

PUBLIC UTILITIES COMMISSION

505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298



Transmitted via e-mail

August 16, 2021

Mr. David Bower, President
North Gualala Water Company
P. O. Box 1000
Gualala, CA 95445

Dear Mr. Bower:

Final Report Transmittal Letter—Review of North Gualala Water Company’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 North Gualala Water Company’s (NGWC) 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 statement of income. The final review report is enclosed.

NGWC’s response to the draft report findings has been incorporated into this final report. NGWC agreed with our review findings. We will post this review report on our website at [Audit Reports by Industry \(ca.gov\)](https://www.cpuc.ca.gov/Audit-Reports-by-Industry).

Please provide a Corrective Action Plan (CAP) addressing the findings and recommendations by September 30, 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 NGWC’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

Mr. David Bower, President
North Gualala Water Company
August 16, 2021
Page 2

cc: Suzette Eissler, Office Manager, North Gualala Water Company
Rachel Peterson, Executive Director, CPUC
Saul Gomez, Deputy Executive Director, Office of the Commission, CPUC
Terence Shia, Director, Water Division
Masha Vorobyova, Assistant Director, UAB
Bruce Berry, Program Manager, Water Division
Raymond Yin, Program and Project Supervisor, UAB
Khusbindar Kaur, Senior Management Auditor, UAB
Sam Niepoth, Staff Services Management Auditor, UAB



REVIEW OF FINANCIAL STATEMENTS

North Gualala Water Company

For the Year Ended December 31, 2019

Utility Audits, Risk and Compliance Division
Utility Audits Branch
August 16, 2021



MEMBERS OF THE TEAM

Angie Williams, Director

Masha Vorobyova, Assistant Director

**Raymond Yin, CPA
Program and Project Supervisor**

**Khusbindar Kaur, CPA
Lead**

**Sam Niepoth
Staff**

A digital copy of this report can be found at:
[Audit Reports by Industry \(ca.gov\)](#)

You can contact our office at:
California Public Utilities Commission
Utility Audits, Risk and Compliance Division
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TABLE OF CONTENTS

EXECUTIVE SUMMARY.....	1
INDEPENDENT ACCOUNTANT’S REVIEW REPORT.....	4
REVIEWED FINANCIAL STATEMENTS	6
Balance Sheet (As Reviewed).....	6
Income Statement (As Reviewed).....	7
Statement of Changes in Shareholders’ Equity (As Compiled).....	8
Notes to Financial Statements.....	9
APPENDIX A—REVIEW FINDINGS AND RECOMMENDATIONS.....	15
APPENDIX B—NGWC’S RESPONSE.....	27

EXECUTIVE SUMMARY

The Utility Audits Branch (UAB) of the California Public Utilities Commission (CPUC) conducted a review of the financial statements of North Gualala Water Company (NGWC) 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 of Financial Statements in the Generally Accepted Government Auditing Standards (GAGAS).

NGWC was incorporated in California on May 17, 1966. NGWC is a Class C water utility with 1,030 active metered water service connections in the vicinity of Mendocino County, California. As a regulated water utility, NGWC 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 them to be in accordance with the USOA. In conjunction with our review of the financial statements, UAB also reviewed, for regulatory purposes, whether NGWC 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 NGWC'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 NGWC filed its 2019 Annual Report timely in compliance with the CPUC directive from the Water Division. However, UAB identified 12 material misstatements in NGWC's Annual Report originally filed with CPUC's Water Division on August 26, 2020, as described in Appendix A – Review Findings and Recommendations. These findings are summarized below:

- Finding 1: NGWC incorrectly reported changes in its ownership equity in Account 215–Retained Earnings instead of Account 206–Subchapter S Corporation Accumulated Adjustments Account. As a result, NGWC overstated Account 215–Retained Earnings by \$1,700,754, and understated Account 206–Subchapter S Corporation Accumulated Adjustments Account by the same amount.
- Finding 2: NGWC misclassified \$469,680 of costs associated with water plant still under construction in Account 101.1–Water Plant in Service (WPIS)–SDWBA instead of Account 105.1–Construction Work in Progress–SDWBA. As a result, NGWC overstated Account 101.1–WPIS–SDWBA/SRF by \$469,880, and understated Account 105.1–Construction Work in Progress–SDWBA by the same amount.

- Finding 3: NGWC incorrectly recorded and deferred its corporate income taxes between 2014 and 2019. NGWC overstated Account 410–Federal Corporate Income Tax Expense, Account 409–State Corporate Income Tax Expense, Account 283–Accumulated Deferred Income Tax Liabilities, and Account 236–Taxes Accrued by \$42,887, \$19,004, \$261,057, and \$40,084, respectively; and understated Account 241–Other Current Liabilities and Account 206–Subchapter S Corporation Accumulated Adjustments Account by \$19,265 and \$219,985, respectively. As a Subchapter S Corporation, NGWC should not have incurred any corporate income tax expense because shareholders of an S Corporation are individually responsible for their proportional corporate income taxes based on their allocated share of total corporate income.
- Finding 4: NGWC did not record \$77,898 of Safe Drinking Water Bond Act (SDWBA) Loan Amortization Expense for assets financed by its 2016 State Revolving Fund Loan (SRF) in Account 407–SDWBA Loan Amortization Expense. In addition, NGWC over-amortized its SDWBA loan in prior years by \$215,883. As a result, NGWC overstated Account 108.1–Accumulated Amortization of SDWBA Loan by \$215,883, and understated Account 407–SDWBA Loan Amortization Expense and Account 206–Subchapter S Corporation Accumulated Adjustments Account by \$77,898 and \$293,781, respectively.
- Finding 5: NGWC did not classify the current portion of its Long-Term Debt totaling \$214,442 to the Short-Term Notes Payable account. As a result, NGWC overstated Account 224–Long-Term Debt by \$214,442 and understated Account 232–Short-Term Notes Payable by the same amount.
- Finding 6: NGWC misclassified \$169,687 of water plant funded with a local grant as utility-funded water plant and incorrectly recorded \$36,398 of related depreciation for the water plant funded by the local grant as utility-funded water plant. As a result, NGWC overstated Account 101–WPIS by \$169,687 and understated Account 101.2–Water Plant in Service–Grant Funds by the same amount. Additionally, NGWC overstated Account 108–Accumulated Depreciation of Water Plant by \$36,398 and understated Account 108.2–Accumulated Depreciation of Water Plant–Grant Funds Account 101.2 by the same amount.
- Finding 7: NGWC incorrectly recorded and reported \$101,625 of the collected but unspent Facilities Fees as Contributions in Aid of Constructions (CIAC). In addition, NGWC incorrectly recorded \$2,760 of Connection Fees as Other Water Revenues instead of recording it as CIAC. As a result, NGWC overstated Account 265–Contributions in Aid of Construction and Account 206–Subchapter S Corporation Accumulated Adjustments Account by \$98,685 and \$2,760, respectively; and understated Account 253–Other Credits by \$101,625.
- Finding 8: NGWC misclassified \$46,016 of deferred credits related to its Conservation Lost Revenues Memorandum Account as Other Current Liabilities in Account 241 instead of reporting it as Other Credits in Account 253. As a result, NGWC overstated Account 241–Other Current Liabilities by \$46,016, and understated Account 253–Other Credits by the same amount.

