

CALIFORNIA WATER SERVICE GROUP

Form 10-Q

August 06, 2010

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q**

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended **June 30, 2010**

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number 1-13883

CALIFORNIA WATER SERVICE GROUP

(Exact name of registrant as specified in its charter)

Delaware

77-0448994

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer identification No.)

1720 North First Street, San Jose, CA.

95112

(Address of principal executive offices)

(Zip Code)

408-367-8200

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in rule 12b-2 of the Exchange Act) Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. Common shares outstanding as of July 31, 2010 20,802,361

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PART I FINANCIAL INFORMATION

Item 1.

FINANCIAL STATEMENTS

The condensed consolidated financial statements presented in this filing on Form 10-Q have been prepared by management and are unaudited.

**CALIFORNIA WATER SERVICE GROUP
CONDENSED CONSOLIDATED BALANCE SHEETS**

Unaudited

(In thousands, except per share data)

	June 30, 2010	December 31, 2009
ASSETS		
Utility plant:		
Utility plant	\$ 1,786,888	\$ 1,709,062
Less accumulated depreciation and amortization	(533,424)	(510,985)
Net utility plant	1,253,464	1,198,077
Current assets:		
Cash and cash equivalents	5,646	9,866
Receivables:		
Customers	27,031	25,567
Regulatory balancing accounts	8,219	10,513
Other	6,036	9,043
Unbilled revenue	19,350	13,417
Materials and supplies at average cost	5,702	5,530
Taxes, prepaid expenses and other assets	19,654	18,305
Total current assets	91,638	92,241
Other assets:		
Regulatory assets	220,621	204,104
Goodwill	2,615	2,615
Other assets	32,094	28,544
Total other assets	255,330	235,263
	\$ 1,600,432	\$ 1,525,581
CAPITALIZATION AND LIABILITIES		
Capitalization:		
Common stock, \$.01 par value	\$ 208	\$ 208
Additional paid-in capital	216,063	215,528
Retained earnings	204,930	204,898
Total common stockholders' equity	421,201	420,634
Long-term debt, less current maturities	380,017	374,269

Total capitalization	801,218	794,903
Current liabilities:		
Current maturities of long-term debt	2,923	12,953
Short-term borrowings	55,150	12,000
Accounts payable	48,830	43,689
Regulatory balancing accounts	903	2,430
Accrued interest	4,033	4,258
Accrued expenses and other liabilities	33,905	35,028
Total current liabilities	145,744	110,358
Unamortized investment tax credits	2,318	2,318
Deferred income taxes, net	94,463	91,851
Pension and postretirement benefits other than pensions	143,543	137,127
Regulatory and other liabilities	92,243	85,780
Advances for construction	188,015	185,027
Contributions in aid of construction	132,888	118,217
	\$ 1,600,432	\$ 1,525,581

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements

Table of Contents**CALIFORNIA WATER SERVICE GROUP
CONDENSED CONSOLIDATED STATEMENTS OF INCOME**

Unaudited

(In thousands, except per share data)

	June 30, 2010	June 30, 2009
For the three months ended		
Operating revenue	\$ 118,321	\$ 116,667
Operating expenses:		
Operations:		
Water production costs	41,834	41,702
Administrative and general	18,480	19,386
Other operations	14,749	14,330
Maintenance	5,158	4,312
Depreciation and amortization	10,638	10,282
Income taxes	7,091	6,789
Property and other taxes	4,087	3,911
Total operating expenses	102,037	100,712
Net operating income	16,284	15,955
Other income and expenses:		
Non-regulated revenue	3,692	3,098
Non-regulated expenses, net	(3,691)	(721)
Gain on sale of non-utility property		72
Income taxes expense on other income and expenses		(992)
Net other income and expenses	1	1,457
Interest expense:		
Interest expense	6,939	5,962
Less: capitalized interest	(1,035)	(640)
Net interest expense	5,904	5,322
Net income	\$ 10,381	\$ 12,090
Earnings per share		
Basic	\$ 0.50	\$ 0.58

Diluted	\$ 0.50	\$ 0.58
Weighted average shares outstanding		
Basic	20,803	20,745
Diluted	20,818	20,767
Dividends declared per share of common stock	\$ 0.2975	\$ 0.2950

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements

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CONDENSED CONSOLIDATED STATEMENTS OF INCOME**

Unaudited

(In thousands, except per share data)

