



California Public Utilities Commission
Division of Water and Audits

Financial Audit of
East Pasadena Water Company
Financial Statements
For the Years Ended December 31, 2011 and 2012

May 5, 2014



Acknowledgement

**The following Commission Staff contributed to the completion of this audit report:
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**Audit of Financial Statements of
East Pasadena Water Company
For the Years Ended December 31, 2011 and 2012**

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PUBLIC UTILITIES COMMISSION

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Independent Auditor's Report

The Utility Audit, Finance and Compliance Branch (UAFCB) of the California Public Utilities Commission (Commission) has audited the accompanying balance sheets of East Pasadena Water Company (EPWC) as of December 31, 2011 and 2012, and the related income statements, statements of retained earnings, and statements of cash flows for the years then ended. EPWC's management is responsible for:

1. Completeness and accuracy of the financial statements presented in the 2011 and 2012 annual reports filed with the Commission.
2. Conformity with accounting requirements of the Commission as set forth in the Uniform System of Accounts for Class B, C and D water utilities, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

The responsibility of the UAFCB is to express an opinion on EPWC's financial statements as a whole based on its audit.

The audit was conducted in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. Accordingly, the audit included examining, on a test basis, evidence concerning EPWC's compliance with the Commission's accounting and reporting requirements and performing such procedures as we considered necessary in the circumstances. The UAFCB believes that its audit provides a reasonable basis for an opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of East Pasadena Water Company as of December 31, 2011 and 2012, and the results of its operations and its cash flows for the years then ended, in compliance with the aforementioned accounting requirements.

The report is intended solely for the information and use by the Commission and EPWC. It should not be used by anyone other than the specified parties.

Bernard Ayanruoh, CPA
Program and Project Supervisor
Utility Audit, Finance and Compliance Branch

**Audit of Financial Statements of
East Pasadena Water Company
For the Years Ended December 31, 2011 and 2012**

Balance Sheets

	As of December 31 for the Year	
	2012	2011
ASSETS		
UTILITY PLANT		
Water Plant in Service (Note 1)	\$10,519,630	\$8,806,303
Construction Work in Progress - Water Plant	97,258	914,502
Accumulated Depreciation of Water Plant	<u>(5,132,538)</u>	<u>(4,814,837)</u>
Net Utility Plant	5,484,350	4,905,968
CURRENT AND ACCRUED ASSETS		
Cash	108,679	473,064
Accounts Receivable - Customers	298,560	294,748
Materials and Supplies	23,028	0
Other Current Assets (Note 2)	<u>240,852</u>	<u>103,831</u>
Total Current Assets	671,119	871,643
Deferred Charges (Note 1)	<u>10,018</u>	<u>27,335</u>
Total Assets	<u>\$6,165,487</u>	<u>\$5,804,946</u>
CATITALIZATION AND LIABILITIES		
CORPORATE CAPITAL AND SURPLUS		
Common Stock	338,751	338,751
Other Paid-in Capital	4	4
Retained Earnings	<u>2,637,761</u>	<u>2,515,457</u>
Total Corporate Capital and Retained Earnings	2,976,516	2,854,212
LONG-TERM DEBT		
Advances from Associated Companies (Note 3)	900,697	769,480
CURRENT AND ACCRUED LIABILITIES		
Accounts Payable	36,774	202,563
Short-term Notes Payable	0	250,000
Customer Deposits	11,596	11,799
Payables to Associated Companies (Note 5)	288,655	78,855
Taxes Accrued (Receivable)	(186,869)	(150,223)
Other Current Liabilities	<u>176,325</u>	<u>170,227</u>
Total Current and Accrued Liabilities	326,481	563,221
DEFERRED CREDITS		
Advances for Construction	4,130	4,405
Accumulated Deferred Investment Tax Credits	3,127	4,014
Accumulated Deferred Income Taxes - ACRS Depreciation	1,223,777	937,182
Accumulated Deferred Income Taxes - Other	<u>5,397</u>	<u>5,654</u>
Total Deferred Credits	1,236,431	951,255
CONTRIBUTIONS IN AID OF CONSTRUCTION		
Contributions In Aid of Construction (Note 4)	1,130,511	1,040,373
Accumulated Amortization of Contributions (Note 4)	<u>(405,149)</u>	<u>(373,595)</u>
Net Contributions In Aid of Construction	<u>725,362</u>	<u>666,778</u>
Total Capitalization and Liabilities	<u>\$6,165,487</u>	<u>\$5,804,946</u>

