



Financial Audit of Big Basin Water Company, Inc. Financial Statements

For the Year Ended December 31, 2017

Utility Audit, Finance and Compliance Branch
August 23, 2019



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Thanks to:
Angie Williams, Raymond Yin, Sharmin Wellington, and Xiaowen Zhao

**Audit of Financial Statements of
Big Basin Water Company, Inc.
For the Year Ended December 31, 2017**

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PUBLIC UTILITIES COMMISSION

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Report of Independent Auditors

Jim McPherson, President
Big Basin Water Company, Inc. (BBWC)
PO Box 197,
Boulder Creek, CA 95006

Report on the Financial Statements

The Utility Audit, Finance and Compliance Branch (UAFCB) of the California Public Utilities Commission (Commission) was engaged to audit the accompanying financial statements of Big Basin Water Company, Inc. (BBWC), which are comprised of the balance sheet as of December 31, 2017, and the related statements of income, retained earnings and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

BBWC's management is responsible for the preparation and fair presentation of the financial statements in accordance with the Uniform System of Accounts (USOA) for Class B, C, and D water utilities adopted and prescribed by the Commission, and accounting principles generally accepted in the United States of America, as described in Note 1 in the Notes to the Financial Statements attached herein. Management is also responsible for the design, implementation, and maintenance of internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

The responsibility of the UAFCB is to express an opinion on BBWC's financial statements based on conducting the audit in accordance with auditing standards generally accepted in the United States of America. Because of the matters described in the basis for disclaimer of opinion paragraph, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for Disclaimer of Opinion

Due to the lack of supporting documentation and historical information on the Water Plant in Service, Other Paid-in Capital, Retained Earnings, and Non-utility Property and Other Assets, UAFCB could not attest to these balances as of December 31, 2017. Although requested repeatedly by UAFCB, BBWC was unable to provide sufficient appropriate audit evidence to substantiate certain reported amounts. As a result, we were unable to verify the following: (1) The reported plant assets of \$2,039,904; (2) A material adjustment of \$1,792,868 to Other Paid-in Capital made by BBWC; (3) The fluctuation of BBWC's Retained Earnings from (\$461,132) to \$65,985 within 2016; and, (4) The Non-utility Property and Other Assets balance reported by BBWC as of December 31, 2016, of \$315,220 based on the information provided should have been treated as a capital distribution. In addition, BBWC reported \$391,670 as of

December 31, 2017, which included charges for personal expenses and loan from shareholders. UAFCB was unable to satisfy itself by other auditing procedures concerning these accounts as described in Note 1 to the financial statements. These accounts, when considered individually or in aggregate, are material to the financial statements taken as a whole.

Disclaimer of Opinion

Because of the significance of the matters described in the Basis for Disclaimer of Opinion paragraph, the UAFCB has not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, the UAFCB does not express an opinion on the financial statements of Big Basin Water Company, Inc. as of December 31, 2017.

Basis of Accounting

We draw attention to Note 1 of the financial statements, which describes the basis of accounting. The financial statements are prepared by BBWC on the basis of the accounting requirements of the California Public Utilities Commission as set forth in the Uniform System of Accounts for Class B, C, and D Water Utilities, which is a basis of accounting other than accounting principles generally accepted in the United States of America.

Use of Report

The report is intended solely for the information and use by the Commission and Big Basin Water Company, Inc. It should not be used by anyone other than the specified parties.

