompanying financial statements.

For the review period, UAB did not note any noncompliance with PU Code Section 818. In addition, SPWC has timely filed its 2019 Annual Report in compliance with the CPUC directive from the Water Division.

Basis of Accounting

For regulatory purposes, the CPUC adopted, through Decision (D.) 16-11-006 on November 16, 2016, the updated USOA, which is a comprehensive basis of accounting other than the generally accepted accounting principles (GAAP) in the United States of America. The CPUC requires all water and sewer utilities to prepare their financial statements in accordance with the accounting framework of the USOA. SPWC's financial statements were prepared based on this regulatory requirement.

We draw attention to Notes to the Financial Statements, in which we described the basis of accounting as well as the accounting differences between GAAP and the USOA. Our conclusion is not modified with respect to this matter.

Views of Responsible Official

UAB provided a draft review report to SPWC for comments on December 23, 2020. SPWC responded via email dated January 4, 2021, agreeing with the review findings and recommendations. SPWC's response is included in Appendix B of this report. The review findings and recommendations presented in this report represent our final determination of this review engagement.

Other Matter - Submission of a Corrective Action Plan

SPWC's management should submit a corrective action plan to the UAB at UtilityAudits@cpuc.ca.gov, with a copy to Bruce DeBerry, Program Manager of Water Division, at Bruce.DeBerry@cpuc.ca.gov by February 25, 2021. The corrective action plan should address how SPWC will implement the recommendations and provide the timing of incorporating UAB's review adjustments to SPWC's books and records. If SPWC is unable to implement UAB's recommendations, the corrective action plan should state the reason(s) for not being able to implement any of the recommendations. SPWC should use the amounts reviewed by the UAB as presented in this report as the basis to file its 2020 Annual Report with the CPUC.

Restricted Use of This Review Report

This review report is intended solely for the information and use by the CPUC and the management of SPWC. It is not intended to be used and should not be used by anyone other than the specified parties. However, this report is a matter of public record and its distribution is not limited.

Angie Williams

Angie Williams, Director
Utility Audits, Risk and Compliance Division

Sierra Park Water Company, Inc.

Balance Sheet (As Reviewed)

As of December 31, 2019

ASSETS	
UTILITY PLANT	
Water Plant in Service	$257,724
Construction Work in Progress	11,769
Accumulated Depreciation of Water Plant	(186,681)
Net Utility Plant	82,812
INVESTMENTS	
Investments in Affiliated Companies	40,405
CURRENT AND ACCRUED ASSETS	
Cash	229,005
Accounts Receivable	22,473
Receivables from Affiliated Companies	51,360
Total Current and Accrued Assets	302,838
Total Assets	$426,055
CAPITALIZATION AND LIABILITIES	
CORPORATE CAPITAL AND SURPLUS	
Common Stock	$3,040
Other Paid-in Capital	20,636
Retained Earnings	396,222
Total Capitalization	419,898
CURRENT AND ACCRUED LIABILITIES	
Accounts Payable	2,036
Customer Deposits	2,164
Taxes Accrued	2,137
Other Current Liabilities	(180)
Total Current and Accrued Liabilities	6,157
Total Equity and Liabilities	$426,055

(See independent accountant's review report and accompanying notes.)

Sierra Park Water Company, Inc.

Income Statement (As Reviewed)

For Year Ended December 31, 2019

OPERATING REVENUES	
Unmetered Water Revenue	$189,166
Less: Refunds required by CPUC Decision 16-08-006	(25,938)
Other Water Revenue	4,813
Total Operating Revenue	168,041
OPERATING EXPENSES	
Plant Operation and Maintenance Expenses	
Power	11,064
Employee Labor	12,177
Materials	1,984
Contract Work	22,250
Transportation Expenses	2,368
Other Plant Maintenance Expenses	25,513
Total Plant Operation and Maintenance Expenses	75,356
Administrative and General Expenses	
Employee Pensions and Benefits	866
Office Services and Rentals	80
Office Supplies and Expenses	5,105
Professional Services	28,469
Insurance	25,887
Regulatory Commission Expense	3,053
General Expenses	1,002
Net Administrative and General Expenses	64,462
Total Operating Expenses	139,818
Depreciation Expense	3,009
Taxes Other Than Income Taxes	4,168
State Corporate Income Tax Expense	800
Total Operating Revenue Deductions	147,795
Net Income	$20,246

(See independent accountant's review report and accompanying notes.)