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

Income Statements

	For the Year of	
	2012	2011
OPERATING REVENUES		
Metered Water Revenue (Note 1)	\$2,318,615	\$2,050,033
Fire Protection Revenue	18,841	17,056
Other Water Revenue	<u>2,940</u>	<u>3,018</u>
Total Operating Revenues	2,340,396	2,070,107
OPERATING EXPENSES		
Plant Operation and Maintenance Expenses		
Purchased Water	126,897	370,220
Power	174,332	155,784
Other Volume Related Expenses	34,827	27,546
Employee Labor	249,123	253,317
Materials	59,844	52,995
Contract Work	91,539	73,222
Transportation Expenses	62,593	66,124
Other Plant Maintenance Expenses	<u>24,544</u>	<u>22,739</u>
Total Plant Operation and Maintenance Expense	823,699	1,021,947
Administrative and General Expenses		
Office Salaries	121,357	113,430
Management Salaries	286,741	280,786
Employee Pensions and Benefits	118,930	138,735
Uncollectible Accounts Expense/(Recovery)	(201)	5,831
Office Services and Rentals	55,065	50,956
Office Supplies and Expenses	39,149	39,726
Professional Services	59,672	79,639
Insurance	111,372	118,130
Regulatory Commission Expense	11,322	31,985
General Expenses	<u>49,890</u>	<u>57,593</u>
Total Administrative and General Expenses	853,297	916,811
Total Operating Expenses	1,676,996	1,938,758
Depreciation Expense (Note 1)	306,793	271,077
Taxes Other Than Income Taxes	85,888	81,134
State Corporate Income Tax Expense (Note 6)	27,070	(20,209)
Federal Corporate Income Tax Expense (Note 6)	<u>69,834</u>	<u>(57,005)</u>
Total Operating Revenue Deductions	2,166,581	2,213,755
Total Utility Operating Income/(Loss)	173,815	(143,648)
Non-Utility Income	(420)	(2,307)
Miscellaneous Non-Utility Expense	1,225	2,600
Interest Expense	<u>54,160</u>	<u>14,512</u>
Total Other Income and Deductions	54,965	14,805
Net Income/(Loss)	<u>\$118,850</u>	<u>(\$158,453)</u>

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

Statements of Retained Earnings

	For the Year of	
	2012	2011
Retained Earnings, Beginning of Year	\$2,515,457	\$2,678,316
CREDITS:		
Net Income	118,850	0
UAFCB Adjustment to Reinstate a Vehicle	1,500	0
UAFCB Adjustment to Professional Services	0	3,131
UAFCB Cumulative Adjustments to Beginning Balance (Footnote 1)	<u>7,848</u>	<u>0</u>
Total Credits	128,198	3,131
DEBITS:		
Net Loss	0	(158,453)
UAFCB Adjustment to Other Current Assets	(5,894)	(5,762)
EPWC Adjustment to Professional Services	<u>0</u>	<u>(1,775)</u>
Total Debits	(5,894)	(165,990)
Retained Earnings, End of Year	<u>\$2,637,761</u>	<u>\$2,515,457</u>

Statements of Retained Earnings Footnote:

(1) This amount represents the cumulative adjustments to the reported beginning balance of Retained Earnings as of January 1, 2012. Detailed computation is shown below:

