



BALANCING ACCOUNTS PERFORMANCE AUDIT

Liberty Utilities (Park Water) Corp.

January 1, 2018, through December 31, 2018

Utility Audits, Risk and Compliance Division
Utility Audits Branch
October 5, 2021



MEMBERS OF THE TEAM

Angie Williams, Director

Masha Vorobyova, Assistant Director

Kevin Nakamura, Supervisor

Cory Carpenter, Lead

Amy Xu, Staff

Yosief Hailemichael, 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
400 R Street, Suite 221
Sacramento, CA 95811**

PUBLIC UTILITIES COMMISSION

505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298



Transmitted via e-mail

October 5, 2021

Mr. Edward Jackson, Director
Rates and Regulatory Affairs (West Region)
Liberty Utilities (Park Water) Corp.
9750 Washburn Road
Downey, CA 90241-7002

Dear Mr. Jackson:

**Final Report Transmittal Letter—Audit of Liberty Utilities' (Park Water) Corp.
Balancing Accounts for the period of January 1, 2018, through December 31, 2018**

The Utility Audits Branch (UAB) of the California Public Utilities Commission (CPUC) has completed its audit of Liberty Utilities' (Park Water) Corp. (LUPWC) Balancing Accounts reported for the period of January 1, 2018, through December 31, 2018. The final audit report is enclosed.

LUPWC's response to the draft report finding and our evaluation of the response are incorporated into this final report. We will post the final audit report on our website at [Audit Reports by Industry \(ca.gov\)](#).

A Corrective Action Plan addressing the finding and recommendations is required. LUPWC's response to the draft report included information on corrective actions implemented.

We appreciate LUPWC's assistance and cooperation during the engagement, and its willingness to implement corrective actions. If you have any questions regarding this report, please contact Kevin Nakamura, Program and Project Supervisor, at (916) 715-8940.

Sincerely,

Angie Williams

Angie Williams, Director
Utility Audits, Risk and Compliance Division

cc: See next page

Mr. Edward Jackson, Director
Rates and Regulatory Affairs (West Region)
Liberty Utilities (Park Water) Corp.
October 5, 2021
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cc: Rachel Peterson, Executive Director, CPUC
Saul Gomez, Deputy Executive Director, Office of the Commission, CPUC
Terence Shia, Director, Water Division, CPUC
Masha Vorobyova, Assistant Director, UAB, CPUC
Kevin Nakamura, Program and Project Supervisor, UAB, CPUC
Cory Carpenter, Senior Management Auditor, UAB, CPUC
Amy Xu, Associate Management Auditor, UAB, CPUC
Yosief Hailemichael, Associate Management Auditor, UAB, CPUC

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EXECUTIVE SUMMARY

The Utility Audits Branch (UAB) of the California Public Utilities Commission (CPUC) conducted a performance audit of the Balancing Accounts administered and reported by Liberty Utilities (Park Water) Corp. (LUPWC) for the audit period of January 1, 2018, through December 31, 2018.

Our audit objectives were to determine whether 1) transactions recorded in LUPWC's balancing accounts from January 1, 2018, through December 31, 2018, were for allowable purposes and supported by appropriate documentation; and 2) the balancing accounts were established and maintained as required by applicable Public Utilities (PU) Code sections, CPUC directives, orders, rules, regulations, and LUPWC's policies and procedures.

Based on our audit objectives, procedures performed, samples tested, and evidence gathered, we found an instance of noncompliance with the requirements for the audit period from January 1, 2018, through December 31, 2018. This instance is described in the Finding and Recommendations section of this audit report. The audit finding is as follows:

Finding: Understated Expenditures in Group Pension Expense Balancing Account

LUPWC understated its pension expenditures, including interest, in its Group Pension Expense Balancing Account (GPEBA) by a total of \$1,694,829. As a result, LUPWC's adjusted 2018 year-end balance should have been reported as an over-collection totaling \$832,596 as outlined in the table below:

Group Pension Expense Balancing Account (GPEBA)	(Over)/Under- Collected Balance
2018 year-end reported balance	(\$2,527,425)
Understated expenditures	1,694,829
Adjusted 2018 year-end balance	(\$832,596)

We issued a draft audit report on September 10, 2021. LUPWC's Director of Rates and Regulatory Affairs (West Region) responded by letter dated September 24, 2021, acknowledging the finding and recommendations and proposing edits to the language in the draft audit report to clarify the nature of the finding for consideration. LUPWC's comments are included in this final report as an attachment in Appendix A – Utility's Response to Draft Audit Report and our evaluation of the comments is included in Appendix B – UAB's Evaluation of Utility's Response.