- Finding 9: NGWC misclassified expenses totaling \$26,037 for unused vacation and sick leave as employee salaries and wages expenses instead reporting it in Account 674–Employee Pension and Benefits. As a result, NGWC overstated Account 630–Employee Labor, Account 670–Office Salaries, and Account 671–Management Salaries by \$2,245, \$11,455, and \$12,337, respectively; and understated Account 674– Employee Pension and Benefits by \$26,037.
- Finding 10: NGWC over-accrued \$20,175 interest expenses in Year 2018. To correct this prior over-accrual in its 2019 Annual Report, NGWC reduced \$20,175 in Account 427– Interest Expense instead of Account 206–Subchapter S Corporation Accumulated Adjustments Account. As a result, NGWC overstated Account 427–Interest Expense by \$20,175, and understated Account 206–Subchapter S Corporation Accumulated Adjustments Account by the same amount.
- Finding 11: NGWC recorded \$18,683 CPUC Users Fee collected from its customers and remitted to the CPUC as a pass-through activity instead of reporting them in the proper accounts as revenue and expenses. As a result, NGWC understated both Account 480– Other Water Revenue and Account–688 Regulatory Commission Expense by \$18,683.
- Finding 12: NGWC incorrectly recorded and reported \$6,180 of late fees, and the \$3,820 of disconnection and reconnection fees in Account 421–Non-Utility Income instead of recording it as Other Water Revenue in Account 480. As a result, NGWC overstated Account 421–Non-Utility Income by \$10,000, and understated Account 480–Other Water Revenue by the same amount.

UAB discussed the findings and recommendations with NGWC during fieldwork. NGWC concurred with the findings and agreed to correct the misstatements identified above. NGWC submitted its revised Annual Report to the CPUC to correct the material misstatements described in Appendix A of this report on June 8, 2021. UAB further discussed the findings and recommendations presented in Appendix A of this report with NGWC at the exit conference on June 16, 2021, and NGWC concurred with the review results. We are not aware of any material modifications that should be made to the revised financial statements. UAB provided a draft review report to NGWC for comments on July 13, 2021. NGWC submitted its comments on July 28, 2021, agreeing to implement UAB’s recommendations. The review findings and recommendations presented in this report represent our final determination of this review engagement.

INDEPENDENT ACCOUNTANT'S REVIEW REPORT

Mr. David Bower, President
North Gualala Water Company
P. O. Box 1000
Gualala, CA 95445

The Utility Audits Branch (UAB) of the California Public Utility Commission (CPUC) has reviewed the financial statements of North Gualala Water Company (NGWC), which comprise the balance sheet as of December 31, 2019, and the related income statement for the year then ended. A review includes primarily applying analytical procedures to management's financial data and making inquiries of NGWC'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

NGWC'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. NGWC'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, NGWC'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 of financial statements 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 NGWC complied with PU Code Section 818 to obtain its long-term debts, and whether NGWC timely filed its 2019 Annual Report as required by CPUC's Water Division. We believe that the results of our procedures provide 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 12 material misstatements in NGWC's Annual Report originally filed with 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, NGWC 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. NGWC'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

We conducted an exit conference on June 16, 2021 and discussed our review results with NGWC management. NGWC management concurred with UAB's findings and agreed to make appropriate adjusting journal entries to its accounting records to correct the material misstatements as described in Appendix A of this report. At the exit conference, we also stated that the final report will include the views of responsible officials. UAB provided a draft review report to NGWC for comments on July 13, 2021. NGWC submitted its comments on July 28, 2021, agreeing to implement UAB's recommendations. 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

NGWC'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 September 30, 2021. The corrective action plan should address how NGWC will implement the recommendations and provide the timing of incorporating UAB's review adjustments to NGWC's books and records. If NGWC 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. NGWC should use the amounts reviewed by the UAB as presented in this report as the basis to file its 2021 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 NGWC. 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

REVIEWED FINANCIAL STATEMENTS

North Gualala Water Company Balance Sheet (As Reviewed) For Year Ended December 31, 2019

ASSETS	
UTILITY PLANT	
Water Plant in Service	\$3,719,207
Water Plant in Service - SDWBA/SRF	4,442,521
Water Plant in Service – Grant Funds	169,687
Construction Work in Progress - Water Plant	324,122
Construction Work in Progress - Water Plant – SDWBA/SRF	469,880
Accumulated Depreciation of Water Plant	(2,297,076)
Accumulated Amortization of SDWBA/SRF Loan	(2,323,566)
Accumulated Depreciation of Water Plant - Grant Funds	(36,398)
Net Utility Plant	<u>4,468,377</u>
CURRENT AND ACCRUED ASSETS	
Cash	386,760
Special Deposits	380,248
Accounts Receivable	100,002
Materials and Supplies	35,604
Other Current Assets	19,481
Deferred Charges	264,055
Total Current and Accrued Assets	<u>1,186,150</u>
Total Assets	<u><u>\$5,654,527</u></u>
CAPITALIZATION AND LIABILITIES	
CORPORATE CAPITAL AND SURPLUS	
Common Stock	\$500
Subchapter S Corporation Accumulated Adjustments Account	2,195,755
Total Capitalization	<u>2,196,255</u>
LONG-TERM DEBT	
Long-Term Debt	2,335,442
CURRENT AND ACCRUED LIABILITIES	
Accounts Payable	16,178
Short-Term Notes Payable	214,442
Customer Deposits	35,280
Interest Accrued	18,189
Other Current Liabilities	26,037
Total Current and Accrued Liabilities	<u>310,126</u>
DEFERRED CREDITS	
Other Credits	147,641
CONTRIBUTIONS IN AID OF CONSTRUCTION	
Contributions in Aid of Construction	1,747,660
Accumulated Amortization of Contributions	(1,082,597)
Net Contributions in Aid of Construction	<u>665,063</u>
Total Equity and Liabilities	<u><u>\$5,654,527</u></u>
<i>(See independent accountant's review report and accompanying notes.)</i>	