Raymond Yin

Raymond Yin, CPA
Program and Project Supervisor
Utility Audit, Finance and Compliance Branch

Balance Sheets

As of December 31, for the		
Year		
	2017	2016 ¹
ASSETS		
UTILITY PLANT		
Water Plant in Service (Note 1)	\$810,936	\$808,281
Water Plant in Service-SDWBA (Note 1)	1,228,968	1,228,968
Accumulated Depreciation of Water Plant (Note 1)	(474,561)	(459,635)
Accumulated Amortization of SDWBA Loan (Note 1)	(1,020,736)	(979,770)
Net Utility Plant	544,607	597,844
 INVESTMENTS		
Non-Utility Property and Other Assets	357,205	315,220
Total Investments	357,205	315,220
 CURRENT AND ACCRUED ASSETS		
Cash	3,034	4,943
Special Deposits	56,675	27,745
Accounts Receivable	0	480
Receivables from Affiliated Companies	1,861	0
Total Current and Accrued Assets	61,570	33,168
Total Assets	963,382	\$946,232
 CAPITALIZATION AND LIABILITIES		
CORPORATE CAPITAL AND SURPLUS		
Common Stock	\$100,000	\$145,302
Other Paid-in Capital	45,302	0
Retained Earnings (Note 1)	108,337	65,985
Total Corporate Capital and Surplus	253,639	211,287
 LONG-TERM DEBT		
Long-term Debt	632,738	653,720
 CURRENT AND ACCRUED LIABILITIES		
Accounts Payable	6,265	0
Other Current Liabilities	70,740	81,225
Total Current and Accrued Liabilities	77,005	81,225
Total Equity and Liabilities	\$963,382	\$946,232

(The accompanying notes and appendices are an integral part of these Financial Statements)

¹ For the year ended December 31, 2016, the amounts were derived from BBWC's 2016 Annual Report and were not audited by UAFCB.

Income Statements

	For the Year of	
	2017	2016¹
OPERATING REVENUES		
Unmetered Water Revenue	\$3,269	\$4,197
Fire Protection Revenue	707	707
Metered Water Revenue	479,972	440,199
Other Water Revenue	6,748	10,859
Total Operating Revenues (Note 1)	490,696	455,962
OPERATING EXPENSES		
Plant Operation and Maintenance Expenses		
Power	19,826	13,125
Employee Labor	66,295	62,207
Materials	4,327	4,650
Contract Work	13,725	9,840
Transportation Expenses	11,342	11,389
Other Plant Maintenance Expenses	7,792	16,110
Total Plant Operation and Maintenance Expenses	123,307	117,321
Administrative and General Expenses		
Office Salaries	7,868	32,900
Management Salaries	117,790	83,244
Employee Pensions and Benefits	1,764	1,698
Uncollectible Accounts Expense	480	0
Office Services and Rentals	1,465	3,911
Office Supplies and Expenses	18,927	13,311
Professional Services	19,234	15,195
Insurance	69,181	61,001
Regulatory Commission Expenses	10,784	0
General Expenses	2,437	2,167
Total Administrative and General Expenses	249,930	213,427
Total Operating Expenses	373,237	330,748
Depreciation Expense (Note 1)	14,926	14,926
SDWBA/SRF Loan Amortization Expense (Note 1)	40,966	40,966
Taxes Other Than Income Taxes	25,651	21,260
State Corporate Income Tax Expense	943	2,168
Total Operating Revenue Deductions	455,723	410,068
Total Utility Operating Income (Loss)	34,973	45,894

(The accompanying notes and the appendices are an integral part of these Financial Statements)

¹ For the year ended December 31, 2016, the amounts were derived from BBWC's 2016 Annual Report and were not audited by UAFCB.

Income Statements (Continues)

	For the Year of	
	2017	2016 ¹
OTHER INCOME AND DEDUCTIONS		
Non-utility Income	\$172,514	\$1,712
Miscellaneous Non-utility Expense	(85,297)	(14,012)
Interest Expense (excluding SDWBA)	(7,021)	(6,914)
Interest Expense (SDWBA)	(27,020)	(27,902)
Total Other Income and Deductions	53,176	(47,116)
 Net Income (Loss)	 \$88,149	 (\$1,222)

(The accompanying notes and the appendices are an integral part of these Financial Statements)

¹ For the year ended December 31, 2016, the amounts were derived from BBWC's 2016 Annual Report and were not audited by UAFCB.

