
**SENATE COMMITTEE ON ENERGY, UTILITIES AND
COMMUNICATIONS**

Senator Ben Hueso, Chair

2019 - 2020 Regular

Bill No:	AB 1072	Hearing Date:	7/2/2019
Author:	Patterson		
Version:	5/22/2019 As Amended		
Urgency:	No	Fiscal:	Yes
Consultant:	Nidia Bautista		

SUBJECT: Public Utilities Commission: audits and reviews

DIGEST: This bill modifies statute regarding the California Public Utilities Commission's (CPUC's) obligation to audit or review the books of the electric, gas, heat, telegraph, telephone and water corporations it regulates.

ANALYSIS:

Existing law:

- 1) Establishes the CPUC has regulatory authority over public utilities, including electrical, gas, heat, telegraph, telephone, and water corporations. (California Constitution, Article XII, §§3 and 4)
- 2) Requires the CPUC to inspect and audit the books and records of each electrical, gas, heat, telegraph, telephone, and water corporation for regulatory and tax purposes. Requires an inspection and audit to be done at least every three years if the utility has over 10,000 customers and at least every five years if the utility has 10,000 or fewer customers. Authorizes the CPUC to inspect and audit the books and records of those utilities in accordance with the CPUC-approved rate case cycle, if that cycle provides for a rate case no less frequently than once every five years. Provides that an audit conducted in connection with a rate proceeding is deemed to fulfill these requirements. (Public Utilities Code §314.5)
- 3) Authorizes the CPUC to conduct financial and performance audits of any entity or program created by any order, decision, motion, settlement, or other action of the CPUC and authorizes the CPUC to conduct additional follow-up work that is related to any findings and recommendations related to the audit. Requires that the audit be completed in a timely manner consistent with the Generally Accepted Government Auditing Standards. (Public Utilities Code §314.6)

This bill:

- 1) Modifies statute regarding the CPUC's obligation to audit the books of the electric, gas, heat, telegraph, telephone and water corporations it regulates, specifically:
 - a) Mandates the CPUC to audit of electric, gas, heat, telegraph, telephone and water corporations serving over 10,000 customers every three years or in accordance with a CPUC case rate with no less frequency than five years.
 - b) Mandates a review or audit of electric, gas, heat, telegraph, telephone and water corporations it regulates serving 10,000 or fewer customers every three years or in accordance with a CPUC case rate with no less frequency than five years.
 - c) Requires the CPUC to complete any review or audit of a utility in a timely manner and consistent with applicable auditing standards.
 - d) Effective January 15, 2020, and annually thereafter, requires the CPUC to post on its internet website its standard practice audit manual, titled "Utility Audit, Finance and Compliance Branch (UAFCB) Audit and Attestation Standard Practice," and any updates to that manual.

Background

CPUC auditing. The CPUC regulates privately owned electric, natural gas, telecommunications, water, railroad, rail transit, and passenger transportation companies, and other utilities in the State. The CPUC's UAFCB provides auditing services to three utility industries under CPUC regulatory authority: telecommunications, energy, and water. Unlike other units at the CPUC conducting audits (Internal Audits) and evaluating internal controls and operations (Enterprise Risk and Compliance Office), UAFCB conducts external financial and compliance audits of the utilities for regulatory purposes. Audits must be conducted in accordance with requirements in the Public Utilities Code, by formal order of the CPUC or by management request. The Branch is comprised of a Director, four Supervisors and 22 auditors.

CPUC and water utilities. As a part of its oversight of water companies, the CPUC regulates 98 privately owned water companies (water utilities), which serve about 14 percent of California's residents. As with other rate-regulated utilities, state law requires the CPUC to verify that a water utility's proposed rates are just and reasonable before it permits the utility to change its rates. The CPUC performs

this verification through a utility's general rate case and by reviewing any additional requests for tariff changes, including through review of advice letters proposed by utilities to implement changes to their rates and operations.