North Gualala Water Company
Income Statement (As Reviewed)
 For Year Ended December 31, 2019

OPERATING REVENUES

Metered Water Revenue	\$1,383,063
Other Water Revenue	35,366
Total Operating Revenue	<u>1,418,429</u>

OPERATING EXPENSES**Plant Operation and Maintenance Expenses**

Power	84,750
Other Volume Related Expenses	9,758
Employee Labor	211,249
Materials	34,400
Contract Work	53,194
Transportation Expenses	30,791
Other Plant Maintenance Expenses	7,140
Total Plant Operation and Maintenance Expenses	<u>431,282</u>

Administrative and General Expenses

Office Salaries	88,128
Management Salaries	91,534
Employee Pensions and Benefits	97,785
Office Services and Rentals	6,000
Office Supplies and Expenses	90,601
Professional Services	174,436
Insurance	56,186
Regulatory Commission Expense	18,683
General Expenses	7,800
Net Administrative and General Expenses	<u>631,153</u>

Total Operating Expenses

1,062,435

Depreciation Expense	62,010
SDWBA/SRF Loan Amortization Expense	210,524
Taxes Other Than Income Taxes	73,329
State Corporate Income Tax Expense	800
Total Operating Revenue Deductions	<u>1,409,098</u>

Total Utility Operating Income

9,331

OTHER INCOME AND DEDUCTIONS

Non-Utility Income	168
Interest expense (excluding SDWBA)	6,346
Interest expense (SDWBA)	72,636
Total Other Income and Deductions	<u>(78,814)</u>

Net Loss\$(69,483)

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

North Gualala Water Company
Statement of Changes in Shareholders' Equity (As Compiled¹)
 For Year Ended December 31, 2019

Stockholder's Equity, Beginning of Year	\$1,734,554
 CREDITS:	
UAB Adjustment to Accumulated Amortization of SDWBA Loan	293,781
UAB Adjustment to interest expense	20,175
UAB Adjustment to Deferred Income Tax Liabilities	261,057
UAB Adjustment to Taxes Accrued	40,084
UAB Rounding Adjustment	3
Total Credits	615,100
 DEBITS:	
Net Loss	69,483
UAB Adjustment to Federal Corporate Tax Expense	42,887
UAB Adjustment to state corporate tax expense	19,004
UAB Adjustment to Other Current Liabilities	19,265
UAB Adjustment to Contributions in Aid of Construction	2,760
Total Debits	153,399
 Stockholder's Equity, End of Year	 \$2,196,255

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

¹ UAB compiled the Changes in Shareholder's Equity based on the reviewed Balance Sheet and Income Statement, and other relevant financial data.

North Gualala Water Company

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 followings describe 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.² The utility must obtain prior written approval from the CPUC for any practice deviates from the aforementioned SPs.

² D.16.11-006 dated November 10, 2016, General Accounting Instructions 4 on Page B14.

North Gualala Water Company (NGWC) utilizes the straight-line remaining life method for each class of asset as prescribed in SP U-4-SM to determine depreciation accruals.

(2) Asset Retirement

USOA requires that water plant be recorded at 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.

NGWC did not retire any assets during the review period.

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.

NGWC reported an inventory balance of \$35,604 in Account 151—Materials and Supplies.

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.

NGWC reported a balance of \$380,248 for cash for restricted use in Account 132, Cash—Special Deposits. The total restricted cash consists of \$237,481 for Safe Drinking Water Bonds Act Loan reserves, \$101,625 of unspent Facilities Fees, and \$41,142 of Customer Security Deposits.

5. Contribution in Aid of Construction (CIAC)

CIAC account records non-refundable contributions of cash, land or other property donated to the water utility to assist it in constructing, extending, or relocating its water system. The funds can be from governmental agencies and others. The balances in this account shall be written off over the period of its estimated service life by charging to Account 272, Accumulated Amortization of Contributions instead of a Deprecation Expense account, with contra credits to the appropriate subaccount of Account 108, Accumulated Depreciation of Water Plant.

(1) Facilities Fees

Facilities Fees are fees collected from ratepayers for the purpose of recovering a certain amount of revenue to offset certain facilities or improvements that are required to serve additional customers. Ordering Paragraph 3 of D.91-04-068 granted authority to Class C and D water utilities, and to districts of Class A and B water utilities with 2,000 or fewer service connections, to institute facilities fees as a part of their requests for a general increase in rates. Through Resolution W-4110, the CPUC granted authority to all Class D water utilities to file generic tariffs to charge fees for new connections for the purpose of generating funds to build a new plant or replace deteriorated plant. Facilities fees received by a water utility shall be deposited in Account 132, Cash–Special Deposits and credited to Account 253, Other Credits. At the time these fees are used for water plant improvements, Account 101, WPIS shall be debited and Account 132, Cash–Special Deposits credited. Concurrently, Account 253, Other Credits shall be debited and Account 265.7, All Other Contributions in Aid of Construction credited. The annual depreciation and amortization of the facilities fees plant additions shall be debited to Account 272, Accumulated Amortization of Contributions, and credited to Account 108.3, Accumulated Depreciation of Water Plant–Other. The use of facilities fees should be in compliance with SP U-28-W.

In its 2019 Annual Report originally filed with CPUC’s Water Division, NGWC incorrectly reported \$101,625 of unspent Facilities Fees collections in Account 265–CIAC instead of reporting the unspent amount as Other Credits in Account 253. On June 8, 2021, NGWC submitted a revised Annual Report to the CPUC and corrected these misstatements.