Statements of Retained Earnings

	For the Year of	
	2017 ¹	2016 ²
Retained Earnings, Beginning of Year	\$65,985	(\$461,132)
CREDITS:		
Net Income	88,149	0
Prior period adjustments by BBWC	0	512,826
UAFCB adjustment to correct discrepancy between Schedule A and Schedule A-9 of BBWC's 2016 Annual Report ³	0	15,513
Total Credits	88,149	528,339
DEBITS:		
Net Loss	0	(1,222)
Prior period adjustment by BBWC	(1,312)	0
UAFCB Adjustment to Non-utility and Other Assets	(29,265)	
UAFCB Adjustment to Metered Water Revenue	(12,061)	0
UAFCB Adjustment to Taxes Other Than Income Taxes	(3,158)	0
UAFCB Cumulative Adjustment to Beginning Balance ⁴	(1)	0
Total Debits	(45,797)	(1,222)
Retained Earnings, End of Year	\$108,337	\$65,985

(The accompanying notes and appendices are an integral part of these Financial Statements)

¹ UAFCB did not audit the retained earnings account for years ended December 31, 2017.

² For the year ended December 31, 2016, the amounts were derived from BBWC's 2016 Annual Report and were not audited by UAFCB. BBWC's 2016 Annual Report reflected a negative beginning Retained Earnings of \$461,132; and an ending RE of \$65,985. BBWC did not provide the reason for the changes in RE of \$528,339. The RE balance included 2016 Net Operating Loss of \$1,222.

³ In its 2016 Annual Report, BBWC reported beginning Retained Earning balance of (\$461,132) in Schedule A, but it reported (\$445,619) in Schedule A-9. A discrepancy of \$15,513 was noted and adjusted hereby UAFCB.

⁴ BBWC's 2017 Annual Report included \$1 immaterial variance as reflected in the adjustment.

Statements of Cash Flows

	For the Year of	
	2017	2016¹
CASH FLOW FROM OPERATING ACTIVITIES:		
Net Income (Loss)	\$88,149	(\$1,222)
Adjustments to Reconcile Net Income to Cash		
Provided by Operating Activities		
Depreciation (Note 1)	14,926	14,926
Amortization-SDWBA Loan (Note 1)	40,966	40,966
Decrease (increase) in Special Deposits	(28,930)	(27,745)
Decrease (increase) in Accounts Receivable	480	(480)
Decrease (Increase) in Receivables from Associated Companies	(1,861)	83,893
Increase (Decrease) in Accounts Payable	6,265	0
Increase (Decrease) in Other Current Liabilities	(10,485)	40,372
Net Cash Provided (Used) by Operating Activities	109,510	150,710
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net Plant Additions	(2,655)	0
Decrease (Increase) in Non-Utility Property and Other Assets	(41,985)	(315,220)
Decrease (Increase) in Retained Earnings per BBWC	(1,312)	512,826
UAFCB adjustment to correct discrepancy between Schedule A and Schedule A-9 of BBWC's 2016 Annual Report ²	0	15,513
UAFCB Cumulative Adjustments to Retained Earnings	(44,485)	0
Net Cash Provided (Used) for Investing Activities	(90,437)	213,119
CASH FLOWS FROM FINANCING ACTIVITIES:		
Increase (Decrease) in Common Stock	(45,302)	0
Increase (Decrease) in Other Paid-in Capital	45,302	0
UAFCB Adjustment to Other Paid-in Capital ³	0	(335,229)
Increase (Decrease) in Long-term Debt	(20,982)	(24,099)
Net Cash Provided (Used) for Financing Activities	(20,982)	(359,328)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(1,909)	4,501
CASH AT BEGINNING OF YEAR	4,943	442
CASH AT END OF YEAR	\$3,034	\$4,943

(The accompanying notes and appendices are an integral part of these Financial Statements)

¹ For the year ended December 31, 2016, the amounts were derived from BBWC's 2016 Annual Report and were not audited by UAFCB.

