



Financial Audit of Canada Woods Water Company-Sewer

Financial Statements

For Year Ended December 31, 2018

Utility Audit, Finance and Compliance Branch
October 31, 2019



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Thanks to:
Angie Williams, Raymond Yin, Sharmin Wellington, and Aaron Louie

**Audit of Financial Statements of
Canada Woods Water Company - Sewer
For the Year Ended December 31, 2018**

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PUBLIC UTILITIES COMMISSION

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Report of Independent Auditors

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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 Canada Woods Water Company (CWWC), which are comprised of the balance sheet as of December 31, 2018, and the related statements of income, proprietary capital, and cash flows for the year then ended, and the related notes to the financial statements.

Management’s Responsibility for the Financial Statements

CWWC’s management is responsible for the preparation and fair presentation of the financial statements presented in the 2018 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 in the Notes to the Financial Statements attached herein. Management is also responsible for the design, implementation, and maintenance of internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error.

Auditor’s Responsibility

The responsibility of the UAFCB is to express an opinion on CWWC’s financial statements based on our 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 from 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.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Basis for Qualified Opinion

Due to the lack of supporting documentation and historical information on the reported Proprietary Capital as described in Note 1(e) to the Audited Financial Statements, UAFCB could not attest to these balances as of December 31, 2018. Therefore, UAFCB does not express an opinion on the balances of Proprietary Capital as of December 31, 2018.

Qualified Opinion

In our opinion, except for the balances of Proprietary Capital as described in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of Canada Woods Water Company as of December 31, 2018, and the results of its operations and its cash flows for the year then ended, in accordance with the accounting requirements of the Commission as set forth in the USOA for Water Utilities, described in Note 1.

Basis of Accounting

We draw attention to Note 1 of the financial statements, which describes the basis of accounting. The financial statements of CWWC were originally prepared on the basis of the accounting requirements of the California Public Utilities Commission as set forth in the USOA for Water Utilities, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Use of Report

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

Raymond Yin

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

Balance Sheets

	As of December 31, for the Year	
	2018	2017¹
ASSETS		
UTILITY PLANT		
Sewer Plant in Service (Note 1)	\$4,396,945	\$4,396,945
Construction Work in Progress	1,783	1,783
Accumulated Depreciation of Sewer Plant (Note 1)	(2,347,073)	(2,203,521)
Net Utility Plant	\$2,051,655	\$2,195,207
CURRENT AND ACCRUED ASSETS		
Cash	21,378	0
Deferred Charges	2,372	0
Total Current and Accrued Assets	23,750	0
Total Assets	\$2,075,405	\$2,195,207
CAPITALIZATION AND LIABILITIES		
CORPORATE CAPITAL AND SURPLUS		
Proprietary Capital (Note 1)	\$407,746	\$432,270
Total Capitalization	407,746	432,270
CURRENT AND ACCRUED LIABILITIES		
Payables to Affiliated Companies	3,558	0
Accounts Payable	6,246	10,185
Net Current and Accrued Liabilities	9,804	10,185
CONTRIBUTIONS IN AID OF CONSTRUCTION		
Contributions in Aid of Construction (Note 1)	3,327,723	3,327,723
Accumulated Amortization of Contributions (Note 1)	(1,669,868)	(1,574,971)
Net Contributions in Aid of Construction	1,657,855	1,752,752
Total Capitalization and Liabilities	\$2,075,405	\$2,195,207

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

¹ The amounts for the year ended December 31, 2017, were reported by CWWC. These amounts have not been audited by UAFCB.

Income Statements

	For the Year of	
	2018	2017 ²
OPERATING REVENUES		
Unmetered Revenue	\$247,058	\$207,906
Other Sewer Revenue	3,459	0
Total Operating Revenues (Note 1)	250,517	207,906
OPERATING EXPENSES		
Plant Operation and Maintenance Expenses		
Power	19,902	18,622
Other Volume Related Expense	133,593	82,309
Employee Labor	0	127,263
Materials	2,666	9,846
Contract Work	222,273	0
Total Plant Operation and Maintenance Expense	378,434	238,040
Administrative and General Expenses		
Office Salaries	0	16,536
Management Salaries	0	43,842
Office Supplies and Expenses	6,334	0
Regulatory Commission Expense	4,645	0
General Expenses	0	7,111
Total Administrative and General Expenses	10,979	67,489
Total Operating Expenses	389,413	305,529
Depreciation Expense (Note 1)	48,656	48,656
Total Operating Revenue Deductions	438,069	354,185
Total Utility Operating Income (Loss)	(187,552)	(146,279)
Net Income	(\$187,552)	(\$146,279)

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

² The amounts for the year ended December 31, 2017, were reported by CWWC. These amounts have not been audited by UAFCB.

