



California Public Utilities Commission
Utility Audit, Finance and Compliance Branch

Financial Audit of
Searles Domestic Water Company
Financial Statements
For the Years Ended December 31, 2015 and 2014

September 5, 2017



Acknowledgement

**The following Commission Staff contributed to the completion of this audit report:
Kayode Kajopaiye, Raymond Yin and Khai Duong**

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Searles Domestic Water Company
For the Years Ended December 31, 2015 and 2014**

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PUBLIC UTILITIES COMMISSION

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Report of Independent Auditors

Avinash Puri, President
Searles Valley Minerals Inc.
9401 Indian Creek Pkwy, Suite 1000
Overland Park, KS 66210

Report on the Financial Statements

The Utility Audit, Finance and Compliance Branch (UAFCB) of the California Public Utilities Commission (Commission) has audited the accompanying financial statements of Searles Domestic Water Company (SDWC), which are comprised of the balance sheets as of December 31, 2015 and 2014, and the related statements of income, retained earnings for the years then ended, and the related notes to the financial statements. The statement of cash flows is not presented in this report due to lack of sufficient verifiable financial data.

Management's Responsibility for the Financial Statements

SDWC's management is responsible for the preparation and fair presentation of the financial statements presented in the 2015 and 2014 annual reports filed with the Commission. The Commission requires that the statements be in accordance with the accounting requirements of the Commission as set forth in the Uniform System of Accounts (USOA) for Water Utilities, as described in Note 1 to 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 SDWC's financial statements based on our audits. 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.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the

entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant estimates made by management, as well as evaluating the overall presentation of the financial statements.

Basis of Disclaimer of Opinion

Management was unable to provide appropriate supporting documentation for the Cash, Retained Earnings as of December 31, 2015 and 2014, and the Payables to Associated Companies balances. We were unable to satisfy ourselves by alternative means concerning the above accounts and as a result were unable to determine if any adjustments might have been necessary in respect of these accounts.

Disclaimer of Opinion

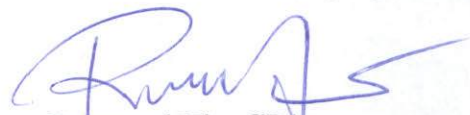
Because of the significance of the matters described in the Basis for Disclaimer of Opinion paragraph, we were not able to obtain sufficient appropriate evidence to provide a basis for our opinion. Accordingly, we do not express an opinion on the financial statements as presented.

Basis of Accounting

We draw attention to Note 1 of the financial statements, which describes the basis of accounting. The financial statements of SDWC were originally prepared on an accrual basis of accounting as required by the USOA or Generally Accepted Accounting Principles (GAAP) but are not in total compliance with the approved reporting standards. SDWC did not write off certain obsolete assets and unused equipment thus misstating Water Plant in Service. The corrections on the reported financial statements were achieved via audit adjustments by the UAFCB.

Use of Report

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



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

**Audit of Financial Statements of
Searles Domestic Water Company
For the Years Ended December 31, 2015 and 2014**

Balance Sheets

	As of December 31 for the Year	
	2015	2014
ASSETS		
UTILITY PLANT		
Water Plant in Service (Note 1)	\$2,627,852	\$2,541,312
Water Plant Construction Work in Progress	0	52,382
Accumulated Depreciation of Water Plant (Note 1)	<u>(1,422,475)</u>	<u>(1,367,688)</u>
Net Utility Plant	1,205,377	1,226,006
CURRENT AND ACCRUED ASSETS		
Cash (Note 1)	250	250
Accounts Receivable – Customers (Note 1)	49,209	43,358
Receivables from Associated Companies (Note 2)	285,474	281,267
Material and Supplies	116,954	106,639
Other Current Assets (Note 1)	<u>6,593</u>	<u>6,959</u>
Total Current and Accrued Assets	458,480	438,473
Total Assets	<u>\$1,663,857</u>	<u>\$1,664,479</u>
CAPITALIZATION AND LIABILITIES		
CORPORATE CAPITAL AND SURPLUS		
Other Paid in Capital	1,317,978	1,303,974
Retained Earnings (Note 3)	<u>323,280</u>	<u>338,307</u>
Total Capitalization	1,641,258	1,642,281
CURRENT AND ACCRUED LIABILITIES		
Customer Deposits	19,087	17,881
Accrued Taxes	<u>3,409</u>	<u>3,634</u>
Total Current and Accrued Liabilities	22,496	21,515
CONTRIBUTIONS IN AID OF CONSTRUCTION		
Contributions in Aid of Construction	18,982	18,982
Accumulated Amortization of Contributions	<u>(18,879)</u>	<u>(18,299)</u>
Net Contributions in Aid of Construction	103	683
Total Capitalization and Liabilities	<u>\$1,663,857</u>	<u>\$1,664,479</u>