6. Safe Drinking Water Bond Act (SDWBA) Loans

SDWBA loans are low-interest loans from the California Department of Water Resources (DWR) to assist water utilities to fund for materials and services used on DWR-approved construction projects. SDWBA loans are repaid through surcharges on customer water bills. Although the accounting treatment of SDWBA loans is similar to GAAP, the USOA requires water utilities to follow the special accounting procedures below:

Water utilities must obtain CPUC’s written approval prior to obtaining a SDWBA loan and instituting a SDWBA surcharge to its ratepayers. Any SDWBA surcharge collected from ratepayers shall be deposited monthly to Account 132, Cash–Special Deposits. The periodical payment of the SDWBA loans and related interest expenses shall be made from this special deposit account.

Plant assets funded by a SDWBA loan are booked in Account 101.1, Water Plant in Service–SDWBA, and are not depreciable. The principal of a SDWBA loan is amortized through the charges to Account 407, SDWBA Loan Amortization Expense, with contra credits to Account 108.1, Accumulated Amortization of SDWBA Loan, over the life of the SDWBA loan.

In its 2019 Annual Report originally filed with CPUC's Water Division, NGWC did not record \$77,898 of Safe Drinking Water Bond Act (SDWBA) Loan Amortization Expense for assets financed by its 2016 State Revolving Fund (SRF) Loan in Account 407. In addition, NGWC overstated the Accumulated Amortization of SDWBA Loan in Account 108.1 by \$215,883 due to over-amortization of SDWBA loan in prior years. On June 8, 2021, NGWC submitted a revised Annual Report to the CPUC and corrected these misstatements.

7. Long-Term Debt

Water utilities are required to obtain prior authorization from the CPUC before incurring any long-term debt. PU Code Section 818 states that,

No public utility may issue stocks and stock certificates, or other evidence of interest or ownership, or bonds, notes, or other evidences of indebtedness payable at periods of more than 12 months after the date thereof unless, in addition to the other requirements of law it shall first have secured from the commission an order authorizing the issue, stating the amount thereof and the purposes to which the issue or the proceeds thereof are to be applied, and that, in the opinion of the commission, the money, property, or labor to be procured or paid for by the issue is reasonably required for the purposes specified in the order, and that, except as otherwise permitted in the order in the case of bonds, notes, or other evidences of indebtedness, such purposes are not, in whole or in part, reasonably chargeable to operating expenses or to income.

As of December 31, 2021, NGWC had the following long-term debts outstanding:

Description	Current Portion	Long-Term Debt	Total Principal Outstanding
1996 SDWBA Loan	\$136,544	\$2,257,542	\$2,394,086
2016 SRF Loan	\$77,898	\$77,899	\$155,797
Total	\$214,442	\$2,335,441	\$2,549,883

(a) 1996 SDWBA Loan

In Resolution F-645, dated January 24, 1996, the CPUC authorized NGWC to enter into a loan agreement with DWR to borrow \$3,081,938 under the SDWBA. In Resolution W-4108, dated August 6, 1998, the CPUC granted NGWC authority to borrow an additional \$1,582,709 (for a total loan principal of \$4,664,647). The proceeds of the loan were used for the replacement of existing water mains, construction of water storage facilities including a pump station and emergency generators, and improvements to NGWC's surface water treatment plant. In April 2000, NGWC obtained the loan from DWR. The combined SDWBA loan carries an interest rate of 2.973%, a term of 35 years, and secured by NGWC's assets. NGWC has consistently paid its semi-annual payments over the last 5 years.

(b) 2016 SRF Loan

In Resolution W-4778, dated July 30, 2009, the CPUC authorized NGWC to secure a \$400,000 planning loan under the SRF Loan Program, to be used to conduct various studies and investigations for the improvement and maintenance of NGWC's water system. In June

2017, NGWC drew \$389,493 from the loan. This is an interest free loan to be paid over 5 years. NGWC has consistently paid its semi-annual payments.

In its 2019 Annual Report originally filed with CPUC's Water Division, NGWC incorrectly classified the current portion of its long-term liabilities totaling \$214,442 in the Short-Term Notes Payable account. As a result, Account 224—Long-Term Debt was overstated by \$214,442 and Account 232—Short-Term Notes Payable was understated by the same amount. On June 8, 2021, NGWC submitted a revised Annual Report to the CPUC and corrected these misstatements.

8. Authorized Costs and Revenues

Under GAAP, regulated entities record recoverable costs authorized by the regulator as Regulatory Assets and amortize them over a period of time. Likewise, authorized revenues for future repayment are recorded as Regulatory Liabilities.

USOA requires water utilities to record authorized costs that are to be amortized over future periods as an asset in Account 180, Deferred Charges. Similarly, authorized revenues for future repayment are recorded as liabilities in Account 253, Other Credits.

NGWC's reported Deferred Charges consist of SDWBA Loan Administrative Fees being amortized, Water Supply Memorandum Account, and Conservation Lost Revenue Memorandum Account. NGWC expects to recover these costs through future General Rate Case (GRC).

9. 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.³

In its 2019 Annual Report originally filed with CPUC's Water Division, NGWC incorrectly treated CPUC Users Fee totaling \$18,683 collected from its customers and remitted to the CPUC as a pass-through activity without reporting the revenue and expenses associated with the collections and remission of the Users Fee. On June 8, 2021, NGWC submitted a revised Annual Report to the CPUC and corrected these misstatements.

10. 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...."

³ D.16.11-006 dated November 10, 2016, General Accounting Instructions 9 on Pages B18 and B19.

NGWC rented its office space from its affiliated company, Bower Limited Partnership. The total rent expense for 2019 was \$6,000.

11. Form of Financial Statements ⁴

(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 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 affects the form of the income statement, the classification of revenues and expenses, and decisions of management in incurring expenses.

12. 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 purpose, the Statement of Cash Flows is not required and therefore excluded from this review report.

13. 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, NGWC has complied with these requirements.

⁴ Regulated Utilities Manual—A Service for Regulated Utilities by Deloitte & Touché USA LLP, pages 36-37.

APPENDIX A—REVIEW FINDINGS AND RECOMMENDATIONS

Finding 1: Incorrect Reporting of Changes in Ownership Equity

Condition:

NGWC incorrectly reported changes in its ownership equity in Account 215—Retained Earnings instead of Account 206—Subchapter S Corporation Accumulated Adjustments Account in the Annual Report originally filed with CPUC’s Water Division on August 26, 2020. NGWC operates as a S Corporation. The USOA requires that Account 206—Subchapter S Corporation Accumulated Adjustments Account be used by S Corporations for reporting changes in its ownership equity. As a result, NGWC overstated Account 215—Retained Earnings by \$1,700,754 and understated Account 206—Subchapter S Corporation Accumulated Adjustments Account by the same amount. NGWC corrected these misstatements in its revised Annual Report submitted to the CPUC on June 8, 2021.