AUDIT REPORT

Background

Balancing Accounts

The CPUC has a responsibility to authorize the rates that regulated utilities may charge their customers. Considering that the rates are derived from projected costs and projected consumption of service, the CPUC authorizes regulated utilities to establish balancing accounts to track the actual costs and the related revenues the utilities collect from ratepayers for specified activities. The primary purpose of a balancing account is to ensure that a utility recovers its CPUC-authorized revenue requirement from ratepayers for a given program or function, but not more or less.

Functionally, a balancing account tracks the difference between actual expenditures associated with the account, revenue authorized for recovery by the CPUC (authorized revenue requirement), and the actual revenues collected within customer rates to cover those specific expenditures. Applicable rules for a given balancing account are presented in the account's preliminary statement, which also includes description of the purpose of the account, the types of costs and/or revenues that are to be tracked in the account, and specific accounting procedures that the utility must follow to record transactions for the balancing account. Additionally, unless approved otherwise, a balancing account is required to accumulate monthly interest at a rate equal to one-twelfth of the most recent month's interest rate on three-month Commercial Paper published by the Federal Reserve.

Actual revenues collected by a utility in rates can be more or less than what CPUC had authorized to collect because rates are always forward-looking and based on forecasted sales. Thus, the balance in a balancing account can either be over- or under-collected. If a balancing account is over- or under-collected, the net balance is typically recovered from or refunded to ratepayers on an annual basis through an adjustment in rates.

In 2018, LUPWC was authorized a total of nine balancing accounts to track differences between actual expenditures associated with the account and authorized for recovery, and the revenues collected within customer rates to cover those specific expenses. In 2018, LUPWC reported a total combined under-collected balanced of \$3.37 million in its balancing accounts. A breakdown of the amounts over or under-collected in rates as of December 31, 2018, by each balancing account is provided in the table below:

Title of Account	Net (Over)/Under- Collected Balance as of Dec. 31, 2018
2015 Water Revenue Adjustment Mechanism/Modified Cost Balancing Account (WRAM/MCBA)	\$ 51,635
2016 WRAM/MCBA	2,751,520
2017 WRAM/MCBA	3,750,263
2018 WRAM/MCBA	1,265,229
2011 Recycled Water-Incremental Cost Balancing Account	985
California Alternative Rates for Water (CARW) Revenue Reallocation Balancing Account	(1,607,153)
Conservation Expense One-Way Balancing Account (CEOWBA)	(334,574)
Consolidated Expense Balancing Account (CEBA)	19,093
Group Pension Expense Balancing Account (GPEBA)	(2,527,425) ¹
Total Net (Over)/Under-Collected Balance	<u>\$3,369,573</u>

Audit Authority

The UAB conducted this audit under the general authority outlined in PU Code sections 314.5, 314.6, 451, 581, 582, 584. Furthermore, PU Code section 792.5 requires the CPUC to review or audit all balancing accounts periodically to ensure that the transactions recorded in the balancing accounts are for allowable purposes and supported by appropriate documentation.

Objective and Scope

Our audit objectives were to determine whether 1) transactions recorded in LUPWC's balancing accounts from January 1, 2018, through December 31, 2018, were for allowable purposes and supported by appropriate documentation; and 2) the balancing accounts were established and maintained as required by applicable PU Code sections, CPUC directives, orders, rules, regulations, and the LUPWC's policies and procedures.

The scope of our audit covered the nine balancing accounts administered and reported by LUPWC for the audit period of January 1, 2018, through December 31, 2018.

Methodology

In planning our audit, we gained an understanding of each balancing account and LUPWC's operations by researching and reviewing relevant PU Code sections, preliminary statements, LUPWC's internal rules, regulations, and policies, CPUC decisions, resolutions, advice letters, and interviewing LUPWC personnel.