For the six months ended	June 30, 2010	June 30, 2009
Operating revenue	\$ 208,593	\$ 203,280
Operating expenses:		
Operations:		
Water production costs	72,289	70,570
Administrative and general	35,924	38,247
Other operations	28,315	26,786
Maintenance	10,109	8,947
Depreciation and amortization	21,430	20,480
Income taxes	8,499	8,021
Property and other taxes	7,990	7,999
 Total operating expenses	 184,556	 181,050
 Net operating income	 24,037	 22,230
Other income and expenses:		
Non-regulated revenue	7,113	5,979
Non-regulated expenses, net	(7,237)	(3,362)
Gain on sale of non-utility property		675
Income taxes benefit (expense) on other income and expenses	60	(1,330)
 Net other (expense) income	 (64)	 1,962
Interest expense:		
Interest expense	13,428	11,000
Less: capitalized interest	(1,854)	(1,319)
 Net interest expense	 11,574	 9,681
 Net income	 \$ 12,399	 \$ 14,511
 Earnings per share		
Basic	\$ 0.60	\$ 0.70

Diluted	\$ 0.60	\$ 0.70
Weighted average shares outstanding		
Basic	20,791	20,738
Diluted	20,806	20,763
Dividends declared per share of common stock	\$ 0.5950	\$ 0.5900

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

Unaudited

(In thousands)

	June 30, 2010	June 30, 2009
For the six months ended:		
Operating activities		
Net income	\$ 12,399	\$ 14,511
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	22,857	21,614
Gain on sale of non-utility property		(675)
Change in value of life insurance contracts	83	(1,827)
Other changes in noncurrent assets and liabilities	(1,008)	3,729
Changes in operating assets and liabilities:		
Receivables	(2,095)	(12,065)
Accounts payable	5,327	9,916
Other current assets	(1,509)	(5,018)
Other current liabilities	(1,347)	(143)
Other changes, net	(1,851)	518
Net adjustments	20,457	16,049
Net cash provided by operating activities	32,856	30,560
Investing activities:		
Utility plant expenditures	(60,458)	(52,930)
Purchase of life insurance	(1,706)	(1,613)
Proceeds on sale of non-utility property		750
Restricted cash (increase)	(13)	
Net cash used in investing activities	(62,177)	(53,793)
Financing activities:		
Short-term borrowings	43,150	20,000
Repayment of short-term borrowing		(48,000)
Advances and contributions in aid of construction	1,620	2,414
Refunds of advances for construction	(3,018)	(2,520)
Dividends paid	(12,367)	(12,233)
Proceeds from long-term debt, net of issuance cost	7,903	96,610
Repayment of long-term debt	(12,187)	(5,439)
Issuance of common stock		30
Net cash provided by financing activities	25,101	50,862
Change in cash and cash equivalents	(4,220)	27,629

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Cash and cash equivalents at beginning of period	9,866	13,869
Cash and cash equivalents at end of period	\$ 5,646	\$ 41,498

Supplemental information

Cash paid for interest (net of amounts capitalized)	\$ 11,316	\$ 8,553
Cash paid for income taxes	\$ 45	\$ 358

Supplemental disclosure of non-cash activities:

Accrued payables for investments in utility plant	\$ 8,755	\$ 7,623
Utility plant contribution by developers	\$ 23,239	\$ 7,584

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements

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CALIFORNIA WATER SERVICE GROUP
Notes to Unaudited Condensed Consolidated Financial Statements
June 30, 2010

(Amounts in thousands, except share and per share amounts)

Note 1. Organization and Operations and Basis of Presentation

California Water Service Group (the Company) is a holding company that provides water utility and other related services in California, Washington, New Mexico and Hawaii through its wholly-owned subsidiaries. California Water Service Company (Cal Water), Washington Water Service Company (Washington Water), New Mexico Water Service Company (New Mexico Water), and Hawaii Water Service Company, Inc. (Hawaii Water) provide regulated utility services under the rules and regulations of their respective state's regulatory commissions (jointly referred to herein as the Commissions). CWS Utility Services and HWS Utility Services LLC provide non-regulated water utility and utility-related services.

Basis of Presentation

The unaudited interim financial information has been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and in accordance with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X promulgated by the Securities and Exchange Commission (SEC) and therefore do not contain all of the information and footnotes required by GAAP and the SEC for annual financial statements. The condensed consolidated financial statements should be read in conjunction with the Company's consolidated financial statements for the year ended December 31, 2009, included in its annual report on Form 10-K as filed with the SEC on March 1, 2010.