Criteria:

The USOA states, in part, that:

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.

206. Subchapter S Corporation Accumulated Adjustments Account

- A. This account shall be used by Subchapter S Corporations for the reporting of changes in its ownership equity.
- B. This account shall include all paid-in-capital not derived from earnings.
- C. This account shall be credited with:
 - 1. Net income.
 - 2. Accounting adjustments not properly attributable to the current period.
- D. This account shall be charged with:
 - 1. Net loss.
 - 2. Accounting adjustments not properly attributable to the current period.
 - 3. Dividends.

Cause:

NGWC stated that it was unaware of the accounting changes in the most recent USOA, which requires Subchapter S Corporations to report its ownership equity in Account 206. NGWC lacks monitoring procedures to identify changes in the regulatory environment to ensure compliance with the accounting requirements mandated by the USOA.

Effect:

Inaccurate reporting of Subchapter S Corporation Accumulated Adjustments Account and Retained Earnings account balances distorted NGWC's financial position as of December 31, 2019, which could mislead decision-makers about NGWC's tax structure and its responsibility for corporate income taxes.

Recommendations:

NGWC should establish and implement monitoring procedures to ensure that it timely identifies changes in regulatory accounting and reporting requirements. It should ensure that Account 206—Subchapter S Corporation Accumulated Adjustments Account is used to report changes in its ownership equity as required by the USOA.

Finding 2: Misclassified Costs for Construction Work in Progress**Condition:**

NGWC misclassified \$469,680 of costs associated with water plant still under construction in Account 101.1—Water Plant in Service (WPIS)—SDWBA instead of recording them in Account 105.1—Construction Work in Progress—SDWBA in the Annual Report originally filed with CPUC's Water Division on August 26, 2020. As a result, NGWC overstated Account 101.1—WPIS—SDWBA/SRF by \$469,880, and understated Account 105.1—Construction Work in Progress—SDWBA by the same amount. NGWC corrected these misstatements in its revised Annual Report submitted to the CPUC on June 8, 2021.

Criteria:

The USOA states, in part, that:

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. The following subaccounts should be maintained, if applicable:

101.1 Water Plant in Service - SDWBA

101.2 Water Plant in Service - Grant Funds

101.3 Water Plant in Service – Other

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. The following subaccounts should be maintained, if applicable:

105.1 Construction Work in Progress – SDWBA

105.2 Construction Work in Progress - Grant Funds

105.3 Construction Work in Progress – Other

Cause:

NGWC lacks internal control procedures over its construction projects to ensure its compliance with the USOA accounting requirements. NGWC also lacks monitoring procedures to ensure that the costs of water plant still under construction, but not yet ready for service, were reported as Construction Work in Progress–SDWBA/SRF in Account 105.1.

Effect:

Inaccurate reporting of WPIS and Construction Work in Progress in the Annual Report, which may be used during NGWC's General Rate Case (GRC) application review process, could potentially impact the water rates for NGWC ratepayers.

Recommendation:

NGWC should establish and implement internal control and monitoring procedures over its construction projects to ensure that costs associated with projects still under construction, but not yet in service, are properly recorded and reported as Construction Work in Progress in Account 105.1.

Finding 3: Inaccurate Reporting of Corporate Income Taxes**Condition:**

NGWC incorrectly reported its corporate income taxes in the Annual Report originally filed with CPUC's Water Division on August 26, 2020. Specifically, NGWC overstated Account 410–Federal Corporate Income Tax Expense, Account 409–State Corporate Income Tax Expense, Account 283–Accumulated Deferred Income Tax Liabilities, and Account 236–Taxes Accrued by \$42,887, \$19,004, \$261,057 (\$61,891 + \$199,166), and \$40,084, respectively; and understated Account 241–Other Current Liabilities and Account 206–Subchapter S Corporation Accumulated Adjustments Account by \$19,265 and \$219,985 (\$199,166 + \$40,084 – 19,265), respectively, as follows:

- NGWC has been structured as a Subchapter S Corporation since 2005. S Corporations do not directly pay income taxes. Instead, shareholders of an S Corporation are individually responsible for their proportional corporate income taxes based on their allocated share of total corporate income. NGWC incorrectly reported \$42,887 of Federal Corporate Income Tax in Account 409 and \$19,004 of State Corporate Income Tax in Account 410. As a result, NGWC overstated Federal Corporate Income Tax in Account 410 by \$42,887, and State Corporate Income Tax in Account 409 by \$19,004; and understated Subchapter S Corporation Accumulated Adjustments Account in Account 206 by \$61,891.
- NGWC deferred \$129,436 of federal corporate income tax expense and \$50,464 of state corporate income tax expense accrued between 2016 and 2018. In addition, NGWC deferred \$19,266 of state and federal corporate income taxes prior to 2016. As a result, NGWC overstated Accumulated Deferred Income Tax Liability in Account 283 by \$199,166, and understated Subchapter S Corporation Accumulated Adjustments Account in Account 206 by the same amount.
- NGWC reported a liability of \$40,084 for accrued corporate income taxes in Account 236–Taxes Accrued in the 2019 Annual Report. However, its accounting records showed no activity in the Taxes Accrued account since December 31, 2015. NGWC acknowledged that this reported liability was due to prior over-accrual of state and federal corporate income taxes. As a result, NGWC overstated Taxes Accrued in Account 236 by \$40,084 and

understated Subchapter S Corporation Accumulated Adjustments Account in Account 206 by the same amount.

- NGWC incorrectly accrued state and federal corporate income taxes and recorded the related liability in Account 236–Taxes Accrued in 2014. NGWC attempted to defer \$19,265 income tax liability. However, NGWC incorrectly recorded the deferred income tax liability by removing the \$19,265 from Account 241–Other Current Liabilities instead of Account 236–Taxes Accrued. As a result, NGWC overstated Account 206–Subchapter S Corporation Accumulated Adjustments Account by \$19,265 and understated Account 241–Other Current Liabilities by the same amount.

NGWC corrected these misstatements in its revised Annual Report submitted to the CPUC on June 8, 2021.