Sierra Park Water Company, Inc.
Statement of Retained Earnings (As Reviewed)
For Year Ended December 31, 2019

Retained Earnings, Beginning of Year	$242,722
CREDITS:	
Net Income	20,246
UAB Adjustment to Other Paid-in Capital	71,308
UAB Adjustment to Federal Corporate Income Tax Expense	10,480
UAB Adjustment to Receivables from Affiliated Companies	51,360
SPWC Adjustments to Accounts Receivable	20,016
Total Credits	173,410
DEBITS:	
UAB Adjustment to Water Plant in Service	(1,340)
UAB Adjustment to Accumulated Depreciation	(4,066)
UAB Adjustment to Employee Labor	(3,038)
UAB Adjustment to Employee Pension and Benefits	(4,151)
UAB Adjustment to Taxes Other than Income Taxes	(7,315)
Total Debits	(19,910)
Retained Earnings, End of Year	$396,222

(See independent accountant's review report and accompanying notes.)

Sierra Park Water Company, Inc.

Notes to Financial Statements

Regulated water utilities are required to prepare their financial statements on accrual basis of accounting set forth in the Uniform System of Accounts (USOA) for Water Utilities adopted in Decision (D.) 16-11-006 by the CPUC on November 16, 2016, which is a comprehensive basis of accounting other than the generally accepted accounting principles (GAAP) in the United States of America. The following describes certain differences in accounting treatments between GAAP and USOA, the company's current accounting practices, and its compliance with applicable regulation and CPUC directives.

1. Purpose of Financial Information and Targeted Audience

The objective of preparing financial statements in accordance with GAAP is to provide information that is useful in making decisions about providing resources to the entity. Users of the financial information include existing and potential investors, lenders, and other creditors.

The purpose of using USOA to prepare financial statements is to have the utilities provide financial transparency of their water operations on a consistent basis. The primary user of the financial information is the CPUC for ratemaking and other compliance purposes.

2. Property, Plant and Equipment

The USOA distinguishes the plant assets for water operations (i.e., Account 101, Water Plant in Service) from those for non-water operations (i.e., Account 121, Non-Water Utility Property and Other Assets), for ratemaking purposes.

(1) Depreciation Methodology
GAAP allows entities to elect a depreciation methodology of their choices, such as straight-line, double-declining balance, or sum-of-the-years digits depreciation method.

USOA requires utilities to use "Straight-line remaining life method." "Remaining life" implies that estimates of future life and salvage value will be re-evaluated periodically and that depreciation rates will be adjusted to reflect any changes in estimates. Water utilities are required to comply with the CPUC's Standard Practice (SP) U-4-SM and SP U-4-M when determining depreciation accruals. Specifically, for the water plant with over $100,000, the utility must maintain separate depreciation reserve by different plant accounts in accordance with Appendix B1 of SP U-4-SM; for the water plant under $100,000, if the utility elects not to separate or maintain the depreciation reserve by accounts, it is appropriate to develop a composite value for remaining life for the entire plant in accordance with Appendix B2 or B3 of SP U-4-SM. The USOA suggested that all utilities maintain a separate accumulated depreciation subaccount for each depreciable plant account; and it is mandatory for water utilities having more than 500 customers.[1] The utility must obtain prior written approval from the CPUC for any practice deviates from the aforementioned SPs.

SPWC computes depreciation using the straight-line remaining life method.

[1] D.16.11-006 dated November 10, 2016, General Accounting Instructions 4 on Page B14.

(2) Asset Retirement
USOA requires that water plant be recorded at the original cost. In USOA's depreciation schedule, the difference between the estimated cost of removal and the salvage value is included in the depreciable base to obtain the annual depreciation expense. When retiring an asset, the cost of removal will reduce the balance of Account 108, Accumulated Depreciation of Water Plant, while the cash received from the salvage value or sale price will increase the balance of Account 108, Accumulated Depreciation of Water Plant. The gain or loss from the asset retirement that is recognized under GAAP is accumulated in Account 108, Accumulated Depreciation of Water Plant under USOA.