Statements of Proprietary Capital

	For the Year of	
	2018 ³	2017 ⁴
Proprietary Capital, Beginning of Year	\$432,270	\$474,536
CREDITS:		
Additional Investments during the year – As reported	156,512	104,013
UAFCB Adjustment to Receivables from Affiliated Companies	21,378	0
2018 Annual Report reflected a reporting error ⁵	10,185	0
Total Credits	188,075	104,013
DEBITS:		
UAFCB Adjustment to Regulatory Commission Expense	(25,047)	
Net Loss	(189,552)	(146,279)
Total Debits	(212,559)	(146,279)
Proprietary Capital, End of Year	\$407,746	\$432,270

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

³ The Proprietary Capital balances were not audited but were the results of UAFCB compiled audit adjustments and Net Income (Loss) for 2018. UAFCB could not attest to the accuracy of the Proprietary Capital balances due to lack of historical information on the account.

⁴ The amounts for the year ended December 31, 2017, were reported by CWWC. These amounts have not been audited by UAFCB.

⁵CWWC reported on its 2017 Annual Report an ending balance of \$432,270 for Proprietary Capital; however, Schedule A-9 of the 2018 Annual Report reported a beginning balance of Proprietary Capital of \$442,455. This resulted in a variance, or a reporting error, of \$10,185 (\$442,455 - \$432,270).

Statements of Cash Flows

	For the Year of	
	2018	2017 ⁶
CASH FLOW FROM OPERATING ACTIVITIES:		
Net Income (Loss)	(\$187,552)	(\$146,279)
Adjustments to Reconcile Net Income to Cash		
Provided by Operating Activities		
Depreciation and Amortization	143,552	143,552
Decrease (Increase) in Deferred Charges	(2,372)	0
Increase (Decrease) in Payables to Affiliated Companies	3,558	0
Increase (Decrease) in Accounts Payables	(3,939)	(6,393)
Net Cash Provided by Operating Activities	<u>(46,753)</u>	<u>(9,120)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Decrease (Increase) in Accumulated Amortization of Contributions	(94,897)	(94,893)
UAFCB Cumulative Adjustment to Proprietary Capital ⁷	(3,669)	0
As Reported Increase (Decrease) Proprietary Capital ⁸	156,512	104,013
2018 Annual Report reflected a reporting error ⁹	10,185	0
Net Cash Used for Investing Activities	<u>68,131</u>	<u>9,120</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net Cash used for Financing Activities	<u>0</u>	<u>0</u>
Net Cash Used for Financing Activities	0	0
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	21,378	0
CASH AT BEGINNING OF YEAR	<u>0</u>	<u>0</u>
CASH AT END OF YEAR	<u><u>\$21,378</u></u>	<u><u>\$0</u></u>

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

⁶ The amounts for the year ended December 31, 2017, were reported by CWWC. These amounts have not been audited by UAFCB.

⁷ For Year 2018, the total UAFCB debit adjustment of (\$3,669) to Proprietary Capital represented the cumulative effect of UAFCB's adjustment to the Proprietary Capital for Year 2018.

⁸ For the purpose of the Statements of Cash Flows, UAFCB included CWWC's reported Additional Investment during the Year of \$156,512 and \$104,013 in Schedule A-9 of the Annual Reports for the Years 2018 and 2017, respectively.

⁹ CWWC reported on its 2017 Annual Report an ending balance of \$432,270 for Proprietary Capital; however, Schedule A-9 of the 2018 Annual Report reported a beginning balance of Proprietary Capital of \$442,455. This resulted in a variance, or a reporting error, of \$10,185 (\$442,455 - \$432,270).