Criteria:

The USOA states, in part, that:

410. Federal Corporate Income Tax Expense

A. This account will be used only by incorporated water utilities.

CPUC Decision 20-07-036, at page 3 states, in part, that:

[i]t has consistently been this Commission’s practice to view utilities as separate from their affiliates for ratemaking purposes. As a result, rates will include allowances only for expenses the utility itself pays... Because there is no corporate tax incurred by [a S Corporation], there is no need for a tax allowance in rates.

Cause:

NGWC lacks monitoring procedures to ensure that it complied with the accounting requirements specified in the USOA by reporting only the income tax expenses directly incurred by NGWC.

Effect:

Inaccurate reporting of State Corporate Income Tax Expense (Account 409) and Federal Corporate Income Tax Expense (Account 410) in the Annual Report, which may be used during NGWC’s GRC application review process, could potentially impact the water rates for NGWC ratepayers. Inaccurate reporting of Taxes Accrued (Account 236) and Other Current Liabilities (Account 241) distorted NGWC’s financial position as of December 31, 2019.

Recommendation:

NGWC should establish and implement monitoring procedures to ensure compliance with the accounting requirements specified in the USOA.

Finding 4: Inaccurate Reporting of SDWBA Plant Amortization

Condition:

NGWC understated the SDWBA Loan Amortization Expense by \$77,898 and overstated the Accumulated Amortization of SDWBA Loan by \$215,883 for assets financed by its SDWBA loan in the Annual Report originally filed with CPUC’s Water Division on August 26, 2020. NGWC did not record the SDWBA Loan Amortization Expense for assets financed by its 2016 SRF Loan. In addition, NGWC over-amortized its SDWBA Loan in prior years. As a result, NGWC overstated

Account 108.1—Accumulated Amortization of SDWBA Loan by \$215,883, and understated Account 407—SDWBA Loan Amortization Expense and Account 206—Subchapter S Corporation Accumulated Adjustments Account by \$77,898 and \$293,781 (\$215,883 + \$77,898), respectively. NGWC corrected these misstatements in its revised Annual Report submitted to the CPUC on June 8, 2021.

Criteria:

The USOA states, in part, that:

8. Safe Drinking Water Bonds Act Loans

Safe Drinking Water Bond Act financed plant will not be depreciated on the books of account through charges to Account 403, Depreciation Expense. Instead, the principal amount of the loan will be amortized through the charges to Account 407, SDWBA Loan Amortization Expense, with contra credits to Account 108.1, Accumulated Amortization of SDWBA Loan, over the life of the SDWBA loan. These amortization charges will not be included in cost of service for ratemaking purposes. The intent of these entries is to have an accumulated depreciation balance equal to the amount of plant financed through the loan, when the SDWBA loan is fully paid.

Cause:

NGWC lacks monitoring procedures to ensure its SDWBA Loan was accurately accounted for in accordance with the accounting requirements specified in the USOA, and properly recorded and reported.

Effect:

By inaccurately recording and reporting of SDWBA loan amortization expense and the related accumulated amortization of the SDWBA Loan, NGWC understated its net income in prior years and its ownership equity as of December 31, 2019. Understated ownership equity can misinform decision-makers about the equity available for reinvestment in NGWC's operations.

Recommendation:

NGWC should establish and implement proper monitoring procedures to ensure the accuracy of its SDWBA Loan Amortization and adherence to the USOA accounting requirements.

Finding 5: Misclassified Current Portion of Long-Term Debt**Condition:**

NGWC did not classify the current portion of its Long-Term Debt totaling \$214,442 to the Short-Term Notes Payable account in the Annual Report originally filed with CPUC's Water Division on August 26, 2020. As a result, NGWC overstated Account 224—Long-Term Debt by \$214,442 and understated Account 232—Short-Term Notes Payable by the same amount. NGWC corrected these misstatements in its revised Annual Report submitted to the CPUC on June 8, 2021.

Criteria:

The USOA states, in part, that:

232. Short-Term Notes Payable

This account shall include the face value of all notes, or other similar evidences of indebtedness, payable on demand or within a period not exceeding one year from the date of issue.

224. Long-Term Debt:

A. This account shall include all notes, conditional sales contracts or other evidences of indebtedness payable more than one year from date of issue.

B. A separate subaccount shall be maintained for each obligation outstanding.

Note: Prior authorization must be obtained from this Commission before any long-term indebtedness may be incurred by the utility. (Public Utilities Code, Section 818.)

Cause:

NGWC lacks monitoring procedures over its accounting and reporting process to ensure that all liabilities due within the next year are classified as short-term liabilities.

Effect:

Understated short-term liabilities distorted NGWC's available working capital and short-term liquidity as of December 31, 2019, which could impact the water rates for NGWC's ratepayers during NGWC's GRC review process.

Recommendation:

NGWC should establish and implement procedures to ensure its liabilities are properly classified and reported in accordance with the accounting requirements of the USOA.

Finding 6: Misclassified Grant-Funded Water Plant in Service**Condition:**

NGWC misclassified \$169,687 of water plant funded with a local grant as utility-funded water plant. In addition, \$36,398 of related depreciation for the water plant funded by the local grant was recorded and reported as utility-funded water plant in the Annual Report originally filed with CPUC's Water Division on August 26, 2020. As a result, NGWC overstated Account 101-WPIS by \$169,687 and understated Account 101.2-Water Plant in Service-Grant Funds by the same amount. Additionally, NGWC overstated Account 108-Accumulated Depreciation of Water Plant by \$36,398 and understated Account 108.2-Accumulated Depreciation of Water Plant-Grant Funds Account 101.2 by the same amount. NGWC corrected these misstatements in its revised Annual Report submitted to the CPUC on June 8, 2021.

Criteria:

The USOA states, in part, that:

11. State and Federal Grant Funds

A. When Grant Funds are received from a funding agency; the utility must place these funds in a separate account that is restricted to Grant Funds only. The funds shall be recorded as a

debit to Account 132 – Cash- Special Deposits and a credit to Account 265.1 – Contributions in Aid of Construction -Government Grant Proceeds. As the grant-funded plant is being constructed, the utility shall record those dollars expended as a debit to Account 105.2 – Construction Work in Progress – Grant Funds and a credit to Account 132 – Cash – Special Deposits. When the authorized plant has been constructed, a second set of entries shall be recorded as a debit to Account 101.2 Utility Plant in Service – Grant Funds and a Credit to Account 105.2 – Construction Work in Progress – Grant Funds.