SPWC did not retire any assets during 2019.

(3) Sale and Acquisition of Properties
Under GAAP, entities recognize gain or loss from disposal of properties and recognize goodwill or gain from a bargain purchase of other entities' segment or properties.

Under USOA, no goodwill or gain is recognized from the sale or acquisition of a water system or unit, unless it is approved by the CPUC's decision. When the utility sells or purchases the water system or unit, the utility shall first record the transaction into a temperate Account 104, Water Plant Purchased or Sold. Within six months from the date of sale or date of acquisition, the utility shall file with the CPUC for approval of the proposed journal entries to clear this account. The difference between the net original cost of the assets acquired and the cost to the acquiring utility shall be charged or credited to Account 114, Water Plant Acquisition Adjustments.

SPWC did not sell or acquire any properties in 2019. However, SPWC did report want plant transferred to it by its affiliated company totaling $185,598 in its 2019 Annual Report. As a result, Account 101–Water Plant in Service was understated by $185,598, Account 108–Accumulated Depreciation was understated by $164,962, and Other Paid-in Capital–Account 211 is understated by $20,636.

3. Inventory

GAAP allows entities to use different methodologies, such as average cost, first-in-first-out, and last-in-first-out, for the valuation of inventory, which includes cost components of raw materials, work-in-process, and finished goods, etc.

Under USOA, the inventory includes meters, materials and supplies. If identifiable, the inventory should be recorded at original cost, which includes transportation charges, sales and use taxes and other directly assignable costs. Items of small value whose original cost cannot be readily determined shall be recorded at current prices. Scrap materials shall be carried in inventory at estimated scrap value.

SPWC did not report any inventory in its 2019 Annual Report.

4. Cash for Restricted Use

Under GAAP, if the restricted funds are considered to offset the current liability, the funds may be included as current asset classification. If the funds are set aside for use in the near future for the liquidation of long-term debts, payments to sinking funds, then the funds should be classified to non-current assets. If unsure of the timing of the use, the restricted cash can be classified to Other Assets.

Under USOA, the restricted funds are recorded to Account 132, Cash–Special Deposits, which should include cash amounts set aside from general corporate funds, deposited in a separate account with fiscal agents or others, and designated for a special use. A separate subaccount shall be maintained for each designated special use. Interest earned from this account shall be credited to Account 421, Non-Utility Income.

SPWC did not report a restricted cash balance in its 2019 Annual Report.

5. Water Utility Users Fee

PU Code, Sections 401 through 410 authorized the CPUC to set a fee annually to water utilities to cover the costs incurred by the CPUC in regulating them. USOA requires water utilities to credit regular operating revenue accounts with amounts of User Fees billed to customers and charge Account 688, Regulatory Commission Expense, with fees paid to the CPUC. [2]

SPWC did not accrue $2,036 of CPUC Users Fee due to the CPUC as of December 31, 2019. SPWC improperly used the cash basis of accounting to report CPUC Users Fee. As a result, Account 688–Regulatory Commission Expense was understated by $2,036.

6. Affiliate Transactions

Affiliate companies are all entities, including any holding companies, that are under direct or indirect common ownership or control with a water utility regulated by the CPUC. Water utilities are required to comply with the rules specified in D.10-10-019 and SP U-21-W for all the transactions with its affiliates.

Rule 12 of SP U-21-W states, in part, that, "Water Utility shall file with the Commission each year a report which includes a summary of all transactions between Water Utility and its affiliated companies for the previous calendar year…."

SPWC's employees routinely perform services for SPWC's affiliated company – Sierra Park Services, Inc. (SPS). SPS fully compensates SPWC for all employee expenses, including wages, benefits, and applicable taxes. However, SPWC did not accrue $51,360 of receivables due from SPS for employee labor cost reimbursements because the SPWC improperly utilized the cash basis of accounting.

Pursuant to D. 16-01-047, SPS is making lease easement payments to SPWC. As of December 31, 2019, SPWC has a long-term receivable from SPS totaling $40,405. In the 2019 Annual Report, SPWC incorrectly reported the long-term receivables from SPS in Account 141–Accounts Receivable-Customers, instead of Account 123–Investment in Affiliated Companies.