We conducted a risk assessment, including evaluating whether LUPWC's key internal controls relevant to our audit objectives were properly designed, implemented, and operating effectively. Our

¹ LUPWC incorrectly reported this amount. Refer to the Finding and Recommendations section of this report for additional details.

assessment included conducting interviews, observing processes, performing walkthroughs, and testing transactions. Deficiencies in internal control that were identified during our audit and determined to be significant within the context of our audit objectives are included in this report.

Additionally, we assessed the reliability of the data extracted from LUPWC's accounting and customer billings systems. Our assessment included examining extracted reports, tracing data between differing report formats to verify completeness, and tracing report data to source documents. We determined the data to be sufficiently reliable to address the audit objectives.

Based on the results of our planning, we developed specific methods for gathering evidence to obtain reasonable assurance to address the audit objectives. To achieve our audit objectives, we:

- Reviewed LUPWC's accounting system, accounting policies, processes and procedures for tracking, monitoring, and recording transactions to its balancing accounts.
- Reviewed LUPWC's customer billing system and policies, processes and procedures for recording and reporting revenues to its balancing accounts.
- Reviewed applicable CPUC decisions, advice letters, proceedings, and preliminary statements to ensure accounts and tariff rates were established and maintained in accordance with CPUC directives.
- Reviewed LUPWC's internal control policies and procedures related to the administration and implementation of its balancing accounts.
- Assessed significance by performing analysis of revenue and expenditure data and evaluating balancing account requirements.
- Reconciled year-end balances recorded in the Balancing Account Monthly Tracking Statements to LUPWC's general ledger and Semi-Annual report filed with the CPUC's Water Division.
- Reviewed external audit reports prepared by independent Certified Public Accounting (CPA) firm on LUPWC's annual financial statements and internal controls to identify potential risks relevant to the audit objectives.
- Obtained an understanding of LUPWC's key internal controls relevant to its balancing accounts, such as accounting and reporting process, customer billing procedures, rate adjustment process, and assessed the design, implementation, and operating effectiveness of selected controls that were significant to the audit objectives by:
 - interviewing key personnel and completing an internal control questionnaire;
 - reviewing LUPWC's policies and procedures and interviewing key personnel;
 - performing walkthroughs of selected customer billings and transactions;
 - verifying appropriate rates were charged on selected customer billings; and

- assessing reliability of recorded and reported revenue and expenditure data.
- Conducted a risk assessment to determine the nature, timing, and extent of substantive testing.
- Performed testing of revenues by judgmentally selecting a non-statistical sample of customer bills and transactions for the months of March, August, and December 2018 to verify that:
 - customer billing rates complied with the CPUC directives and approved tariffs;
 - billed revenues were recorded accurately in each respective balancing account; and
 - year-end over- or under-collected balances were properly and timely settled in rates.
- Determined whether LUPWC properly reported and recorded monthly interest in each Balancing Account Monthly Tracking Statement by recomputing the monthly interest amounts reported for each month in all nine balancing accounts.
- Performed testing of expenditures by judgmentally selecting a non-statistical sample of significant expenditure transactions for the following three out of nine balancing accounts:

Balancing Account Name	Total Expenditures Tested	Total Expenditures Recorded in 2018	Percent Tested
Modified Cost Balancing Account (MCBA)	\$665,648	\$7,362,096	9%
Conservation Expense One-Way Balancing Account (CEOWBA)	184,651	427,470	43%
Group Pension Expense Balancing Account (GPEBA)	210,773	843,093	25%
Totals	\$1,061,072	\$8,632,659	12%

For the selected samples, errors found, if any, were not projected to the intended (total) population.

- Traced sampled expenditures recorded in LUPWC’s accounting records to supporting documentation and determined whether transactions were accurate, allowable, supported by appropriate source documents, and maintained in compliance with applicable CPUC directives, orders, rules, regulations, and the LUPWC’s policies and procedures.

We did not audit LUPWC’s financial statements. We limited our audit scope to planning and performing audit procedures necessary to obtain reasonable assurance that LUPWC reported, incurred, and maintained its balancing accounts in accordance with the applicable criteria. We considered LUPWC’s internal controls only to the extent necessary to plan the audit and achieve our audit objectives.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our finding and conclusions based on our audit objectives.