B. Depreciation accrued on the depreciable portion of grant funded properties shall be charged to Account 265.1 Contributions in Aid of Construction – Government Grant Funds instead of Account 403 – Depreciation Expense and credited to Account 108.2 – Accumulated Depreciation of Water Plant – Grant Funds.

Cause:

NGWC lacks monitoring procedures over its reporting process to ensure that grant-funded water plant is accurately accounted for and reported in the Annual Report.

Effect:

Misclassification of grant-funded water plant as utility-funded water plant in the Annual Report, which may be used during NGWC’s GRC application review process, could potentially impact the water rates for NGWC ratepayers.

Recommendation:

NGWC should establish and implement procedures to ensure the accurate reporting of grant-funded water plant in Account 101.2–WPIS–Grant Funds in accordance with the accounting requirements specified in the USOA.

Finding 7: Misclassified Contributions in Aid of Construction

Condition:

NGWC incorrectly recorded and reported \$101,625 of the collected but unspent Facilities Fees as Contributions in Aid of Construction (CIAC) in the Annual Report originally filed with CPUC’s Water Division on August 26, 2020. In addition, NGWC incorrectly recorded \$2,760 of Connection Fees collected from customers in 2018 for new meter installation as Other Water Revenues instead of recording the collections as CIAC. As a result, NGWC overstated Account 265–Contributions in Aid of Construction and Account 206–Subchapter S Corporation Accumulated Adjustments Account by \$98,685 (\$101,625 - \$2,760) and \$2,760, respectively; and understated Account 253–Other Credits by \$101,625. NGWC corrected these misstatements in its revised Annual Report submitted to the CPUC on June 8, 2021.

Criteria:

The USOA states, in part, that:

10. Facilities Fees

C. When facilities fees are received by a water utility, the amount received shall be deposited in Account 132 – Cash-Special deposits and credited to Account 253 – Deferred [sic. Other] Credits. Interest earned on these fees shall be debited to Account 132- Cash-Special Deposits and credited to Account 421 – Non-Utility Income.

D. At the time these fees are used for water plant improvements, Account 101 – Water Plant in Service shall be debited and Account 132 – Cash – Special Deposits credited. Concurrently, Account 253 Other Credits shall be debited and Account 265.7 – Contributions in Aid of Construction credited.

253. Other Credits

This account shall include advance billings, unamortized premium on debt, items in suspense and other credit items not provided for in other accounts. This account shall also include specific revenues (Revenue Balancing Account) that the Commission has authorized the utilities to record for future repayment.

Cause:

NGWC lacks monitoring procedures over its accounting and reporting process to ensure compliance with the accounting requirements specified in the USOA.

Effect:

Incorrectly recording unspent Facilities Fees as CIAC instead of deferred credits distorted NGWC's Balance Sheet and could misinform decision makers that these Facilities Fees had been spent for allowable purposes. Additionally, overstated CIAC and contributed water plant could lead to premature and excessive amortization of CIAC and contributed water plant, which could potentially impact decision makers during NGWC's GRC review process about the need for new water plant.

Recommendation:

NGWC should establish and implement monitoring procedures over its accounting and reporting process to ensure compliance with the accounting requirements specified in the USOA.

Finding 8: Misclassified Deferred Credits**Condition:**

NGWC misclassified \$46,016 of deferred credits related to its Conservation Lost Revenues Memorandum Account as Other Current Liabilities in the Annual Report originally filed with CPUC's Water Division on August 26, 2020. As a result, NGWC overstated Account 241–Other Current Liabilities by \$46,016, and understated Account 253–Other Credits by the same amount. NGWC corrected these misstatements in its revised Annual Report submitted to the CPUC on June 8, 2021.

Criteria:

The USOA states, in part, that:

14. Balancing Accounts

A. Balancing accounts are established only upon Commission authority and are recorded on a utility's accounting books as either a deferred charge (Account 180) or Other Credits (Account 253). A separate subaccount shall be maintained for each balancing account authorized by the Commission.

253. Other Credits

This account shall include advance billings, unamortized premium on debt, items in suspense and other credit items not provided for in other accounts. This account shall also include

specific revenues (Revenue Balancing Account) that the Commission has authorized the utilities to record for future repayment.

Cause:

NGWC lacks monitoring procedures over its accounting and reporting process to ensure compliance with the accounting requirements specified in the USOA.

Effect:

Inaccurate reporting of Other Current Liabilities (Account 241) and Other Credits (Account 253) distorted NGWC's financial position as of December 31, 2019, and overstated NGWC's available working capital, which could impact the water rates for NGWC's ratepayers during NGWC's GRC review process.

Recommendation:

NGWC should establish and implement monitoring procedures to ensure compliance with the accounting requirements specified in the USOA.

Finding 9: Misclassified Vacation and Sick Leave**Condition:**

NGWC misclassified expenses totaling \$26,037 for unused vacation and sick leave as employee salaries and wages expenses instead reporting it in Account 674—Employee Pension and Benefits in the Annual Report originally filed with CPUC's Water Division on August 26, 2020. As a result, NGWC overstated Account 630—Employee Labor, Account 670—Office Salaries, and Account 671—Management Salaries by \$2,245, \$11,455, and \$12,337, respectively; and understated Account 674—Employee Pension and Benefits by \$26,037. NGWC corrected these misstatements in its revised Annual Report submitted to the CPUC on June 8, 2021.

Criteria:

The USOA States, in part, that:

674. Employee Pensions and Benefits

This account shall include all accruals under employee pension plans to which the utility has irrevocably committed such funds and payments for employee accident, sickness, hospital and death benefits, or insurance therefore. Include also expenses for medical, educational or recreational activities of employees.

Cause:

NGWC lacks monitoring procedures over its accounting and reporting process to ensure compliance with the accounting requirements specified in the USOA.

Effect:

NGWC's misclassification of expenses reduces the comparability of its financial statements with other small water utilities. Consistent financial presentation among small water utilities aids decision makers in analyzing the performance and financial position of NGWC relative to the small water utility industry.

Recommendation:

NGWC should establish and implement monitoring procedures to ensure compliance with the accounting requirements specified in the USOA.