[2] D.16.11-006 dated November 10, 2016, General Accounting Instructions 9 on Pages B18 and B19.

7. Form of Financial Statements [3]

(1) Balance Sheet
Unlike the financial statements of other industries, the financial statements of regulated water utilities present the water plant as the first major caption on the asset side of the balance sheet, and capitalization is first on the liability side. Current assets and current liabilities are relegated to a comparatively unimportant position in the center of the balance sheet, rather than being placed prominently as in statements for non-regulated industries.

(2) Income Statement
The form of the Income Statement reflects the classification of revenues and expenses in ratemaking. Operating revenues and expenses are referred to as "above the line" because they are allowable in ratemaking, and the result of deducting total operating expenses from total operating revenues is the operating income. Other Income and Deductions are referred to as "below the line" because they are applied after operating income and are not allowable in ratemaking. The "below the line" items include interest revenue, dividend income, other revenues that are from non-water utility operations and/or non-water utility properties, expenses that are unrelated to water utility operations, and interest expense (the interest expense is recovered through the authorized rate of return). The concept of "above the line" revenues and expenses being allowable in ratemaking affect the form of the income statement, the classification of revenues and expenses, and decisions of management in incurring expenses.

8. Exclusion of Statement of Cash Flows

Financial Accounting Standards Board specifies in its Statement of Financial Accounting Standards No. 95 that a Statement of Cash Flows is part of a complete set of financial statements under GAAP. However, Codification of Statements on Auditing Standards AU-C Section 800.A35 states, in part, that, "Special purpose financial statements may not include a statement of cash flows…." Since the USOA is an accounting framework other than GAAP for regulatory purposes, the Statement of Cash Flows is not required and therefore excluded from this review report.

9. Compliance filing of 2019 Annual Report with the CPUC

PU Code, Sections 581, 582, and 584, and the CPUC's directive (i.e., Water Division's annual memorandum to water and sewer utilities) require all regulated water and sewer IOUs to file an Annual Report with the CPUC every year. For the year being reviewed, SPWC has complied with these requirements.

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[3] Regulated Utilities Manual—A Service for Regulated Utilities by Deloitte & Touché USA LLP, pages 36-37.

APPENDIX A—REVIEW FINDINGS AND RECOMMENDATIONS

Finding 1: Improper Reporting of Water Plant in Service

Condition:
SPWC made reporting errors relating to Water Plant in Service (WPIS) in its 2019 Annual Report originally filed with the CPUC's Water Division on May 28, 2020. Our review of supporting documentation revealed that Account 101–WPIS was understated by a net amount of $172,489 (understated by $185,598; and overstated by $1,340 and $11,769), Account 108–Accumulated Depreciation of Water Plant was understated by a net amount of $166,814 (understated by $164,962 and $4,066; and overstated by $2,214), Account 403–Depreciation Expense was overstated by $2,214, Account 105–Construction Work in Progress (CWIP) was understated by $11,769 and Account 211–Other Paid-in Capital (OPIC) was understated by $20,636 as follows:

- SPWC did not correctly report the water plant transferred to SPWC by its affiliated company totaling $185,598. The CPUC Decision 16-01-047 required that SPWC's affiliated company to transfer these assets to the SPWC at no cost. The original cost of the transferred assets was $185,598. At the time of the transfer, these assets had an accumulated depreciation balance of $164,962 and a net value of $20,636. As a result, Account 101–WPIS was understated by $185,598, Account 108–Accumulated Depreciation of Water Plant was understated by $164,962, and Account 211–OPIC was understated by $20,636.

- SPWC overstated depreciation expense by $2,214 in its 2019 Annual Report. The Depreciation Schedule showed that the depreciation expense for 2019 totaled $3,009. However, SPWC reported the Depreciation Expense totaling $5,223 in its Annual Report. As a result, Accumulated Depreciation of Water Plant in Account 108 and Depreciation Expense in Account 403 were overstated by $2,214.

- SPWC understated its Accumulated Depreciation of Water Plant in Account 108 by $4,066, and overstated WPIS in Account 101 by $1,340 due to prior year recording errors.