Conclusion

Based on our audit objectives, procedures performed, samples tested, and evidence gathered, we found an instance of noncompliance with the requirements for the audit period of January 1, 2018, through December 31, 2018. This instance is described in the Finding and Recommendations section of this audit report.

Follow-up on Prior Audit Findings

We have not previously conducted an audit of the LUPWC's regulatory balancing accounts.

Views of Responsible Officials

We issued a draft audit report on September 10, 2021. LUPWC's Director of Rates and Regulatory Affairs (West Region) responded by letter dated September 24, 2021, acknowledging the finding and recommendations and proposing edits to the language in the draft audit report to clarify the nature of the finding for consideration. LUPWC's comments are included in this final report as an attachment in Appendix A – Utility's Response to Draft Audit Report and our evaluation of the comments is included in Appendix B – UAB's Evaluation of Utility's Response.

Restricted Use

This audit report is intended solely for the information and use of LUPWC and the CPUC; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of the final audit report, which is a matter of public record and will be available on the CPUC website at [Audit Reports by Industry \(ca.gov\)](https://www.cpuc.ca.gov/Audit-Reports-by-Industry).

Angie Williams

Angie Williams, Director
Utility Audits, Risk and Compliance Division

FINDING AND RECOMMENDATIONS

Finding: Understated Expenditures in Group Pension Expense Balancing Account

Condition:

LUPWC understated its pension expenditures, including interest, in its GPEBA totaling \$1,694,829. The discrepancy occurred due to an actuarial error. During the planning phase of the audit, LUPWC disclosed that its independent actuarial firm failed to provide the amortization of actuarial gains and losses of Park Water's pension plan that occurred prior to its acquisition by Liberty Utilities in January 2016. During the process of closing its financial statements for the year ending December 31, 2019, LUPWC discovered these prior discrepancies while comparing the pension expenses recorded in its general ledger to the pre- and post-acquisition reports provided by its independent actuarial firm. The understated pension expenditures caused LUPWC's 2018 year-end balance in its GPEBA to be overstated.

The purpose of the GPEBA is to track the difference between group pension expenses authorized in rates and actual pension expenses incurred. Due to understated expenditures, the reported year-end 2018 over-collected balance in its GPEBA of \$2,527,425 was overstated and should be reflected as an adjusted over-collected balance of \$832,596 as outlined in the table below:

Group Pension Expense Balancing Account (GPEBA)	(Over)/Under- Collected Balance
2018 year-end reported balance	(\$2,527,425)
Overstated amount	1,694,829
Adjusted 2018 year-end balance	<u><u>(\$832,596)</u></u>

Criteria:

PU Code sections 581, 582, and 584 require that the utility provide timely, complete, and accurate data to the CPUC.

PU Code section 587 requires water corporations to annually submit a report that describes all significant transactions as specified by the CPUC.

Pursuant to D.16-01-009, the CPUC authorized LUPWC to establish the GPEBA to track the difference between adopted and actual pension expenses.

General Order (GO) 104-A mandates that each utility filed an annual report of its operations in such form and content as prescribed by the CPUC.

Cause:

During the audit period, LUPWC lacked monitoring and oversight policies and procedures to timely prevent and detect errors and to ensure expenditure amounts are accurately and timely recorded and reported in its GPEBA.

Effect:

It is imperative for each utility to ensure that its over or under-collected balances in its balancing accounts are accurate, complete, and in compliance with applicable laws, rules, regulations, directives, etc., to ensure ratepayers do not pay any more or less in rates than necessary.

Recommendations:

LUPWC should request CPUC authorization in its Test Year 2022 general rate case (GRC) application to recover the adjusted balance recorded in its GPEBA. LUPWC should also develop and implement monitoring and oversight policies and procedures to facilitate prevention and timely detection of errors and to ensure expenditures are accurately and timely recorded and reported to each balancing account in accordance with all applicable guidelines and directives.