Finding 10: Incorrect Reversal of Prior Year Accounting Error**Condition:**

NGWC over-accrued \$20,175 interest expenses in Year 2018. To correct this prior over-accrual in its Annual Report originally filed with CPUC's Water Division on August 26, 2020, NGWC reduced \$20,175 in Account 427–Interest Expense instead of Account 206–Subchapter S Corporation Accumulated Adjustments Account. As a result, NGWC overstated Account 427–Interest Expense by \$20,175, and understated Account 206–Subchapter S Corporation Accumulated Adjustments Account by the same amount. NGWC corrected these misstatements in its revised Annual Report submitted to the CPUC on June 8, 2021.

Criteria:

The USOA states, in part, that:

206. Subchapter S Corporation Accumulated Adjustments Account

- A. This account shall be used by Subchapter S Corporations for the reporting of changes in its ownership equity.
- B. This account shall include all paid-in-capital not derived from earnings.
- C. This account shall be credited with:
 - 1. Net income.
 - 2. Accounting adjustments not properly attributable to the current period.
- D. This account shall be charged with:
 - 1. Net loss.
 - 2. Accounting adjustments not properly attributable to the current period.
 - 3. Dividends.

Cause:

NGWC lacks monitoring procedures over its accounting and reporting process to ensure compliance with the accounting requirements specified in the USOA.

Effect:

Inaccurate reporting of Interest Expense in the proper periods distorted NGWC's 2018 and 2019 net income and stockholders' equity, and reduced the comparability of NGWC's financial statements with other small water utilities. Consistent financial presentation among small water utilities aids decision makers in analyzing the performance and financial position of NGWC relative to the small water utility industry.

Recommendation:

NGWC should establish and implement monitoring procedures to ensure compliance with the accounting requirements specified in the USOA.

Finding 11: Incorrect Recording of CPUC Users Fee

NGWC recorded \$18,683 CPUC Users Fee collected from its customers and remitted to the CPUC as a pass-through activity instead of reporting them in the proper accounts as revenue and expenses. As a result, NGWC understated both Account 480—Other Water Revenue and Account—688 Regulatory Commission Expense by \$18,683. NGWC corrected these misstatements in its revised Annual Report submitted to the CPUC on June 8, 2021.

Criteria:

The USOA states, in part, that:

618. Regulatory Compliance Expense

A. This account shall include all expenses (except salaries of regular utility employees) incurred by the utility in connection with formal matters before regulatory commissions.

B. Amounts of regulatory commission expense which, by direction of the commission is to be spread over future periods shall be charged to Account 180, Deferred Charges and amortized by charges to Account 688, Regulatory Commission Expense.

480. Other Water Revenue

This account shall include revenue from water operations other than the delivery of water or provision of fire protection. This account shall be appropriately subdivided.

9. 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.

Cause:

NGWC stated it was not aware of the USOA requirement that CPUC Users Fee collected from its customers should be reported as Other Water Revenue and Users Fee remitted to the CPUC should be reported as Regulatory Commission Expense. NGWC lacks monitoring procedures over its accounting and reporting process to ensure compliance with the accounting requirements specified in the USOA.

Effect:

Inaccurate reporting of Other Water Revenue in Account 480 and Regulatory Commission Expense in Account 688 in the Annual Report, which may be used during NGWC's GRC application review process, could potentially impact the water rates for NGWC's ratepayers.

Recommendations:

Since UAB has provided an electronic copy of the USOA to NGWC on February 25, 2021, NGWC should follow the USOA accounting requirements to record and report CPUC Users Fee on a going forward basis. In addition, NGWC should establish and implement monitoring procedures to ensure compliance with the accounting requirements specified in the USOA.

Finding 12: Incorrect Reporting of Late Fees and Disconnection and Reconnection Fees**Condition:**

NGWC incorrectly recorded and reported \$6,180 of late fees and the \$3,820 of disconnection and reconnection fees in Account 421–Non-Utility Income in the Annual Report originally filed with CPUC’s Water Division on August 26, 2020. As a result, NGWC overstated Account 421–Non-Utility Income by \$10,000, and understated Account 480–Other Water Revenue by the same amount. NGWC corrected these misstatements in its revised Annual Report submitted to the CPUC on June 8, 2021.

Criteria:

The USOA states, in part, that:

421. Non-Utility Income

In this account is entered all income not includible in operating revenue accounts 460 through 480.

Items

- Interest income
- Dividend income
- Gross income from non-water utility operations
- Net gain on sale of non-water utility property

480. Other Water Revenue

This account shall include revenue from water operations other than the delivery of water or provision of fire protection. This account shall be appropriately subdivided.

Items

- Fees for changing, temporarily shutting off or reconnecting services
- Maintenance of appliances or repair of piping on customers’ premises
- Rental income from water property.

Cause:

NGWC’s accounting policy of recording late fees, disconnection fees, and reconnection fees does not comply with the USOA.

Effect:

Inaccurate reporting of Other Water Revenue and Non-Utility Income in the Annual Report, which may be used during NGWC’s GRC application review process, could potentially impact the water rates for NGWC’s ratepayers.

Recommendation:

NGWC should update its accounting policy to ensure that late fees, disconnection fees, and reconnection fees are recorded and reported in accordance with the accounting requirements specified in the USOA.

APPENDIX B—NGWC'S RESPONSE

NORTH GUALALA WATER COMPANY



July 27, 2021

State Of California
Public Utilities Commission
Attn: Mr Raymond Yin and Ms. Khusbindar Kaur
505 Van Ness Avenue
San Francisco CA 94102

Dear Mr. Yin and Ms. Kaur,

The North Gualala Water Company (NGWC) would like to thank the staff of the Utility Audits Branch (UAB) for all the assistance provided during the Commission's review of our company's 2019 Annual Report. While it is unfortunate that we had several conflicts in terms of timing, we really appreciate the UAB's patience and extremely helpful and understanding staff.

We have reviewed the July 2021 Draft Review of Financial Statements (Draft) provided to us and it appears that it is complete and accurately represents our discussions as well as what was found during the review.

As noted in the Draft, all identified issues were corrected by NGWC during the review process and a revised 2019 Annual Report was filed with the Commission. NGWC will follow the Commission's recommendations provided in the Draft to the best of our abilities. This will help NGWC assure the Commission can rely on future Annual Reports to be complete and correct.

Sincerely,

David D. Bower
President

Delivered Via Email