- SPWC included the construction costs totaling $11,769 relating to the incomplete project to add meters in Account 101–WPIS instead of Account 105–CWIP. As a result, Account 105–CWIP was understated by $11,769, and Account 101–WPIS was overstated by the same amount.

SPWC corrected these misstatements in its revised financial statements submitted to UAB on October 21, 2020.

Criteria:
The USOA states, in part, that:

> **2. General Accounting Instructions**
> B. All books of account, together with records and memoranda supporting the entries therein, shall be kept in such a manner as to support fully the facts pertaining to such entries.

The books and records referred to herein include not only the accounting records in a limited technical sense, but also all other records, reports, correspondence, memoranda and information useful in determining the facts regarding a transaction.

101. Water Plant in Service
A. This account shall include the original cost of all water plant owned and used by the utility in providing water service.

105. Construction Work in Progress - Water Plant
This account shall include the cost of water plant in process of construction, but not yet ready for service.

211. Other Paid-in Capital
A. This account shall include all non-Subchapter S Corporation's paid-in capital not derived from earnings. It shall include such items as premiums and discounts related to the issuance of capital stock, donations to the utility of its capital stock, credits arising from the forgiveness of debt.

Cause:
SPWC lacks procedures to ensure its compliance with the USOA accounting requirements. SPWC lacks adequate controls over its financial reporting process to ensure that all Water Plant in Service and related depreciation, including assets transferred to it by its affiliated company, were properly reported in its Annual Report. SPWC also lacks monitoring procedures to ensure that cost of water plant in process of construction, but not yet ready for service, were reported as Construction Work in Progress in Account 105.

Effect:
Inaccurate reporting of Water Plant in Service, Accumulated Depreciation, Depreciation Expense, and Construction Work in Progress in the Annual Report, which may be used during SPWC's General Rate Case (GRC) application review process, could potentially impact the water rates for SPWC's rate payers. Inaccurate reporting of OPIC distorted SPWC's financial position, which may impact decision-makers.

Recommendations:
SPWC should establish and implement policies and procedures to ensure adherence to the USOA accounting and financial reporting requirements relating to Water Plant in Service. SPWC should also implement procedures to monitor Water Plant in Service construction projects to ensure that cost of water plant in process of construction, but not yet ready for service, are reported as Construction Work in Progress in Account 105.

Finding 2: Improper Correction of Prior Year Accounting Error

Condition:
SPWC incorrectly reported a balance of $71,308 in Account 211–OPIC in its Annual Report originally filed with the CPUC's Water Division on May 28, 2020, to correct a prior year reporting error in Account 141–Accounts Receivable. SPWC understated its Accounts Receivable balance reported in the 2018 Annual Report by $91,324. Schedule A-8 – Retained Earnings in the 2019 Annual Report showed a $20,016 adjustment to retained earnings for prior period accounting adjustment. SPWC did not provide documentation or adequate explanation relating to the $20,016 adjustment to retained earnings. After further review of the SPWC's 2018 and 2019 general ledgers,

trial balances, and Annual Reports, UAB noted that the $20,016 adjustment to the Retained Earnings accounts was related to the accounts receivable reporting error in the 2018 Annual Report. We also noted that the remaining $71,308 to correct the prior year accounts receivable reporting error of $91,324 was incorrectly reported as OPIC in Account 211 instead of the Retained Earnings in Account 215. As a result, Account 211–Other Paid in Capital was overstated by $71,308, and Account 215–Retained Earnings was understated by the same amount. However, SPWC corrected these misstatements in its revised financial statements submitted to UAB on October 21, 2020.

Criteria:
USOA states, in part, that:

> **2. General Accounting Instructions**
> B. All books of account, together with records and memoranda supporting the entries therein, shall be kept in such a manner as to support fully the facts pertaining to such entries. The books and records referred to herein include not only the accounting records in a limited technical sense, but also all other records, reports, correspondence, memoranda and information useful in determining the facts regarding a transaction.
>
> **211. Other Paid-in Capital (for corporations only)**
> A. This account shall include all non-Subchapter S Corporation's paid-in capital not derived from earnings. It shall include such items as premiums and discounts related to the issuance of capital stock, donations to the utility of its capital stock, credits arising from the forgiveness of debt of the utility; credits arising out of a reorganization of the utility, or in connection with its recapitalization.
>
> **215. Retained Earnings (for corporations only)**
> A. This account shall reflect corporate earnings retained in the business.
> B. The account shall be credited with:
> 1. Net income.
> 2. Accounting adjustments not properly attributable to the current period.
>
> C. The account shall be charged with:
> 1. Net losses.
> 2. Accounting adjustments not properly attributable to the current period.
> 3. Dividends.