APPENDIX A—UTILITY'S RESPONSE TO DRAFT AUDIT REPORT



Liberty Utilities (Park Water) Corp.
9750 Washburn Road
Downey, CA 90241-7002
Tel: 562-923-0711
Fax: 562-861-5902

Transmitted via e-mail

September 24, 2021

Angie Williams, Director
California Public Utilities Commission
Utility Audits, Risk and Compliance Division
400 R Street, Suite 221
Sacramento, CA 95811

Re: Liberty Utilities (Park Water) Corp. Response to the Draft Audit Report for Liberty Utilities (Park Water) Corp. Balancing Accounts for the audit period of January 1, 2018, through December 31, 2018

Dear Director Williams:

Liberty Utilities (Park Water) Corp. (Liberty) hereby submits its review of the Draft Report issued on September 10, 2021 by the Utility Audits Branch (UAB) of the California Public Utilities Commission (CPUC) regarding the Balancing Accounts Performance Audit for the Period of January 1, 2018 through December 31, 2018 (Draft Report).

Liberty appreciates the UAB's review and ongoing engagement throughout the audit process. Liberty has implemented measures consistent with the UAB's recommendation but requests edits to the language in the Draft Report to clarify the nature of the finding (as illustrated in redline and strikethrough below).

Liberty provides its requested edits to the UAB's executive summary, conclusion, cause and recommendation:

Liberty
Response to UAB Draft Audit Report

September 24, 2021
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Executive Summary

Based on our audit objectives, procedures performed, samples tested, and evidence gathered, we found an instance of ~~noncompliance~~ **an error and misstatement of the balance recorded in the Group Pension Expense Balancing Account consistent** with the requirements for the audit period from January 1, 2018, through December 31, 2018. This instance is described in the Finding and Recommendations section of this audit report.

Conclusion

Based on our audit objectives, procedures performed, samples tested, and evidence gathered, we found an instance of ~~noncompliance~~ **an error and misstatement of the balance recorded in the Group Pension Expense Balancing Account consistent** with the requirements for the audit period of January 1, 2018, through December 31, 2018. The instance is described in the Finding and Recommendations section of this audit report.

Finding: Understated Expenditures in Group Pension Expense Balancing Account

Cause:

During the audit period, LUPWC lacked monitoring and oversight policies and procedures to timely prevent and detect errors and to ensure expenditure amounts are accurately and timely recorded and reported in its GPEBA. **LUPWC subsequently implemented pension training to all Finance and Accounting employees. The recorded sessions are available on demand for new employees or as refresher training for existing employees.**

Recommendations:

LUPWC should request CPUC authorization in its Test Year 2022 general rate case (GRC) application to recover the adjusted balance recorded in its GPEBA. **Liberty requested CPUC authorization for recovery of the adjusted balance recorded in the GPEBA in its current general rate case (GRC) application. The adjusted GPEBA is currently under review by the CPUC in LUPWC's Test Year 2022 GRC application (A.21-07-004) filed on July 2, 2021.** LUPWC should also develop and implement monitoring and oversight policies and procedures to facilitate for the prevention and timely detection of errors, and to ensure expenditures are accurately and timely recorded and reported to each balancing account in accordance with all applicable guidelines and directives. **LUPWC has developed and implemented monitoring and oversight policies and procedures for the prevention and timely detection of errors, accurate and timely recording to each balancing account in accordance with all applicable guidelines and directives.**

Liberty
Response to UAB Draft Audit Report

September 24, 2021
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Sincerely,

LIBERTY UTILITIES (PARK WATER) CORP.

/s/ Edward N. Jackson

Edward N. Jackson
Director, Rates and Regulatory Affairs (West Region)
Edward.Jackson@libertyutilities.com

cc:

Kevin Nakamura, UAB, Kevin.Nakamura@cpuc.ca.gov

Cory Carpenter, UAB, Cory.Carpenter@cpuc.ca.gov

Tiffany Thong, Liberty, Tiffany.Thong@libertyutilities.com

APPENDIX B—UAB'S EVALUATION OF UTILITY'S RESPONSE

We appreciate LUPWC's response and the suggested edits to the language in the draft audit report's Executive Summary, Conclusion, and Finding and Recommendations sections. We determined that LUPWC's suggested edits do not provide additional factual information to support any revisions. Therefore, they remain unchanged in this final audit report.

We also commend LUPWC for its efforts in the development and implementation of corrective actions noted in their response, namely requesting CPUC's authorization to recover the adjusted balance, as well as developing and implementing employee training and oversight policies and procedures to help prevent and timely detect future errors of this nature.