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

Income Statements

	For the Year of	
	2015	2014
OPERATING REVENUES		
Metered Water Revenue	\$551,880	\$586,234
Public Fire Protection Revenue	2,375	2,375
Other Water Revenue	<u>30,575</u>	<u>29,268</u>
Total Operating Revenues (Note 1)	584,830	617,877
OPERATING EXPENSES		
Plant Operation and Maintenance Expenses		
Purchased Water	75,245	82,154
Employee Labor	146,543	126,537
Materials	59,035	37,572
Contract Work	15,502	14,474
Transportation Expenses	<u>16,462</u>	<u>35,983</u>
Total Plant Operation and Maintenance Expense	312,787	296,720
Administrative and General Expenses		
Office Salaries	37,060	34,306
Management Salaries	47,932	44,535
Employee Pensions and Benefits	55,795	53,805
Uncollectible Accounts Expenses	1,391	5,647
Office Supplies and Expenses	14,838	17,215
Professional Services	2,600	4,089
Insurance	7,283	8,760
Regulatory Commission Expense	8,851	8,778
General Expenses	9,417	9,599
Expenses Capitalized	<u>(21,406)</u>	<u>(34,611)</u>
Total Administrative and General Expenses	<u>163,761</u>	<u>152,123</u>
Total Operating Expenses	476,548	448,843
Depreciation Expense (Note 1)	72,860	63,228
Taxes Other Than Income Taxes	33,244	32,414
State Corporate Income Tax Expense	<u>0</u>	<u>0</u>
Total Operating Revenue Deductions	582,652	544,485
Total Utility Operating Income	2,178	73,392
Interest Expense	<u>(310)</u>	<u>(449)</u>
Total Other Income and Deductions	(310)	(449)
Net Income	<u>\$1,868</u>	<u>\$72,943</u>

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

Statements of Retained Earnings

	For the Year of	
	2015	2014
Retained Earnings, Beginning of Year	\$338,307	\$254,035
CREDITS:		
UAFCB Audit Adjustment to Advances for Construction	0	13,576
UAFCB Audit Adjustment to Accrued Taxes	4,221	3,578
Net Income`	1,868	72,943
Total Credits	6,089	90,097
DEBITS:		
UAFCB Cumulative Adjustment to Beginning Balance ¹	(14,004)	0
UAFCB Adjustment to Other Current Assets	(7,112)	(5,825)
Total Debits	(21,116)	(5,825)
 Retained Earnings, End of Year	 \$323,280	 \$338,307

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

¹ This amount represents the cumulative adjustments to the reported beginning balance of Retained Earnings as of January 1, 2015. Detailed computation is shown below:

Retained Earnings as of 12/31/2014 – As Audited	\$338,307
Retained Earnings as of 12/31/2014 – As Reported	324,303
Variance – UAFCB Cumulative Adjustment to Beginning Balance	<u>\$ 14,004</u>

Statements of Cash Flows

The Statement of Cash Flows has not been prepared since all SDWC cash activities were handled by Searles Valley Minerals Inc. (SVM) in an SVM cash account. Funds of both companies were commingled during the audit period.

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

Notes to Financial Statements

(1) Summary of Significant Accounting Policies

Searles Domestic Water Company (SDWC) is a Class C water utility that provides water service to approximately 810 customers within the unincorporated communities of Argus, Trona, Pioneer Point, Borosivay and South Trona, all within San Bernadino County. The customers are primarily year- round residents and include 807 metered as well as 3 flat rate accounts. The SDWC system is supplied from parent company Searles Valley Minerals Inc. (SVM).

The financial statements of SDWC were originally prepared on an accrual basis of accounting as required by the Uniform System of Accounts (USOA) or Generally Accepted Accounting Principles (GAAP). The Statements of Retained Earnings and Statements of Cash Flows are not required by the Commission when SDWC files its Annual Reports with the Commission. Therefore, the accompanying Statements of Retained Earnings were compiled by UAFCB based on the audited financial information of SDWC's Balance Sheets and Income Statements. The Statements of Cash Flows were not prepared due to the fact that SDWC did not have a bank account and all its cash transactions were commingled and handled by its parent's Searles Valley Minerals Bank of America checking account.

(a) Appendices

The accompanying Appendices are an integral part of the financial statements. Appendix A and Appendix B present the net financial impact resulting from UAFCB's audit adjustments for Years 2015 and 2014, respectively. Appendix C and Appendix D summarize the detail UAFCB audit adjustments for Years 2015 and 2014, respectively.