Cause:
SPWC lacked adequate accounting policies and procedures and a review process to ensure that all account balances were properly reported in the Annual Report. SPWC also lacked adequate internal controls over prior year accounting error corrections to ensure that it performed adequate analysis and maintained appropriate supporting documentation relating to prior year error corrections.

Effect:
Inaccurate reporting of Other Paid-in Capital and Retained Earnings distorts SPWC's financial position as of December 31, 2019. Misclassification of Retained Earnings as Other Paid-in Capital distorted the sources of corporate capital, while overstated Accounts Receivable can improperly inflate the SPWC's working capital.

Recommendations:
The SPWC should strengthen its accounting policies and procedures and develop and implement a review process to ensure that all account balances in the Annual Report are accurately reported in

the Annual Report. SPWC should also develop and implement procedures that require it to perform in-depth analysis of retained earnings and maintain supporting documentation for any adjustments made to retained earnings due to prior year accounting error corrections.

Finding 3: Improper Use of Cash Basis of Account to Report Cost Reimbursements

Condition:
SPWC did not report $51,360 of receivables due from its affiliated company for employee labor cost reimbursements in its Annual Report originally filed with the CPUC's Water Division on May 28, 2020, because SPWC improperly utilized the cash basis of accounting. The USOA requires utilities to use the accrual basis of accounting. In 2019, SPWC's affiliated company reimbursed SPWC $39,568 for shared employee costs incurred in 2018. SPWC did not accrue the $39,568 receivable from the affiliated company in 2018 and incorrectly recorded this amount as a reduction to expenses in Account 630–Employee Labor in 2019 when the reimbursement was received. In addition, SPWC did not accrue $51,360 of receivables due from its affiliated company for employee labor cost reimbursements relating to quarters two, three, and four in 2019. As a result, Receivables from Affiliated Companies were understated by $51,360 and Employee Labor Expense, Employee Pensions and Benefits, and Taxes Other than Income Taxes were overstated by $3,038, $4,151, and $4,603, respectively. However, SPWC corrected these misstatements in the revised financial statements submitted to UAB on October 21, 2020.

Criteria:
The USOA states, in part, that:

> **2. General Accounting Instructions**
> A. The books of account of all water utilities shall be kept by the double entry method, on an accrual basis. Each utility shall post its accounts monthly and shall close its books at the end of each calendar year.
>
> **142. Receivables from Affiliated Companies**
> This account shall include the debit balances subject to current settlement in open accounts with affiliated companies, and notes and drafts which affiliated companies are liable, and which mature and are expected to be paid in full no later than one year from date of issuance, together with interest thereon. Items which do not bear a specified due date but which have been carried for more than 90 days and items which are not paid within 90 dates from due date shall be transferred to Account 123, Investments by Affiliated Companies.

Cause:
SPWC accounting policy to record transactions using the cash basis of accounting does not conform with the USOA requirements. SPWC lacks internal controls over financial reporting to ensure that the Annual Report is prepared using the accrual basis of accounting as required by the USOA.

Effect:
Inaccurate reporting of Employee Labor expenses (Account 630) in the Annual Report, which may be used during SPWC's GRC application review process, could potentially impact the water rates for SPWC. Inaccurate reporting of Receivables from Affiliated Companies (Account 142) improperly distorted SPWC's financial position as of December 31, 2019.

Recommendation:
SPWC should revise its accounting policies and procedures to ensure that SPWC prepares its annual report using accrual basis of accounting as required by the USOA.