² In its 2016 Annual Report, BBWC reported beginning Retained Earning balance of (\$461,132) in Schedule A, but it reported (\$445,619) in Schedule A-9. A discrepancy of \$15,513 was noted and adjusted hereby UAFCB.

³ BBWC's 2016 Annual Report contained significant and unsupported changes from the 2015, including Non-utility Property and Other Assets increased by \$315,220, Receivables from Associated Company decreased by \$83,893, and Other Paid-in Capital decreased by \$1,792,868. These changes caused the 2015 ending balances not to reconcile to the 2016 beginning balances, which resulted in a variance between Assets and Equity plus Liabilities of \$1,457,639. Thus, Other Paid-in Capital decreased of \$1,792,868 - \$1,457,639 results in the variance of \$335,229 for 2016.

Notes to Financial Statements

(1) Summary of Significant Accounting Policies

Big Basin Water Company, Inc. (BBWC) is a Class C water utility that serves 592 metered and 5 flat rate customers in Santa Cruz County, between Boulder Creek and Big Basin with a water system that has a total storage capacity of approximately 2,483,000 gallons.

The Company has prepared the accompanying financial statements on the basis of accounting set forth in the Uniform System of Accounts (USOA) for Water Utilities adopted and prescribed by the Commission, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. Under that basis of accounting, certain transactions, such as adjustments of certain estimated operating expenses related to prior years have been recorded directly in the statements of retained earnings. Accounting principles generally accepted in the United States of America would require such transactions to be recorded in the statement of income.

As stated in the Basis for Disclaimer of Opinion on our audit report, we were unable to express an opinion on BBWC's reported financial statements because we could not determine the accuracy of multiple accounts with material balances due to BBWC's inability to provide us with sufficient appropriate audit evidence to verify them. Therefore, even if BBWC incorporates certain audit adjustments made by UAFCB, BBWC's financial data could not be relied upon.

The Statements of Cash Flows are not required by the Commission when BBWC filed its Annual Reports with the Commission. Therefore, the accompanying Statement of Cash Flows for 2017 was compiled by UAFCB based on the 2017 financial information of BBWC Balance Sheets and Income Statements. Likewise, the Statement of Cash Flows for 2016 was compiled by UAFCB based on the 2016 reported or unaudited financial information of BBWC Balance Sheets and Income Statements.

(a) Appendices

The accompanying Appendices are an integral part of the financial statements. Appendix A presents the net financial impact resulting from audit adjustments by Utility Audit, Finance, and Compliance Branch (UAFCB) for the Year 2017. Appendix B summarizes the UAFCB detail audit adjustments for the Year 2017.

(b) Water Plant in Service

Utility plant should be recorded at original cost when first constructed or purchased. BBWC did not maintain a detail list of water plant assets. Even though UAFCB repeatedly requested the supporting documents for the water plant assets, BBWC was unable to provide UAFCB with a detail list supporting the value of the utility's assets. UAFCB was unable to satisfy itself by other auditing procedures concerning this account balance of \$2,039,904. Therefore, UAFCB was unable to verify the accuracy of this account.

(c) Water Plant in Service - SDWBA

Utility plant funded using Safe Drinking Water Bond Act (SDWBA) aka State Revolving Fund (SRF) is recorded at a SDWBA loan amount. BBWC's SDWBA loan of \$1,228,968 from the California Department of Water Resources (DWR) was fully funded as of 1991. DWR restructured a loan amount of \$742,951 at the same interest rate as the original loan of 4.14% with a repayment period of twenty-five (25) years from 2012 through 2037. BBWC is required to repay the loan principal plus interest by making semi-annual installment payments of \$24,001 until the loan is paid in full. The purpose of the loan was to assist in the financing of a construction project, which will enable the BBWC to meet the California safe drinking water standards.