(b) Water Plant in Service

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

SDWC did not write off some of its out- of- service assets and its plant's reporting is not in total compliance with USOA requirements. Therefore, UAFCB made audit adjustments to correctly state Water Plant in Service.

(c) Current Assets

Cash was not reported in compliance with USOA. Accounts Receivable – Customers and Other Current Assets were overstated. Since all cash transactions are co-mingled with SVM cash and recorded in an intercompany account (Note 2), UAFCB could not verify SDWC's portion and consequently does not express an opinion on this account. UAFCB has made audit adjustments to correct the reported Accounts Receivable and Other Current Assets balances based on available and verifiable information from SDWC.

(d) Depreciation of Water Plant

Depreciation is computed using a straight-line composite rate of 2.7% (equivalent to depreciating the plant assets over approximately 37 years) to depreciate all of its plant assets for ratemaking purpose and for reporting the depreciation expense in its Annual Reports filed with the Commission.

(e) Revenues

SDWC revenues are obtained from metered service to its customers on an annual basis. In addition, a small portion of SDWC revenue is from flat rate. SDWC computed its water revenues based on tariffs approved by the Commission.

(f) Interest Expense

SDWC pays 7% on the amount of customer deposits refunded each year. The 7% rate has been approved by the Commission.

(2) Payables to / Receivables from Associated Companies

In its 2014 and 2015 annual reports, SDWC reported for Payables to Associated Companies (USOA Account 235) net debit balances of (\$204,355) and (\$204,754), respectively. The audited balances were (\$281,267) in 2014 and (\$285,474) in 2015. The Payables to Associated Companies carries the net balance of customer billing collections deposited into the Searles Valley Minerals (SVM) bank account and various charges from SVM to SDWC during each reporting period. UAFCB reclassified the net debit balances in this account to Receivables from Associated Companies to comply with USOA.

SDWC did not have its own cash account during the audit period. SDWC deposited all cash receipts into SVM's bank account. SVM recorded a debit to its Cash and a credit to its intercompany account when cash was received for SDWC. SDWC recorded a debit entry to its "Payable to Associated Companies" and posted a credit to Accounts Receivable recording revenue collections. The same approach was used for all charges and expenses paid by SVM on behalf of SDWC. These transactions would also be recorded by SDWC as a credit entry to Payables to Associated Companies and as a debit entry to expenses.

SDWC did not provide adequate, verifiable supporting documentation for the "Payables to Associated Companies" account beginning balances. As a result, UAFCB was unable to verify the accuracy of these reported Payables to Associated Companies amounts. Therefore, UAFCB does not express an opinion on these reported account balances.

(3) Retained Earnings

SDWC did not provide adequate, verifiable supporting documentation for the beginning balances. As a result, UAFCB was unable to verify the accuracy of these reported amounts. Therefore, UAFCB does not express an opinion on them.

(4) Annual Reports

Per California Public Utilities Code, Sections 581, 582, and 584, SDWC is required to file an annual report with the Commission every year. However, SDWC did not properly file Schedule A in its 2015 Annual Report. Specifically, SDWC incorrectly inputted the ending balances as of December 31, 2015 in Column "d" of Schedule A. SDWC should have input those financial data in Column "c" of that schedule because Column "d" is reserved for inputting the ending balances as of December 31, 2014, which are missing in that schedule.

SDWC, in spite of significant business activities with Searles Valley Minerals an affiliated company, is not required to file an Affiliate Transaction Report with the Commission and comply with the Affiliate Transaction Rules, as adopted by D.10-10-019.

Appendix A

Summary of Net Financial Impact Resulting from UAFCB's Audit Adjustments for Year 2015

The following is a summary of net financial impact resulting from UAFCB's audit adjustments for Year 2015.

Audit Adj. No.	Annual Report				Description	For the Year 2015	
	Sch.	Line	Col.	Acct No.		Debit	Credit
<u>Net Financial Impact on Balance Sheets Items:</u>							
1	A	2	c	101	Water Plant in Service		\$17,765
1	A	11	c	108	Accumulated Depreciation of Water Plant	\$17,765	
2	A	30	c	141	Accounts Receivable - Customers		8,430
7	A	31	c	142	Receivables from Associated Companies	285,474	
3	A	34	c	174	Other Current Assets		7,112
8	A	43	c	211	Other Paid-in-Capital		71,999
3,4,5,6	A	44	c	215	Retained Earnings		11,113
2,6,7,8	A	60	c	235	Payables to Associated Companies		204,754
5	A	61	c	236	Accrued Taxes	4,221	
4	A	67	c	252	Advances for Construction	13,576	
<u>Net Financial Impact on Income Statements Items:</u>							
2	B-2	15	b	676	Uncollectible Accounts Expenses	\$137	

Appendix B

Summary of Net Financial Impact Resulting from UAFCB's Audit Adjustments for Year 2014

The following is a summary of net financial impact resulting from UAFCB's audit adjustments for Year 2014.