Finding 4: Misclassified Long-Term Receivables from Affiliated Company

Condition:
SPWC improperly reported receivables due from an affiliated company for lease easement in Account 141–Accounts Receivable–Customers totaling $40,405 in its Annual Report originally filed with CPUC's Water Division on May 28, 2020. The lease easement is a long-term receivable; and the Memorandum of Understanding between SPWC and its affiliated company shows the final payment for the lease easement is due in June 2022. Therefore, the receivable from the affiliated company for lease easement should have been reported in Account 123–Investments in Affiliated Companies. As a result, Account 141–Accounts Receivable–Customers was overstated by $40,405 and Account 123– Investments in Affiliated Companies was understated by the same amount. However, SPWC corrected these misstatements in its revised financial statements submitted to UAB on October 21, 2020.

Criteria:
USOA states, in part, that:

> **123. Investments in Affiliated Companies**
> Receivables from affiliated companies which do not bear a specific due date but which have been carried as a receivable from affiliated companies for more than 90 days and other receivable items which are not paid within 90 days from due date shall be recorded in this account.
>
> **141. Accounts Receivable - Customers**
> This account shall include amounts due from customers for water service. Note: Accounts receivable other than from customers for water service shall be included in Account 174, Other Current Assets, or in Account 121, Non-Water Utility Property and Other Assets, as appropriate.

Cause:
SPWC lacked adequate controls over its financial reporting process to ensure that receivables from affiliated companies were recorded in accordance with the USOA.

Effect:
Inaccurate reporting of Accounts Receivable and Investments from Affiliated Companies distorted SPWC's financial position and improperly inflated SPWC's working capital as of December 31, 2019.

Recommendations:
SPWC should develop policies and procedures to ensure compliance with the USOA. SPWC should ensure that long-term receivables from affiliated companies are properly reported as Investments in Affiliated Companies.

Finding 5: Misclassified Power Expense

Condition:
SPWC incorrectly reported the cost of power to operate its water plant totaling $11,064 in Account 610–Purchased Water instead of Account 615–Power in its Annual Report originally filed with the CPUC's Water Division on May 28, 2020. The reporting error occurred due to a clerical error. SPWC corrected these misstatements in its revised financial statements submitted to UAB on October 21, 2020.

Criteria:
The USOA states, in part, that:

> **610. Purchased Water**
> This account shall include the cost at the point of delivery of water purchased for resale.
>
> **615. Power**
> This account shall include the cost of power and fuel used to operate pumps.

Cause:
SPWC lacked adequate review process to ensure that the information was accurately reported in the Annual Report.

Effect:
Inaccurate reporting of Purchased Water in Account 610 and Power Expense in Account 615 distorted SPWC's Income Statement. Misclassification of expenses reduces the comparability of financial statements among small water utilities.

Recommendation:
SPWC should implement a review process to ensure that information in the Annual Report is accurately reported.

Finding 6: Improper Use of Cash Basis of Accounting to Report Corporate Income Taxes

Condition:
SPWC improperly recorded income tax refunds totaling $10,480 as a credit (reduction) in Account 410–Federal Corporate Income Tax Expense in its Annual Report originally filed with the CPUC's Water Division on May 28, 2020. SPWC made an overpayment of income taxes in 2017 and reported the overpayment as an expense using the cash basis of accounting. The USOA requires for overpayment to be reported as a prepayment in Account 174–Other Current Assets. As a result, Federal Corporate Income Tax Expense was understated by $10,480 in the 2019 Annual Report. However, SPWC corrected these misstatements in its revised financial statements submitted to UAB on October 21, 2020.

Criteria:
USOA states, in part, that:

> **2. General Accounting Instructions**
> A. The books of account of all water utilities shall be kept by the double entry method, on an accrual basis. Each utility shall post its accounts monthly and shall close its books at the end of each calendar year.

174. Other Current Assets
A. This account shall include prepayment of rents, taxes, insurance and similar expenses for which payment have been made in advance of the period to which they apply. As the periods covered by such prepayments expire, this account shall be credited and the proper operating expense or other accounts shall be charged with the amounts applicable to the current period.

Cause:
SPWC accounting policy to record transactions using the cash basis of accounting does not conform with the USOA requirements. SPWC lacked internal controls over financial reporting to ensure that the Annual Report was prepared using the accrual basis of accounting as required by the USOA.

Effect:
Submitting inaccurate financial information on the Annual Report, which may be used during the Utility's GRC proceeding, could impact the Utility's water rates.