Retained Earnings as of 01/01/2012 – As Reported	\$2,523,305
Retained Earnings as of 01/01/2012 – As Audited	<u>2,515,457</u>
Variance – UAFCB Cumulative Adjustments to Beginning Balance	<u><u>\$7,848</u></u>

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

Statements of Cash Flows

	For the Year of	
	2012	2011
CASH FLOW FROM OPERATING ACTIVITIES:		
Net Income/(Loss)	\$118,850	(\$158,453)
Adjustments to Reconcile Net Income to Cash Provided by Operating Activities		
Depreciation ¹	289,733	249,705
Decrease (Increase) in Accounts Receivable - Customers	(3,812)	(43,425)
Decrease (Increase) in Receivables from Associated Companies	0	19,798
Decrease (Increase) in Materials and Supplies	(23,028)	0
Decrease (Increase) in Other Current Assets	(137,021)	129,955
Decrease (Increase) in Deferred Charges	17,317	21,629
Increase (Decrease) in Accounts Payable	(165,789)	161,404
Increase (Decrease) in Short-term Notes Payable	(250,000)	250,000
Increase (Decrease) in Customer Deposits	(203)	(21,627)
Increase (Decrease) in Payable to Associated Companies	209,800	78,855
Decrease (Increase) in Taxes Accrued (Receivable)	(36,646)	(255,578)
Increase (Decrease) in Other Current Liabilities	6,098	13,641
Increase (Decrease) in Advances for Construction	(275)	(275)
Increase (Decrease) in Accumulated Deferred Investment Tax Credits	(887)	(888)
Increase (Decrease) in Deferred Income Taxes - ACRS Depreciation	286,595	60,368
Increase (Decrease) in Deferred Income Taxes - Other	(257)	(257)
Net Cash Provided by Operating Activities	<u>310,475</u>	<u>504,852</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net Plant Additions	(1,713,327)	(322,672)
Increase (Decrease) in Construction Work in Progress –Water Plant	817,244	(827,326)
Increase (Decrease) in Contributions In Aid of Construction	90,138	25,366
UAFCB Cumulative Adjustments to retained Earnings ²	(132)	(4,406)
Net Cash Used for Investing Activities	<u>(806,077)</u>	<u>(1,129,038)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Increase (Decrease) in Long-term Debt	<u>131,217</u>	<u>627,662</u>
Net Cash Used for Financing Activities	<u>131,217</u>	<u>627,662</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(364,385)	3,476
CASH AT BEGINNING OF YEAR	<u>473,064</u>	<u>469,588</u>
CASH AT END OF YEAR	<u>\$108,679</u>	<u>\$473,064</u>

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

¹ For Statements of Cash Flows purpose, UAFCB excluded \$21,372 and \$17,060 amortization of property losses from the depreciation expense for Years 2011 and 2012, respectively.

² For Year 2011, the total UAFCB debit adjustment of \$4,406 to Retained Earnings was presented in the 2011 Summary of Audit Adjustments. For Year 2012, the total UAFCB debit adjustment of \$132 to Retained Earnings represented the cumulative effect of UAFCB's adjustments to the Retained Earnings for Years 2011 and 2012.

Notes to Financial Statements

(1) Summary of Significant Accounting Policies

East Pasadena Water Company (EPWC) is a wholly owned subsidiary of California-Michigan Land and Water Company (Cal-Mich) which was incorporated in the State of California on December 23, 1910. Initially, Cal-Mich operated as a real estate company but was later incorporated as a public water utility in 1913. In 1963, Cal-Mich sold its water system and properties to EPWC with authorization from the California Public Utilities Commission (Commission). EPWC is a class B water utility serving about 2,952 customers in Southern California communities including Arcadia, San Gabriel, Temple City, Pasadena and Los Angeles County.