Notes to Financial Statements

(1) Summary of Significant Accounting Policies

Canada Woods Water Company (CWWC) provides sewer services; which involves emptying their customers' septic tank on a monthly basis for their 147 unmetered customers in its service territory around the Carmel area. CWWC was incorporated in the state of Delaware as a single member Limited Liability Company. CWWC contracts with Carmel Lahaina Utility Services, Inc. (CLUS) to manage the utility. As a sewer utility, CWWC must comply and adhere to the Commission's USOA for Class A, B, C, and D water and sewer utilities.

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

The Statements of Cash Flows are not required by the Commission when CWWC files its Annual Reports with the Commission. Therefore, the accompanying Statements of Cash Flows were compiled by UAFCB based on the audited financial information of CWWC Balance Sheets and Income Statements.

CWWC provides water, reclaimed water, and sewer services to its customers. Activities related to those services were separately identifiable in CWWC's general ledger. However, for purposes of reporting to the CPUC, the water and reclaimed water were grouped together and reported in the water annual reports, while the sewer operations were reported in the sewer annual reports. CWWC directly allocated water and sewer revenue to the water and sewer operations based on their respective actual billings. CWWC billed the water and reclaimed water services based on the usage at tariff rates approved by the CPUC, while CWWC billed the sewer services at the CPUC-approved flat rates based on the size of each home's sewage tank. CWWC's methodology for allocating expenses between water and sewer operations are directly associated with each utility's transaction meaning if the expense is clear and identifiable it is allocated to the appropriate function water or sewer. However, if the expense or overhead is not identifiable to a specific utility, the methodology for allocating the expense is approximately 70% to water operations (60% to water and 10% to reclaimed water) and 30% to sewer operations. CWWC acknowledges allocating most of the expenses to the water function as it is the biggest of the three functions of the utilities and requires the most work.

(a) Appendices

The accompanying Appendices are an integral part of the financial statements. Appendix A presents the net financial impact resulting from UAFCB's audit adjustments for the year ended 2018. Appendix B presents UAFCB detail audit adjustments for the year ended 2018.

(b) Sewer Plant in Service

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

(c) Depreciation and Accumulated Depreciation of Sewer Plant

Depreciation was computed on a composite depreciation rate of 3.27% in order to depreciate all plant assets for ratemaking purposes and reporting the depreciation expense in CWWC's Annual Reports filed with the Commission. The Commission's Standard Practice (SP) U-04-SM, Paragraph 22, specifies that the annual composite depreciation rate should normally fall within the range of 2.0% to 3.5%.

(d) Proprietary Capital

UAFCB could not attest to the accuracy of the Proprietary Capital balance due to the lack of historical information. Expressing an opinion on the Proprietary Capital balance as of December 31, 2018, would require auditing the Proprietary Capital from the inception of the company. Due to the limitations of our audit scope, we cannot and do not express an opinion on the Proprietary Capital balance as of December 31, 2018.

Total investment of \$400,000 was transferred from the owner to CWWC and then allocated to the water and sewer utilities for the year ended 2018. The Water utility was allotted \$243,488 and the Sewer utility was allotted \$156,512 of the total \$400,000. CWWC does not have an official allocation methodology for the additional investments that it receives; funds are allocated based on the needs of the utilities at that time. CWWC's Annual Report reflected an operating loss of \$211,413 from its sewer operations for the year ended December 31, 2018.

(e) Contributions in Aid of Construction (CIAC) and Accumulated Depreciation of CIAC

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.

(f) Revenue

CWWC primarily obtained its sewer revenue from unmetered revenue services based on tariffs approved by the Commission. CWWC billed its customers on a monthly flat-rate basis dependent on the size of the septic tank the customer has.

(g) Contract Work

Contract Work represents all repair and maintenance work that is not performed by the Sewer Company's employees. CWWC contracts all work relating to the continual operation of the utility to CLUS, which hires its own staff to run the operation. CWWC reported \$120,190 under Employee Labor, \$18,333 under Office Salaries, \$70,604 under Management Salaries, and \$9,918 under Professional Services as expenses; however, all individuals are considered employees of CLUS. Since those costs were contract expenses not incurred directly by CWWC's employees, UAFCB reclassified them to Contract Work expenses.