The classes of water utilities are differentiated into four classes based on the number of service connections:

- There are nine water utilities with Class A (more than 10,000 connection);
- There are five water utilities with Class B (between 2,000 & 10,000 connections);
- There are twenty-two water utilities with Class C (between 500 & 200 connections); and,
- There are sixty-two water utilities with Class D (fewer than 500 connections)

State Auditor's report. In December 2018, the State Auditor issued a report (2018-118) of the CPUC Water Division regarding the granting of rate increases for water utilities and found, the CPUC failed to meet statutory requirements to audit the Large Class A and small water utilities. The State Auditor indicated that for Class A utilities, serving private water utility customers with approximately 1.5 million service connections, the CPUC failed to audit and was relying on the Office of the Public Advocates (formerly the Office of Ratepayer Advocates), an independent office within the CPUC, to conduct its reviews during the course of the general rate cases to comply with the law. The current audit also included the finding that the CPUC failed to complete most of the audits of the small utilities in the five-year time frames established by law. The State Auditor reported, "We found that the CPUC completed only 20 of the approximately 75 required audits of small water utilities for the five-year period of fiscal years 2013-14 through 2017-18. The CPUC agreed with the State Auditor's findings and stated it's "UAFCB is currently developing policies and procedures and revamping its audit program to ensure it addresses both compliance and financial accountability issues with the water utilities." The CPUC also cited the need for additional auditor positions focused on small water utilities.

Comments

AB 1072. This bill was introduced in response to the State Auditor's 2018 report. Among the State Auditor's finding was that the CPUC was not conducting audits as frequently as required, and there was concern expressed that some of the audits that were conducted did not fulfill the intent of the law.

CPUC audits. The CPUC's UAFCB has the authority to be used by the CPUC to conduct audits, reviews and/or attestation examinations of matters concerning regulated utilities of the CPUC. In conducting these functions the UAFCB adheres

to auditing standards and guidelines from various sources including, but not limited to, the following: 1) Professional Standards of American Institute of Certified Public Accountants; 2) Generally Accepted Auditing Standards, (A Comprehensive Restatement of Standards for Auditing, Attestation Compilation, and Review by Miller); 3) Generally Accepted Accounting Principles; and 4) AICPA Statements on Standards for Attestation Engagements. The CPUC's UAFCB maintains a document entitled, Utility Audit, Finance and Compliance Branch UAFCB Audit and Attestation Standard Practice (UAASP), which was last updated in December 2013. The document provides the applicable auditing, attestation standards and procedures that UAASP applies during their engagement with a water utility. The UAFCB staff is told to apply the requirements contained in the UAASP when conducting water utility financial audits, financial statements audits (collectively referred to as audits) and attestation engagements. However, the UAASP practice manual is neither regularly updated nor publically available. Mandating that the report is published annually and available on the CPUC's website, will keep standards current and the water districts apprised of applicable standards, updates and additional important information.

Updated audit procedures for Class A water utilities. In response to the State Auditor's report, the CPUC has proposed updated audit policies and procedures as an alternative to audits of Class A water utilities. Among the updates, the CPUC will require each Class A water utility to contract an independent Certified Public Accountant (CPA) to conduct an audit of the utility and have the audit and other specified financial documents filed with the CPUC. The CPUC auditing branch would then review the audit and financial documents, determine whether additional information is necessary, and post the final review and corresponding documents on the CPUC's website. The CPUC has proposed this approach as an alternative to conducting audits of the Class A water utilities in an effort to reduce costs to ratepayers while still providing the benefits of the financial audit.

Prior/Related Legislation

SB 1410 (Morrell, Chapter 361, Statutes of 2018) required the threshold number of customers served by CPUC regulated utility that would be subject to more frequent audit requirements from over 1,000 to over 10,000 customers served.

AB 2168 (Williams, Chapter 805, Statutes of 2016) required the CPUC to periodically review balancing accounts of utilities based on a risk-based approach to ensure transactions are for allowable purposes.

FISCAL EFFECT: Appropriation: No Fiscal Com.: Yes Local: No

SUPPORT:

California Water Association (Sponsor)

OPPOSITION:

None received

ARGUMENTS IN SUPPORT: According to the author:

AB 1072 is needed to provide clarity to small water and telephone providers about the timeline and standards under which the CPUC must complete an audit or review of their utility. This has been an issue for the small regulated water systems in my district and statewide. The bill is needed to ensure that the CPUC can comply with the auditing standards outlined in statute in a timely and transparent manner.

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