(d) Accumulated Depreciation and Depreciation Expense of Water Plant

The depreciation expense was computed at a composite rate of 2.1% in order to depreciate all plant assets for ratemaking purposes and for reporting the depreciation expense in BBWC's Annual Reports filed with the Commission. BBWC could not provide supporting documents for the 2.1% composite rate it used to depreciate its plant assets

(e) Accumulated Amortization and Amortization Expense of SDWBA Loan

The SDWBA loan of \$1,228,968 from DWR carries a compounded interest rate of 4.14% per annum. The 30 years loan amortization period commenced in 1992 and was restructured in 2012 for 25 years, which ends 2037; the amortization expense is computed on a straight-line basis for the remaining years.

(f) Other Paid-in Capital

In its 2017 Annual Report, BBWC reported zero (\$0) Other Paid-in Capital. Even though UAFCB repeatedly requested the supporting documents for the substantial decrease of \$1,792,868 from the 2016 beginning balance, BBWC could not provide UAFCB adequate documentation to support the change. UAFCB was unable to satisfy itself by other auditing procedures concerning this account. Therefore, UAFCB was unable to verify the accuracy of this account.

(g) Non-utility Property and Other Assets

This account included personal credit card charges, loans from shareholders, etc. that were not related to providing services to its customers. BBWC reported a balance of \$315,220 as of December 31, 2016. Since BBWC's Board of Directors' Minutes did not authorize shareholder loans or allow its shareholders to charge its business credit card for personal purchases, those transactions should not have been recorded in this account. The credit card charges for personal purchases should have been treated as dividends to shareholders and recorded in Account 215, Retained Earnings. Due to scope limitation, UAFCB did not audit the balance of \$315,220 as of December 31, 2016, nor did UAFCB make an audit adjustment to it. Similarly, BBWC reported a balance of \$391,670 as of December 31, 2017.

UAFCB adjusted \$29,265 relating to personal purchases from this account.
UAFCB's audit adjustment is presented in Audit Adjustment 1 of Appendix B.

(h) Operating Water Revenue

BBWC's water service revenue came from unmetered service (flat rate), private fire protection service, and metered service customers. For 2017, BBWC's water service revenue from unmetered service, private fire protection service, and metered water service were approximately 0.68%, 0.15%, and 98.59% of total water service revenue, respectively. BBWC billed its customers for water services based on tariffs approved by the Commission. BBWC's 2017 Annual Report submitted to the Commission was inaccurate. BBWC had understated Metered Water Revenue by \$12,061 based on their Water Revenue Report. The reported Operating Water Revenue of \$478,635 would be adjusted to \$490,972, which also includes \$276 immaterial variance that UAFCB did not make adjustment to.

(i) Retained Earnings

UAFCB could not attest to the accuracy of the Retained Earnings balances due to the lack of historical information on them. Expressing an opinion on the Retained Earnings Balances as of December 31, 2017, would require auditing the Retained Earnings balances from the inception of the company. Although UAFCB did not audit BBWC's financial data for the year 2016 or prior, UAFCB noted a fluctuation of BBWC's Retained Earnings from (\$461,132) to \$65,985 within 2016. BBWC did not provide documents to support its own prior period adjustment of \$512,826 shown in Schedule A-9 of the 2016 Annual Report. In addition, the reported Retained Earnings balance should have been reduced by the amounts recorded in Non-utility Property and Other Assets that pertained to the use of business funds for personal expenses. BBWC could not provide UAFCB adequate documentation to support the change of the reported amounts. UAFCB was unable to satisfy itself by other auditing procedures concerning the reported amount. Due to limitation of our audit scope and BBWC's inability to provide adequate documents to support the fluctuation as discussed above, we cannot and do not express an opinion on the Retained Earning balance as of December 31, 2017.

(j) User Fees

Water Utilities should include the User Fees into the water services billings charged to their customers and record the total billed amounts as their operating revenue. Payments of User Fees to the Commission should be recorded into the Regulatory Commission Expense account when payments are due.

(2) Annual Reports

Per California Public Utilities Code, Sections 581, 582, and 584, BBWC is required to file an annual report with the Commission every year. For the year being audited, BBWC has complied with these requirements.