EPWC has prepared the accompanying Balance Sheets, Income Statements, and Statements of Retained Earnings on the basis of accounting set forth in the Uniform System of Accounts for Class B, C, and D 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 operating expenses, revenues, depreciation, and amortization related to prior years are 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 income statements. The Statement of Retained Earnings and the Statement of Cash Flows were not required by the Commission when EPWC filed its annual reports with the Commission. Therefore, the accompanying Statements of Cash Flows were compiled by the UAFCB based on the financial information in EPWC's Balance Sheets, Income Statements, and Statements of Retained Earnings.

(a) Utility Plant

Utility plant is recorded at original cost when it is first constructed or purchased. Retired utility plants were removed from utility plant accounts at cost and charged against accumulated depreciation.

(b) Depreciation

Depreciation is computed on a straight-line composite rate of 2.907 % to depreciate all of its plant assets for ratemaking purpose and for reporting the depreciation expense in its Annual Reports filed with the Commission.

(c) Deferred Charges

Deferred Charges consisted primarily of deferred amortizable systems study and General Rate Case (GRC) fees, and tax accruals prepared in accordance with SFAS No.109.

(d) Revenues

All EPWC's customers are metered, with residential customers billed bimonthly and commercial customers billed monthly. EPWC's water revenues were billed based on tariffs approved by the Commission.

(2) Other Current Assets

Other Current Assets consisted primarily of prepayments for insurance, property taxes, Raymond Basin water master administrative fees, and San Gabriel Basin assessment prescriptive pumping rights.

(3) Long-term Debts

As of December 31, 2012 EPWC has the following Long-term Debts:

Description	Outstanding Balance As of December 31, 2012
Notes Payable – Cal-Mich (a)	\$75,148
Notes Payable – Cal-Mich (b)	<u>825,549</u>
Total Long-term Debt	<u>\$900,697</u>

All outstanding long-term debts were directly obtained from a related party, Cal-Mich, which is EPWC’s parent company.

(a) Note Payable \$75,148

This long-term debt was authorized by the Commission Decision (D.)96-10-017 on October 9, 1996, for \$300,000 to enable EPWC complete the construction of water reservoirs. The initial repayment terms were not specified and only interest payments were made between 1996 and 2004. In 2005 Cal-Mich issued a formal promissory note to EPWC which stipulated a repayment period of 10 years from January 1, 2005, through January 1, 2015, with an initial annual interest rate of 6% subject to annual rate adjustments.

(b) Note Payable \$825,549

This long-term debt was authorized by the Commission D.12-03-009 on March 8, 2012, for \$900,000 to enable EPWC construct a well for continuous water supply. The term of this note is 10 years from October 1, 2011, through August 30, 2021, with interest rates being Prime Rate announced in the Wall Street Journal’s Western edition plus 2%. Interest rates are restricted to a minimum of 5.25% and a maximum of 10%, or as allowed by law.

(4) Contributions In Aid of Construction (CIAC) and Accumulated Amortization of Contributions

CIAC represents nonrefundable contributions of cash or property received from various parties for purposes of constructing additions to utility plant. Depreciation applicable to such contributed plant is charged against the CIAC account rather than to depreciation expense until the amount applicable to such properties has been completely amortized. In both 2011 and 2012, EPWC used an amortization rate of 2.907% determined in the test year of its 2009 GRC as the basis to amortize the Contributions.

(5) Receivables from and Payables to Associated Companies

EPWC maintains a schedule of intercompany receivables and payables between itself and Cal-Mich to track the net result at the end of every year. The main components of this schedule includes tax provisions, Cal-Mich’s payments to the banks for EPWC’s line of credit, fund transfers between companies, and employee payroll transactions related to bonuses. The ending

balances were used to determine either a receivable or payable between the two entities. For 2011 and 2012, the schedule indicated a payable to Cal-Mich of \$78,855 and \$288,655, respectively.

(6) Income Taxes

In 2012, EPWC paid \$69,834 and \$27,070 federal and State income taxes, respectively. In 2011, EPWC did not pay any federal or State income taxes because of the tax credits carried over from prior years.

(7) Annual Reports

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