The preparation of the Company's condensed consolidated financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the balance sheet dates and the reported amounts of revenues and expenses for the periods presented. Actual results could differ from these estimates.

In the opinion of management, the accompanying condensed consolidated financial statements reflect all adjustments that are necessary to provide a fair presentation of the results for the periods covered. The results for interim periods are not necessarily indicative of the results for any future period.

Due to the seasonal nature of the water business, the results for interim periods are not indicative of the results for a twelve-month period. Revenue and income are generally higher in the warm, summer months and lower in the cooler winter months.

The Company operates in one reportable segment providing water and related utility services.

The Company evaluated its operations through the time these financial statements were issued and determined there were no subsequent events requiring additional adjustments or disclosures as of the time these financial statements were issued.

Note 2. Summary of Significant Accounting Policies

Revenue

Revenue includes monthly cycle customer billings for regulated water and wastewater services at rates authorized by regulatory commissions and billings to certain non-regulated customers. Revenue from metered customers includes billings to customers based on monthly meter readings plus an estimate for water used between the customer's last meter reading and the end of the accounting period. Flat rate customers are billed in advance at the beginning of the service period. The revenue is prorated so that the portion of revenue applicable to the current accounting period is included in that period's revenue, with the balance recorded as unearned revenue on the balance sheet and recognized as revenue when earned in the subsequent accounting period. In addition, effective July 1, 2008 with the adoption of the Water Revenue Adjustment Mechanism (WRAM) and the Modified Cost Balancing Account (MCBA), Cal Water records the difference between what is billed to its regulated customers and that which is authorized by the California Public Utilities Commission (CPUC).

Under the WRAM, Cal Water records the adopted level of volumetric revenues as authorized by the CPUC for metered accounts (adopted volumetric revenues). In addition to volumetric-based revenues, the revenue requirements approved by the CPUC include

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service charges, flat rate charges, and other items that are not subject to the WRAM. The adopted volumetric revenue considers the seasonality of consumption of water based upon historical averages. The variance between adopted volumetric revenues and actual billed volumetric revenues for metered accounts is recorded as a component of revenue with an offsetting entry to a current or long-term asset or liability balancing account (tracked individually for each Cal Water district). The variance amount may be positive or negative and represents amounts that will be billed or refunded to customers in the future.

Under the MCBA, Cal Water tracks adopted expense levels for water production costs (purchased water, purchased power, and pump taxes), as established by the CPUC. Variances (which include the effects of changes in both rate and volume) between adopted and actual purchased water, purchased power, and pump tax expenses are recorded as a component of revenue, as the amount of such variances will be recovered from or refunded to the Company's customers at a later date. This is reflected with an offsetting entry to a current or long-term asset or liability regulatory balancing account (tracked individually for each Cal Water district).

The balances in the WRAM and MCBA assets and liabilities accounts fluctuate on a monthly basis depending upon the variance between adopted and actual results. The recovery or refund of the WRAM is netted against the MCBA over- or under-recovery for the corresponding district and is interest bearing at the current ninety day commercial paper rate. When the net amount for any district achieves a pre-determined level at the end of any calendar year (i.e., at least 2.5 percent over- or under-recovery of the approved revenue requirement), Cal Water will file with the CPUC to refund or collect the balance in the accounts. Account balances less than those levels may be refunded or collected in Cal Water's general rate case proceedings or aggregated with future calendar year balances for comparison with the recovery level. As of June 30, 2010 included in the net regulatory balancing accounts, current and long-term assets were \$8.2 million and \$20.6 million, respectively, and the net regulatory balancing accounts current and long-term liabilities were \$0.9 million and \$1.5 million, respectively. As of December 31, 2009, included in the net regulatory balancing accounts, current and long-term assets were \$10.5 million and \$5.1 million, respectively, and the net regulatory balancing accounts current and long-term liabilities were \$2.4 million and \$0.9 million, respectively.