Appendix A

Summary of Net Financial Impact Resulting from UAFCB's Audit Adjustments for Year 2017

The following is a summary of net financial impact resulting from UAFCB's audit adjustments for Year 2017:

Audit Adjustment Number	Annual Report				Description	For the Year 2017	
	Sch.	Line	Col.	Acct. No.		Debit	Credit

Net Financial Impact on Balance Sheets Items:

1, 2	A	22	c	121	Non-utility Property and Other Assets		\$34,465
7, 8	A	33	c	142	Receivables from Affiliated Companies	\$1,861	
3	A	2	c	201	Common Stock	45,302	
3	A	5	c	211	Other Paid-in Capital		45,302
1,4,9	A	6	c	215	Retained Earnings	44,484	
6	A	17	c	231	Accounts Payable		6,265
2	A	22	c	241	Other Current Liabilities	5,200	

Net Financial Impact on Income Statements Items:

7, 8, 9	B	8	c	408	Taxes Other Than Income Taxes		\$5,399
9	B	16	c	426	Miscellaneous Non-utility Expense	\$380	
4	B-1	17	b	470	Metered Water Revenue		12,061
5	B-2	22	b	678	Office Services and Rentals		1,491
5	B-2	23	b	681	Offices Supplies and Expenses	1,491	
6	B-2	26	b	688	Regulatory Commission Expense	6,265	

Appendix B

Summary of Audit Adjustments for Year 2017

Audit Adj. No.	Annual Report				Description	For the Year 2017	
	Sch.	Line	Col.	Acct. No.		Debit	Credit
1	A	6	c	215	Retained Earnings	\$29,265	
	A	22	c	121	Non-utility Property and Other Assets <i>To adjust credit card payments recorded in Non-utility Property and Other Assets to the audited amount.</i>		\$29,265
2	A	22	c	241	Other Current Liabilities	\$5,200	
	A	22	c	121	Non-utility Property and Other Assets <i>To reclassify loan repayment recorded in Non-utility Property and Other Assets to Other Current Liabilities.</i>		\$5,200
3	A	2	c	201	Common Stock	\$45,302	
	A	5	c	211	Other Paid-in Capital <i>To reclassify Common Stock to Other Paid-in Capital to reflect the par value.</i>		\$45,302
4	A	6	c	215	Retained Earnings	\$12,061	
	B-1	23	b	470	Metered Water Revenue <i>To adjust Metered Water Revenue to the audited amount.</i>		\$12,061
5	B-2	23	b	681	Office Supplies and Expenses	\$1,491	
	B-2	22	b	678	Office Services and Rentals <i>To reclassify Office Services and Rentals to Office Supplies and Expense.</i>		\$1,491
6	B-2	26	b	688	Regulatory Commission Expense	\$6,265	
	A	17	c	231	Accounts Payable <i>To record Regulatory Commission Expense to agree with the audited amount.</i>		\$6,265

Financial Audit of Big Basin Water Company, Inc. Financial Statements
For the Year Ended December 31, 2017

Audit Adj. No.	Annual Report				Description	For the Year 2017	
	Sch.	Line	Col.	Acct. No.		Debit	Credit
7	A	33	c	142	Receivables from Affiliated Companies	\$874	
	B	8	c	408	Taxes Other Than Income Taxes <i>To reclassify Taxes Other Than Income Taxes to Receivables from Affiliated Companies for the Sewer Co. property taxes.</i>		\$874
8	A	33	c	142	Receivables from Affiliated Companies	\$987	
	B	8	c	408	Taxes Other Than Income Taxes <i>To reclassify Taxes Other Than Income Taxes to Receivables from Affiliated Companies due to Sewer Co. payroll taxes.</i>		\$987
9	A	6	c	215	Retained Earnings	\$3,158	
	B	16	c	426	Miscellaneous Non-utility Expense	380	
	B	8	c	408	Taxes Other Than Income Taxes <i>To adjust Taxes Other Than Income Taxes to account for accruals and reclassify penalties to Miscellaneous Non-utility Expense.</i>		\$3,538