(2) Annual Reports

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

Appendix A

Summary of Net Financial Impact Resulting from UAFCB’s Audit Adjustments for Year 2018

The following is a summary of net financial impact resulting from UAFCB’s audit adjustments for Year 2018.

Audit Adj. No.	Annual Report				Description	For the Year 2018	
	Sch.	Line	Col.	Acct No.		Debit	Credit
<u>Net Financial Impact on Balance Sheets Items:</u>							
1	A	30	c	131	Cash	\$21,378	
2,8	A	39	c	180	Deferred Charges	2,372	
1,7	A	10	c	218	Proprietary Capital	3,669	
2	A	16	c	230	Payables to Affiliated Companies		\$3,558
<u>Net Financial Impact on Income Statements Items:</u>							
9	B-1	26	b	480	Other Sewer Revenue		\$3,459
3	B-2	9	b	630	Employee Labor		120,190
3, 4, 5,6	B-2	11	b	650	Contract Work	\$219,045	
4	B-2	18	b	670	Office Salaries		18,333
5	B-2	19	b	671	Management Salaries		70,604
10	B-2	23	b	681	Office Supplies and Expenses	6,334	
6	B-2	24	b	682	Professional Services		9,918
7,8,9	B-2	26	b	688	Regulatory Compliance Expense		20,402
10	B-2	27	b	689	General Expenses		6,334

Appendix B

Summary of Audit Adjustments for Year 2018

Audit Adj. No.	Annual Report				Description	For the Year 2018	
	Sch.	Line	Col.	Acct. No.		Debit	Credit
1	A	30	c	131	Cash	\$21,378	
	A	10	c	218	Proprietary Capital <i>To allocate a proportional Cash derived from both water and sewer operations that were entirely reported under the water operations to the sewer operations.</i>		\$21,378
2	A	39	c	180	Deferred Charges	\$3,558	
	A	16	c	230	Payables to Affiliated Companies <i>To record the portion of CPUC-approved Deferred Charges pertaining to CWWC's General Rate Case costs belonging to Sewer operations that was originally recorded in the water operations.</i>		\$3,558
3	B-2	11	b	650	Contract Work	\$120,190	
	B-2	9	b	630	Employee Labor <i>To reclassify Employee Labor provided by contracted services.</i>		\$120,190
4	B-2	11	b	650	Contract Work	\$18,333	
	B-2	18	b	670	Office Salaries <i>To reclassify Office Salaries provided by contracted services.</i>		\$18,333
5	B-2	11	b	650	Contract Work	\$70,604	
	B-2	19	b	671	Management Salaries <i>To reclassify Management Salaries provided by contracted services.</i>		\$70,604
6	B-2	11	b	650	Contract Work	\$9,918	
	B-2	24	b	682	Professional Services <i>To reclassify contracted repair and maintenance services to the proper account.</i>		\$9,918
7	A	10	c	218	Proprietary Capital	\$25,047	
	B-2	26	b	688	Regulatory Commission Expenses <i>To remove the reported incorrect Regulatory Commission Expense in Sewer CWWC's Annual Report.</i>		\$25,047

Appendix B (continued)

Summary of Audit Adjustments for Year 2018

Audit Adj. No.	Annual Report				Description	For the Year 2018	
	Sch.	Line	Col.	Acct. No.		Debit	Credit
8	B-2	26	b	688	Regulatory Commission Expense	\$1,186	
	A	39	c	180	Deferred Charges <i>To amortize CPUC-approved Deferred Charges pertaining to CWWC's General Rate Case costs for 2018.</i>		\$1,186
9	B-2	26	b	688	Regulatory Compliance Expense	\$3,459	
	B-1	26	b	480	Other Sewer Revenue <i>To include unrecorded CPUC User Fees collected from sewer customers to comply with CPUC accounting guidelines.</i>		\$3,459
10	B-2	23	b	681	Office Supplies and Expenses	\$6,334	
	B-2	27	b	689	General Expenses <i>To reclassify General Expenses to agree with the audited amount.</i>		\$6,334