Audit Adj. No.	Annual Report				Description	For the Year 2014	
	Sch.	Line	Col	Acct No.		Debit	Credit
<u>Net Financial Impact on Balance Sheets Items:</u>							
1	A	30	c	141	Accounts Receivable - Customers		\$2,238
4	A	31	c	142	Receivables from Associated Companies	\$281,267	
2	A	34	c	174	Other Current Assets		5,825
7	A	43	c	211	Other Paid-in-Capital		71,999
2,3,5	A	44	c	215	Retained Earnings		11,329
1,4,6,7	A	60	c	235	Payables to Associated Companies		204,355
5	A	61	c	236	Accrued Taxes	3,578	
3	A	67	c	252	Advances for Construction	13,576	
<u>Net Financial Impact on Income Statement Items:</u>							
6	B	5	c	408	Federal Insurance Contribution Act		\$2,675

Appendix C

Summary of Audit Adjustments for Year 2015

Audit Adj. No.	Annual Report				Description	Debit	Credit
	Sch.	Line	Col.	Acct No.			
1	A	11	c	108	Accumulated Depreciation of Water Plant	\$17,765	
	A	2	c	101	Water Plant in Service		\$17,765
<i>To correctly report Water Plant in Service and Accumulated Depreciation of Water Plant.</i>							
2	B-2	15	b	676	Uncollectible Accounts Expense	\$137	
	A	60	c	235	Payables to Associated Companies	8,293	
	A	30	c	141	Accounts Receivables – Customers		\$8,430
<i>To correctly record Accounts Receivable – Customers.</i>							
3	A	44	c	215	Retained Earnings	\$7,112	
	A	34	c	174	Other Current Assets		\$7,112
<i>To correctly report Accounts Receivable - Customers.</i>							
4	A	67	c	252	Advances for Construction	\$13,576	
	A	44	c	215	Retained Earnings		\$13,576
<i>To correctly report Advances for Construction and Retained Earnings.</i>							
5	A	67	c	236	Accrued Taxes	\$4,221	
	A	44	c	215	Retained Earnings		\$4,221
<i>To correctly report Accrued Taxes.</i>							

Summary of Audit Adjustments for Year 2015

Audit Adj. No.	Annual Report				Description	Debit	Credit
	Sch.	Line	Col.	Acct No.			
6	A	60	c	235	Payables to Associated Companies	\$428	
	A	44	c	215	Retained Earnings		\$428
<i>To correctly state Beginning Retained Earnings and Payables to Associated Companies.</i>							
7	A	31	c	142	Receivables from Associated Companies	\$285,474	
	A	60	c	235	Payables to Associated Companies		\$285,474
<i>To correctly report intercompany accounts.</i>							
8	A	60	c	235	Payables to Associated Companies	\$71,999	
	A	43	c	211	Other Paid-in-Capital		\$71,999
<i>To correctly report intercompany accounts.</i>							

Appendix D

Summary of Audit Adjustments for Year 2014

Audit Adj. No.	Annual Report				Description	Debit	Credit
	Sch.	Line	Col.	Acct No.			
1	A	60	c	235	Payables to Associated Companies	\$2,238	
	A	30	c	141	Accounts Receivable - Customers <i>To correctly report Accounts Receivable - Customers.</i>		\$2,238
2	A	44	c	215	Retained Earnings	\$5,825	
	A	34	c	174	Other Current Assets <i>To correctly report Other Current Assets.</i>		\$5,825
3	A	67	c	252	Advances for Construction	\$13,576	
	A	44	c	215	Retained Earnings <i>To correctly report Advances for Construction.</i>		\$13,576
4	A	31	c	142	Receivables from Associated Companies	\$281,267	
	A	60	c	235	Payables to Associated Companies <i>To correctly state Intercompany accounts.</i>		\$281,267
5	A	61	c	236	Accrued Taxes	\$3,578	
	A	44	c	215	Retained Earnings <i>To correctly report Other Paid-in Capital.</i>		\$3,578
6	A	60	c	235	Payables to Associated Companies	\$2,675	
	B	5	c	408	Federal Insurance Contribution Act <i>To correctly report FICA taxes.</i>		\$2,675
7	A	60	c	235	Payables to Associated Companies	\$71,999	
	A	43	c	211	Other Paid-in-Capital <i>To correctly report Intercompany accounts</i>		\$71,999