Recommendation:
SPWC should develop and implement accounting policies and procedures that requires it to prepare its annual report using accrual basis of accounting as required by the USOA.

Finding 7: Improper Recording of CPUC Users Fee

Condition:
SPWC understated Regulatory Commission Expense in Account 231 and Accounts Payable in Account 231 by $2,036; and overstated Taxes Other than Income Taxes in Account 408 by $2,712 in its Annual Report originally filed with the CPUC's Water Division on May 28, 2020, due to the following reasons:

- SPWC did not accrue $2,036 of CPUC Users Fee due to the CPUC as of December 31, 2019. SPWC improperly used the cash basis of accounting to report CPUC Users Fee.

- SPWC improperly reported the 2018 CPUC Users Fee as Taxes Other than Income Taxes in Account 408 totaling $2,712 in its 2019 Annual Report.

SPWC corrected these misstatements in its revised financial statements submitted to UAB on October 21, 2020.

In addition, SPWC did not include the CPUC Users Fee in its customer bills as required by PU Code Sections 401 through 415.

Criteria:
USOA states, in part, that:

2. General Accounting Instructions
A. The books of account of all water utilities shall be kept by the double entry method, on an accrual basis. Each utility shall post its accounts monthly and shall close its books at the end of each calendar year.

9. Water Utility Users Fee

Public Utilities Code Sections 401 through 415 provide that the Commission shall annually set a fee to be paid by water utilities to cover the costs incurred by the Commission in regulating them. A percentage of gross revenues is added to customer bills and paid by the water companies to the Commission.

A. Class A water utilities pay a percentage of gross revenues quarterly; Class B, C, and D water utilities pay a designated amount, based on gross revenues, on January 15 of the following year. Sales of water for resale and Interdepartmental water sales should be excluded from gross revenues when computing the Water Utility Users fee.

B. Water utilities will credit regular operating revenue accounts with amounts billed to customers and charge account 688, Regulatory Commission Expense, with fees paid to the Commission.

PU Code Section 404 states, in part, that:

(a) The commission shall authorize each person or corporation subject to Section 421 or 431 to annually adjust its rates or charges for intrastate services so as to collect from its customers and subscribers an amount sufficient to pay the amount of the fee required by Section 421 or 431 together with the costs of collecting the fee from each customer or subscriber.

(b) Each person or corporation subject to Section 421 or 431 may identify separately, on the bill of each customer or subscriber, the amount to be paid by each customer or subscriber for purposes of funding the commission pursuant to this chapter.

Cause:

SPWC's accounting policy to record transactions using the cash basis of accounting does not conform with the USOA requirements. SPWC lacked adequate controls over its financial reporting process to ensure that it complied with the accounting requirements specified in the USOA for recording and reporting of CPUC Users Fee. SPWC stated that it was unaware that it could bill its customers for the Users Fee remitted to the CPUC. SPWC lacked adequate monitoring procedures to ensure compliance with CPUC's directives regarding CPUC Users Fee.

Effect:

Inaccurate reporting of Regulatory Commission Expense and Taxes Other than Income Taxes in the Annual Report, which may be used during SPWC's GRC application process, could potentially impact water rates for SPWC's ratepayers. Inaccurate reporting of Accounts Payable in the Annual Report distorted SPWC's financial position and misstated its working capital.

Recommendations:

SPWC should revise its accounting policies and procedures to ensure that SPWC records and reports its transactions using accrual basis of accounting, as required by the USOA. SPWC should implement policies and procedures to ensure compliance with the USOA by recording the CPUC Users Fee in Account 688–Regulatory Commission Expense. SPWC should also implement monitoring procedures to ensure it complies with applicable laws and regulations, including PU Code 404, which requires the SPWC to include CPUC Users Fee in customer bills.

APPENDIX B—SPWC'S RESPONSE

SPWC submitted the following response via email to the UAB's draft review report on January 4, 2021:

> We are in agreement with the draft review findings pertaining to the 2019 Sierra Park Water Company Annual Report. The majority of the findings are the result of converting to an accrual basis of accounting, fiscal year end change to calendar year, and USOA conversion as stated in the draft report.
>
> We look forward to receiving the final review report.