Note 3. Stock-based Compensation

Long-Term Incentive Plan

The long-term incentive plan was replaced on April 27, 2005, by a stockholder-approved equity incentive plan. The Long-Term Incentive Plan allowed granting of nonqualified stock options, some of which are currently outstanding. There will be no future grants made. The Company had accounted for options using the intrinsic value method. Options were granted at an exercise price that was not less than the per share common stock market price on the date of grant. The options vested at a 25% rate on their anniversary date over their first four years and are exercisable over a ten-year period. At June 30, 2010, options are fully vested and exercisable at a weighted average price of \$25.50. No options were granted for the six-month periods ended June 30, 2010 and 2009.

Equity Incentive Plan

The Company's Equity Incentive Plan, which was approved by shareholders on April 27, 2005, is authorized to issue up to 1,000,000 shares of common stock. As of June 30, 2010 and 2009, the Company granted Restricted Stock Awards (RSAs) of 36,909 and 21,000 shares, respectively, of common stock both to officers and to directors of the Company. Employee options vest over forty-eight months, while director options vest at the end of twelve months. In the second quarters of 2010 and 2009, the shares were valued at \$35.48 and \$38.38 per share, respectively, based upon the fair market value of the Company's common stock on the date of grant.

During the first six months of 2009, the Company granted Stock Appreciation Rights (SARs) to officers of 71,500 shares, which vest ratably over forty-eight months and expire at the end of ten years. The Company did not grant any SARs in 2010.

The Company has recorded compensation costs for the RSAs and SARs in Operating Expense in the amount of \$0.5 million for both the six months ended June 30, 2010 and June 30, 2009.

Note 4. Earnings Per Share Calculations

The computations of basic and diluted earnings per share are noted below. Basic earnings per share are computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflect the potential dilution that could occur if securities or

other contracts were exercised or converted

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into common stock. RSAs are included in the common shares outstanding because the shares have all the same voting and dividend rights as issued and unrestricted common stock.

The SARs outstanding of 180,210 shares are anti-dilutive for the three and six months ended June 30, 2010 and 2009.

All options are dilutive and the dilutive effect is shown in the table below.

(In thousands, except per share data)

	Three Months Ended June 30	
	2010	2009
Net income available to common stockholders	\$ 10,381	\$ 12,090
Weighted average common shares, basic	20,803	20,745
Dilutive common stock options (treasury method)	15	22
Shares used for dilutive computation	20,818	20,767
Net income per share basic	\$ 0.50	\$ 0.58
Net income per share diluted	\$ 0.50	\$ 0.58

	Six Months Ended June 30	
	2010	2009
Net income available to common stockholders	\$ 12,399	\$ 14,511
Weighted average common shares, basic	20,791	20,738
Dilutive common stock options (treasury method)	15	25
Shares used for dilutive computation	20,806	20,763
Net income per share basic	\$ 0.60	\$ 0.70
Net income per share diluted	\$ 0.60	\$ 0.70

Note 5. Pension Plan and Other Postretirement Benefits

The Company provides a qualified, defined-benefit, non-contributory pension plan for substantially all employees.

The Company makes annual contributions to fund the amounts accrued for the qualified pension plan. The Company also maintains an unfunded, non-qualified, supplemental executive retirement plan. The costs of the plans are charged to expense or are capitalized in utility plant as appropriate.

The Company offers medical, dental, vision, and life insurance benefits for retirees and their spouses and dependents. Participants are required to pay a premium, which offsets a portion of the cost.

Cash payments by the Company related to pension plans and other postretirement benefits were \$6.6 million for the six months ended June 30, 2010. The estimated cash contribution to the pension plans for 2010 is \$23.5 million. The estimated contribution to the other benefits plan for 2010 is \$5.6 million.

The following table lists components of the pension plans and other postretirement benefits. The data listed under pension plan includes the qualified pension plan and the non-qualified supplemental executive retirement plan. The data listed under other benefits is for all other postretirement benefits.

Three Months Ended June 30**Six Months Ended June 30**

	Pension Plan		Other Benefits		Pension Plan		Other Benefits	
	2010	2009	2010	2009	2010	2009	2010	2009
Service cost	\$ 2,451	\$ 2,354	\$ 793	\$ 954	\$ 4,902	\$ 4,560	\$ 1,586	\$ 1,458
Interest cost	3,332	3,158	783	890	6,664	6,176	1,566	1,408
Expected return on plan assets	(2,051)	(1,871)	(279)	(208)	(4,102)	(3,578)	(558)	(393)
Recognized net initial APBO (1)	N/A	N/A	69	69	N/A	N/A	138	138
Amortization of prior service cost	1,649	1,533						